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CFA SINGAPORE INSIGHTS

By Lutfey Siddiqi

Designing the investment firm of the future

Firms need to assess their business on five fronts to find out if they are future-ready. **By Lutfey Siddiqi**

THE problem with the future is that it is not here yet. Virtually every aspect of our lives is in a state of flux. While change may have always been a constant, several factors come together to make this an industrial revolution of a fundamental kind.

Every profession is having to grapple with existential questions as well as questions of leadership. Investment management is no exception.

A recent survey by CFA Institute reveals a disconnect between employee and employer. For example, 53 per cent of individuals believe in the business case for enhanced diversity, but only 14 per cent believe that inclusion practices will be implemented fast enough. More than half (54 per cent) agree that they personally bring a sense of purpose and meaning to their work, but only 28 per cent believe this to be true for their firm overall; 26 per cent believe that their firm prioritises shareholders over clients, when only 15 per cent of their C-suite would agree with that.

So, how do you chart a course for the investment firm of the future? We start by unpacking the firm of the present into five dimensions and consider deliberate action to shape changes in each. Every firm must ask itself: What is our business model, operating model, people model, investment model and distribution model?

Business model

Over nearly two decades, rapid growth in globalisation and financialisation of economies created tailwinds for the investment industry. Firms would compete for share in a growing pie, topline growth would take precedence over costs and business models looked like identikits of each other. That is no longer the case: secular trends now demand greater cost control, greater precision and agility, and a greater degree of competitive differentiation.

Some of the headwind is driven by regulatory requirements, many of which are incomplete but all of which point towards more capital, more process and more formalised risk management.

On that backdrop, firms need to be explicit and granular about their competitive edge. Where and how do you wish to compete? What business are you happy to let go of? Crucially, will you stick to your knitting if a perceived competitor with a different business model generates higher returns for a quarter or two?

The investment firm of the future will focus on brand differentiation and the degree of professionalism in its operating culture.

Operating model

It's no use saying that a business model relies on customisation and agility when the operating infrastructure does not support it.

First, when it comes to IT tools, the choice between building in-house versus buying external products is now skewed much more towards the latter.

Second, data capture is as much about organisational habits as it is about aggregation technology. For example, are you disciplined about writing call reports? Is too much of your client information "hoarded" by the primary relationship manager? Professional decisions must be informed by a rich dashboard of real-time metrics around both product performance and distribution.

Third, client outreach will increasingly utilise behavioural analysis and predictive algorithms to generate Amazon-style recommendations: "People like you like products like this".

People model

Often in Asia, organisations can be too hierarchical with too much of a power distance between office holders. At the same time, there is a propensity for one-way broadcasts (often by e-mail announcements) as opposed to interactive engagement with members of staff. Information can be internally opaque and siloed. Furthermore, senior teams can be deficient in diversity – not only in terms of gender and ethnicity, but also in background and age.

The firm of the future must deliberately design for diversity. Diversity makes an organisation less brittle and more risk-resilient. It also allows for a 360-degree appraisal of opportunities. How we interact with and challenge each other, what actions we take to de-bias our decisions and how we react to failure define our culture which in turn determines our future-readiness.

If your business model claims to be client-centric, are your people empowered to deliver on that claim especially when there might be near-term tradeoffs? Do your approval processes allow for nimble decisions or do you have to "wait for HQ to respond" to minor issues?

Leaders have to contend with the duality of greater supervisory responsibility on the one hand and more diffused control on the other. The challenge is less like the territorial conquest of a military general and more like that of Ernest Shackleton, who led the crew of his ice-adrift ship Endurance for months without a single casualty.

Too often, regulation-driven changes are not communicated to clients until the 11th hour. Leaders need to engage openly to help contextualise change, especially when it might inconvenience them. Why not make your compliance training material publicly available online?

Investment model

An investment firm needs to have a distinct investment culture. Do you have a Chief Investment Office that can rise above the noise of day-to-day trading? Do you have systematic methodologies for building a portfolio matched to target outcomes? Are you disciplined about blending top-down and bottom-up analysis? Do you have a framework assessing suitability of private equity or hedge funds?

Investment models must also respond to a rapid mainstreaming of environmental, social and governance (ESG) concerns. It is no longer sufficient to just report on financial returns – investment firms are increasingly required to demonstrate stewardship around how they generated those returns and their wider impact.

Distribution model

When it comes to technology for client use, it is important to be clear about the objective. Is it purely a cost-cutting exercise or is it motivated by a desire to enhance the customer experience? Is it meant to empower or supplant the human interface? Can my relationship manager take instructions from me or will she have to call the same generic hotline? Both types of operating models are valid as long as they are consistent with the stated business model of the firm. Firms that fail to strike the right "people-automation mix" will disappoint both clients and staff.

The use of detailed personal intelligence about customers has been limited in the investment industry so far. There is ample scope for finer categorisation of customers and more relevant targeting with the help of analytics. Firms should systematically track client measures on trust, satisfaction, expectation and outcome through feedback loops – bearing in mind that feedback is a privilege not an entitlement.

These five dimensions offer an organising framework as investment firms make the messy journey from present to future. More than any other region, Asia offers a set of economic fundamentals, historical backdrop and policy regimes that should make that journey slightly easier.

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