

How scalable customization is driving change in the investment management industry

**Accenture Whitepaper in
cooperation with Tindeco**

We live in a world of nearly endless possibilities for customization – from streaming entertainment on-demand and 3D printing your own objects, to personalized medicine. As expectations for customization rise across many areas of life, clients will also increasingly expect customized solutions from their investment managers.

Interestingly enough, 80% of respondents to a recent Accenture survey¹ in the Asset Management space in North America indicated that “customization for the masses” will be important in 2025.

The demand for customized solutions will only rise as more relevant data on individuals becomes available, and more assets become tradable due to the rise of tokenization. That’s why successful investment managers need to focus more and more on providing their clients with customized investment solutions while keeping their costs under control: they have to make customization scalable.

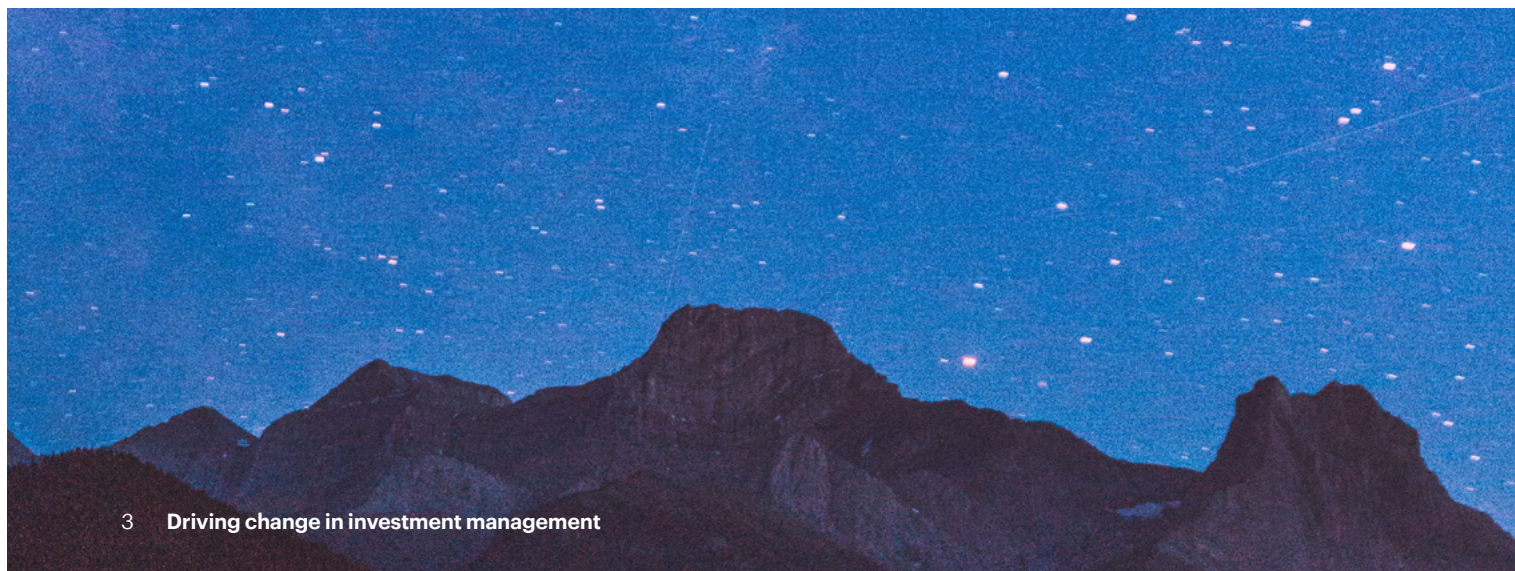
Today, technology has put this goal within the reach for investment managers. And as this trend gathers momentum, we expect the marginal cost of production of highly customized investment solutions to fall sharply towards zero. To succeed in this market, investment managers should be acting already today and start implementing the right technology and operating model.²

The Past

One of the most dominant features of the investment management industry in the past years has been the rise of passive indexing at the expense of active investing. Initially, passive investing was an approach for institutional investors, but its influence spread to private clients as the market for exchange-traded funds (ETFs) developed. Passive, market capitalization-based indexing should be optimal, according to economic theory: from modern portfolio theory to the capital asset pricing model and the efficient markets hypothesis, economists have developed a set of models in the second half of the last century which basically recommended investors to “buy the market portfolio and hold it.”

While these theories probably are too simplistic to capture much of what goes on in financial markets in reality, they were attractive due to their use of elegant mathematics, the simple advice they provided and perhaps most of all their ability to be computed. However, people often underappreciated the degree to which the assumptions underlying these models were driven by the limited computational power available when they were developed.

The technology capabilities of the past were largely limited: hardware couldn't be scaled, and software was monolithic in nature. Back then, poor scalability meant that dedicated hardware had to be purchased and maintained online to meet peak demand. This restricted the number of portfolios which could be modelled and assured that computationally intensive analytics were avoided wherever possible. Monolithic software supported monolithic investment processes, leaving armies of portfolio managers and quants to work outside of the main platforms using purpose-agnostic modelling tools like Excel.



The Present

Today, clients increasingly expect investment solutions which reflect their macroeconomic views, moral values, and specific financial requirements. This is true for both private and institutional investors. Different motivations could stem from complex regulatory requirements, the desire to invest according to environmental, social and governance (ESG) criteria, strongly held views on financial markets or the need to adapt to existing (and evolving) investment exposures and liabilities.³

An investor's requirements may be based on the attributes of single assets or groups thereof (including the entire portfolio). Some people might want to ensure that any automotive sector exposure is in specific brands, while others could want to prevent such exposure.

A growing number of clients have detailed preferences that may differ from sector to sector and country to country. Catering to all these needs and desires is costly today and therefore usually unavailable to anyone except for the largest clients of a firm.

Yet, customization will lead to more satisfied clients. Client satisfaction – in return – is a key driver of the share of wallet and the stickiness of a client. Furthermore, customization may be easier to explain and deliver to clients than reliable investment outperformance. Hence, it is not surprising that early adopters are already responding today to the opportunity by piloting systematic investment processes and new technologies designed to deliver scalable customization.



The Future

In the following sections we propose how the future of investment management may evolve from three different perspectives: investment management solutions, technology and industry structure.

Investment Management Solutions

The world of investment management is set to change markedly. The recognition that clients want different investment solutions and that the industry can economically deliver them is growing.

Successful solutions will however go further than taking into account client values such as ESG criteria by scoring assets and portfolios or using blacklists and whitelists. Investment managers need also to be able to provide dynamic, systematic, holistic and goal-based investment solutions. Those are mostly complex solutions which require managers to consider a client's liabilities and specific expenditure goals and manage their assets dynamically to reach the clients' goals.

Early adopters are already changing how they engage with clients by providing hybrid solutions which combine elements of discretionary management with advice. Such solutions require a coordinated yet partially independent investment decision process.

The client is still able to choose exactly which functions or tasks they want to delegate to the investment manager and which decisions will be reserved for themselves. Clients will also be able to more granularly define how a manager performs tasks over which he has discretion such as rebalancing portfolios during market crashes.

A common theme among both private and institutional clients is the desire to avoid large drawdowns. Yet, others may have strong preference for managers to "buy the dips." Such preferences imply that a different approach to rebalancing portfolios also needs to be applied to provide an appropriate investment solution. Rules-based investing, supported by the proper investment technology, gives investment managers the ability to deliver such highly customized investment solutions economically.

Special Focus: Rules-Based Investing

Rules-based investment management means different things to different people. Some may regard rules-based investment management simply as quantitative investment strategies. Others would consider rules-based investment management as a benchmark for their investment strategies from which deviation may be allowed.

Passive investing, for example, is by definition rules-based investing. It is dynamic in nature, but only in a relative simple sense. The rule is to track a benchmark which is itself generally rebalanced on a regular basis, according to rules of the index provider.

We define rules-based investment management to be investment management where systematic investment decisions are defined as investment rules. The rules determine or suggest the actions to be taken by the investment manager based upon the inputs to the rules (which are constantly evolving). These rules are then encoded as algorithms and implemented in software, designed to support rules-based investment.

By defining rules-based investment programs, the new world of investment management will extend into systematic investing to provide more value to clients. The focus on diversification could give way to a focus customization, meaning investment managers will increasingly seek to tailor the risks to which they expose clients based upon their specific requirements. They will also seek to implement virtually all systematic workflows on an automated basis. As a consequence, the investors should see a true value-add in the strategies applied and executed.

Investment Technology

Providing scalable customization requires different investment technology. It depends upon scalable investment management platforms that are based on flexible technology which can support computationally intensive problem solving. Fortunately, recent advancements in the cloud space are bringing such solutions within reach. We believe two key developments form the basis which will support this more advanced investment technology:

- Cloud based micro-service design that is suitable for modelling the many granular steps of an investment process – each of which needs to be customized.
- Elastic computing power that is necessary to support the simulation and optimization engines which in turn are required to design, test, and optimally combine investment rules and to actively manage large numbers of customized portfolios on an ongoing basis.

Rather than supporting the automation of a limited set of systematic investment processes, a customization platform needs to be designed to support virtually any rules-based investment process and also allow investment managers to retain the flexibility to incorporate insight-based investment decisions in a structured manner.

An optimal portfolio of rules would be a complete set of instructions for how a manager would behave at any point in time, contingent upon the state of the world which prevails. Such basic rules-based automation—combined with mid- and back-office digitalization such as machine learning and distributed ledger technology (DLT)—, will change the economics of investment management to such a degree that the total cost of production could reach low single-digit basis points for any customized portfolio in liquid, publicly traded assets.



Investment Industry

The firms able to deliver customized portfolios at scale are likely to prosper. The result might be a shift in the industry away from prioritizing active performance, especially in the liquid asset classes, continuing the trend exemplified in the move towards passive investing.

As the technologies and processes that support scalable customization are deployed, we would expect the industry to (re-)organize more around functional needs rather than around normative client types. Today, asset managers, wealth managers and digital platforms are usually focused on institutional, private and retail clients respectively.

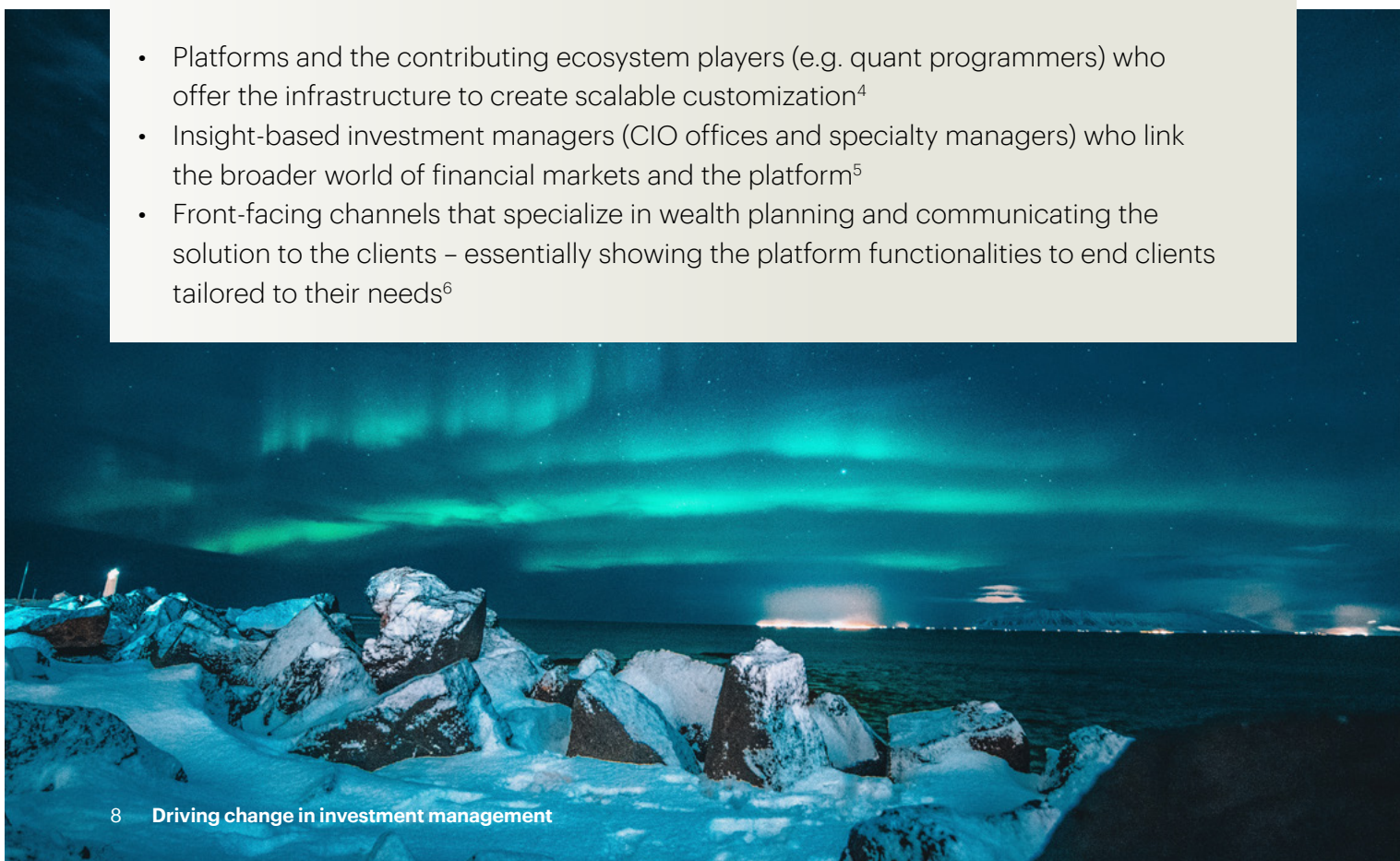
These changes will not happen overnight. Hence, the dynamics matter. We believe that early movers will likely be more those mid-sized asset managers that don't have

significant legacy systems. They may be able to scale more rapidly in the near to medium term while adapting their target operating models to the new realities that will be emerging. Eventually, they may even be able to manage hundreds of billions of dollars with only a handful of staff.

Firms with multiple non-modular legacy systems might struggle. They would have to develop, test, and deploy new technologies and operating models which might also cannibalize some parts of their old business. Their transformation process would require a shareholder base that can understand the narrative and is not reluctant to make the necessary investments today to likely be among the leaders of tomorrow. For those players the coming decade could be one of acquisitions and investments in disruptive models, as they drive their change journey.

In the future, we expect the following segments to emerge:

- Platforms and the contributing ecosystem players (e.g. quant programmers) who offer the infrastructure to create scalable customization⁴
- Insight-based investment managers (CIO offices and specialty managers) who link the broader world of financial markets and the platform⁵
- Front-facing channels that specialize in wealth planning and communicating the solution to the clients – essentially showing the platform functionalities to end clients tailored to their needs⁶



Regardless of the size of any business, some of key questions to ask yourself when thinking about scalable customizations are the following

“ Are you able to offer customized investment solutions to your clients today?

Do you expect your clients to increasingly demand customized investment solutions?

Does your technology support you in delivering scalable customization?

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References

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About Tindeco

Tindeco is a leading WealthTech company and offers the Tindeco VISION technology platform. VISION supports asset and wealth managers in the implementation of highly scalable operating models to enable them to efficiently deliver customised investment solutions. Managers can use VISION to design, test and implement rules-based investment portfolios – automating the systematic elements of their investment process. The award-winning VISION platform is a fully integrated solution based on a cloud microservices design for maximum flexibility and scalability. Tindeco is based in Zug, Switzerland with a development hub in Edinburgh, Scotland.

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