



**OPERATIONAL
PERFORMANCE OF BROKERS**

**Market Survey
Asia Securities
2004**

Summary of Findings

Version 1.0

**Z/Yen Limited
5-7 St. Helen's Place
London EC3A 6AU
UK**

**(44-20) 7562-9562 (telephone)
(44-20) 7628-5751 (facsimile)
hub@zyen.com (email)
www.zyen.com (web)**

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1. Introduction

1.1 Scope of Study

This document is the report of the Operational Performance of Brokers - Market Survey - Asian Securities 2004 carried out by Z/Yen Limited for a consortium of 9 major Banks.

The study was performed based on individual interviews using a structured questionnaire, as developed by Z/Yen and the participating Banks (the Brokers). leading Investment Managers (the Clients) were interviewed between September and November 2004.

The Sponsoring Brokers were as follows:

- ABN AMRO
- CSFB
- Deutsche Bank
- HSBC
- JP Morgan
- Merrill Lynch
- Morgan Stanley
- Royal Bank of Scotland
- UBS

A list of the Clients interviewed can be found in section 6.

1.2 Approach

The approach adopted for this study was to:

- Z/Yen set up and facilitated a series of workshops with the Banks to agree and finalise scope, structure, format and questions;
- The Banks selected the Clients who they wished to be interviewed and introduced Z/Yen to senior operations personnel;
- Z/Yen performed the interviews and documented responses and additional comments;
- Z/Yen published the findings and presented these to the Banks.

2. Executive Summary - Overall Summary of Findings

2.1 Background

28 Clients completed the survey between 1st October and 10th December 2004. Three-quarters of organisations interviewed were asset managers. Also included in the survey were three central banks, one hedge fund, a Treasury department of a bank and two private banks.

5 Clients were based in Australia, 2 in China, 9 in Hong Kong, 11 in Singapore and 1 in South Korea. Responses were on a regional (Asia Pacific) and country-specific basis (in some cases, the European and/or North American branch of the Client also participated in their regional surveys).

2.2 Key Messages

There were a number of points in the survey on which Clients were almost unanimous. Other key messages varied by Client but nevertheless responses can be usefully categorised. This section summarises these key messages:

- **Generally high level of satisfaction with sponsoring Brokers:** In the rankings sections, few marks for any Broker were below 3 (satisfactory). In general, Clients were satisfied or better with the operational services they received from the sponsoring Brokers.
- **Focus on core processing:** Clients placed a very high value on core operational processes (significantly above the value placed upon CRM activities). For most, the main points that they wanted to emphasise to Broker operations were, "*timely and accurate confirmations*".
- **Emphasis on minimum standards of performance:** For most, there were a set of minimum standards for essential operational processes - especially for delivery of equity confirmations. The focus of Clients' operations management was on Brokers who did not regularly deliver to these standards. Significantly exceeding the performance thresholds did not carry much additional weight over just meeting them.
- **The bar is lower for fixed income than equities:** Many Clients had rigorous standards for receipt of equity confirms (often two hours from trade). Fixed income standards were more relaxed with a large number instructing the custodian and including trades in fund manager positions before receipt of a confirmation.
- **High operational performance maintains business levels:** Half of the Clients indicated that operational performance could have a positive impact on business flow, though most of these added that their influence was much more likely to be in reducing business flow to a selected Broker. Where Operations departments were involved in the formal Broker selection process, they received a relatively small proportion (5 or 10%) of the Broker vote.

- **Poor operational performance loses business:** Consistent failure to meet minimum standards of operational performance typically leads to a series of actions, initiated by the Client Operations groups.

Action on sub-standard operational performance begins with peer-to-peer discussions within operations, followed if necessary by escalation to the Fund Manager/Trader. If these steps did not yield results, most Clients said that a suspension of trading would result.

While such suspensions were rare (one or two occurrences a year at most) and generally relatively short, one Broker was struck off by a Client in the Japanese market over two years ago with no resumption of trading to date.

- **No “one-size-fits-all” support model to satisfy all Clients:** There was no common agreement on whether Client service should be via a single point of contact, or via a range of known individuals. Similarly, while most Clients wanted semi-annual (or even more frequent meetings) with their key Brokers, some did not want any meetings at all unless there was a specific issue to discuss.
- **Cultural differences:** While there were no significant differences between the overall responses received from Hong Kong and Singapore based Clients, it was noticeable that Australian Clients placed more emphasis on the strength of personal relationships between Broker and Client staff. The majority cited face-to-face meetings between staff of all levels as a very useful precursor to a strong relationship.
- **Importance of well communicated and seamless staff transitions:** Irrespective of preferred support model, a number of Clients felt that staff changes were not always well communicated and that it took a significant amount of time to build working relationships with the new staff.
- **Knowledge of market practise and of the Client's business:** Clients generally expected Broker staff to have a greater knowledge of market practise than their own and to be able to advise on changes where appropriate. A few pointed out that more frequently traded markets are well understood by most; it is the exceptional cases that cause difficulties and provide opportunities for Client service and relationship management staff to shine.
- **CRMs should carry weight within the organisation:** A number of Clients stressed the importance of the relationship manager having the ability to drive changes within the organisation. This may be to rectify recurring problems or to provide tailored services to the Client where required.
- **A quarter of Clients maintain Management Information (MIS) on Broker operations:** A small number of Clients maintained their own MIS on Broker operational performance (or bought this from OMGEO). These Clients were generally the most active managers of their relationships with the Brokers.

- **Clients who do not maintain Broker operations MIS would like to receive this:** These statistics would also assist as a focus for discussion in relationship management meetings. The desired frequency varied by Client between monthly and semi-annually. (Fails reporting was required on a daily basis by most).
- **Website access is “nice-to-have”, but not essential:** A small number of Clients would be happy to use Broker websites to investigate issues before speaking to Broker staff. For most Clients though, this was at best a useful additional service, but emphasised that ideally, Brokers should inform them of issues before they themselves spot them.
- **No clear technology adoption trends:** There was no widespread move towards CTM. There was also no strong move towards increased automation of fixed income confirms; for many, trade volumes were thought to be too low to justify the expense.
- **Few major operations & technology projects planned:** No more than 4 Clients said that they planned to begin using any one of the technologies listed in the survey in the next two years.
- **Feedback and benchmarking:** Many Clients were interested in receiving Broker feedback on their operational performance – if they were at the root of problems, they wanted to know about it. The six monthly reviews were cited as one (but not the only) opportunity to provide such feedback. Over half of the Clients surveyed were also interested in peer ranking of their organisation's operational performance against other investment managers.

2.3 Core Transaction Management (Operations Best Practice)

Clients were asked to apply a weighting to 7 categories of Core Transaction Management (Operational Performance), both Domestically and Internationally. The results were as follows:

	US / European Equities	Japanese Equities	Asia Pacific Equities
Confirmation Timing	33%	32%	32%
Confirmation Accuracy	26%	27%	29%
Settlement Performance	19%	20%	18%
Fails Management	9%	11%	10%
Interest Claim Management	6%	4%	4%
Static Data Management	6%	6%	6%

	US / European Fixed Income	Japanese Fixed Income	Asia Pacific Fixed Income
Confirmation Timing	35%	34%	32%
Confirmation Accuracy	27%	27%	27%
Settlement Performance	18%	21%	20%
Fails Management	8%	8%	9%
Interest Claim Management	6%	4%	6%
Static Data Management	6%	6%	6%

Confirmation timing and accuracy were consistently rated as the most important factors in core transaction management. A large number of Clients also stated these as the most important areas of focus that they would like to stress to Brokers' operations departments. Accurate confirmations were viewed as essential to effective settlement and a key tool in avoiding fails. A large number of Clients also said that they would not include unconfirmed trades in the following day's NAV or fund manager positions, increasing the visibility of Broker confirmation performance beyond the Client operations department.

Standards for equity confirmations were significantly tighter than for fixed income confirmations. While all required same day confirmations (generally within 2 hours of trade) for equities, some were content to receive fixed income confirmations any time before settlement. The principal reason for this was the lack of automation of fixed income confirm processing in many Client operations departments. Two directly expressed an intention to begin tightening up their demands in this area. Some also indicated plans to automate fixed income confirmations during the next two years and can also be expected to begin demanding that fixed income processing standards match those for equities.

Settlement performance was the next most highly rated factor and received approximately the same weighting as the remaining factors (Fails Management, Interest Claim Management and Static Data Management) combined. This reflects the common view that avoidance of problems is much more important than successful resolution of them, with one stating that they didn't expect fails to happen at all.

There were no material differences in the relative weightings between equities and fixed income.

2.4 Client Management

For the purposes of this survey, the participating banks/Brokers have agreed the following terminology:

- **Client Service (CS): An individual or team who is/are the day-to-day contacts for Operational Issues.**
- **Client Relationship Management (CRM): An individual/team responsible for the overall operational relationship.**

Clients were asked to apply a weighting to 6 categories of Client Management. The results were as follows:

	Equities	Fixed Income
Client Service	31%	31%
Client Relationship Management	21%	19%
Linguistic Skills	8%	9%
Product Knowledge	15%	18%
Regular MIS	6%	7%
Responsiveness to Queries	19%	16%

Client Service was rated by a large majority of respondents as the most important factor in effective Client management, expressing a pragmatic focus on swift resolution of problems when they do occur. The factors that Clients listed as being key to effective Client Service included:

- Provision of timely and accurate confirmations;
- Prompt response to queries;
- Proactivity;
- Sound knowledge of markets and internal processing;
- Understanding of any specific Client requirements;
- Effective communication of staff changes; and
- Back up Client service contacts should be able to provide full cover; seamless service is essential.

There were no material differences in the relative weightings between equities and fixed income.

There were mixed views on the value provided by Client relationship management. This factor received approximately 20% of the overall weighting and was valued by some who saw the CRM as a useful escalation point and someone who should hold the power to "get things changed". The key points mentioned for successful Client relationship management were:

- Knowing the Client;
- Having the ability to co-ordinate regionally and access information globally;
- Monitoring performance;
- Having the ability to tailor services for Clients;
- Being an effective escalation point; and
- Ensuring that the root (and not just the effect) of issues is addressed.

A small number of respondents simply wanted to deal with whoever could resolve the issue and placed a low value on relationship management activities.

Almost all Clients thought that Operational Review meetings were useful. Of those who were specific about the Broker representation that they required at these sessions, 13 mentioned the CRM along with some member of the Client service staff or an operations head, while 7 preferred simply to meet with the appropriate operations head and his/her staff and made no mention of a CRM in this regard.

2.5 Linkage of Operational Performance to Business

Approximately half of the Clients interviewed indicated that high operational performance had the power to increase business flow if all other things were equal. However, these Clients all said that front office factors (especially pricing and ability to source hard-to-find stocks) significantly outweighed Operations' influence. Most of these Clients also suggested that operational factors were much more likely to have a negative influence by causing a reduction of business flow to a particular Broker.

The main scenario cited for the positive influence of Operations on business flow was the situation where one Broker provides poor operational service and is suspended or struck off. In this case, Operations departments believed that they could sometimes have a significant influence in determining how this business was reallocated. (One Client cited an example where trading on a particularly sensitive new mandate had been ceased with two Brokers due to unreliable performance and transferred to a third, more trusted Broker. This change was on the advice of the Operations department).

Three Broker Operations departments indicated that they did hold a small share of the vote in the formal Broker selection process and in these cases, operations certainly could have a positive influence on the flow of business.

2.6 Internet Portals

Although 72% of Clients expressed an interest in Broker websites, for most this would be a "nice-to-have" additional feature. Very few would use these before calling a Client service representative. For most, the website would be more likely to be used to access management information or if all other routes to the required information failed.

For the remaining 28%, the consensus opinion was summed up by one who said "*we don't want to have to access lots of different websites to get the information we require*".

2.7 Top Clients/Overall Differential

There was no obvious trend in the differential between marks awarded by preferred Clients and those from others in the survey. In a few cases, the marks from preferred Clients were significantly lower than the overall average. This may have been in part due to the relatively small sample sizes in some of the voting categories.

2.8 Penalisation of Banks

Poor operational service does have a negative impact on business flow. Almost all Clients had a mechanism for escalating severe operational problems via the trader/fund manager, and if all else failed to temporarily (or even permanently) cease trading with a Broker in a particular market. The most likely factor to cause this was late or inaccurate confirmations. These were cited as having particular visibility to traders where operational policy was to exclude unconfirmed trades from the next day's positions and NAV.

2.9 Strategic Direction - Initiatives Planned

Although two Clients indicated that they were currently undergoing major strategic reviews of operations technology, there was generally a marked absence of major initiatives. None of the suggested technologies had already been adopted by more than 50% of those interviewed and no more than 4 Clients (14%) indicated that they planned to adopt any one new technology during the coming 2 years.

While most Clients have automated their equities matching processes via some mechanism, most have not yet taken this step for fixed income trading. Many feel that the expense is not justified by the trading volumes involved.

2.10 Next Steps

Z/Yen will arrange individual feedback sessions with each of the sponsoring Brokers early in 2005. The Clients who participated in the survey will each receive a summary copy of the report.

Z/Yen plans to repeat this survey in Q3/Q4 of 2005.

2.11 General Client comments/observations.

Of the 28 Clients who participated, most were very willing to answer follow up questions in face-to-face meetings or over the telephone. Most also believed that the survey would be a useful feedback tool and made comments such as:

"We are very happy to give a little of our time to help out the Brokers"

"I look forward to seeing how the responses affect the services that we receive"

"The survey is very comprehensive and will provide good feedback to the Brokers".

21 Clients declined to participate in the survey this year. 5 of these cited current workloads, but hoped to participate in future surveys. 4 were concerned about the possible release of confidential information and 2 had no significant operations department in the region. Z/Yen was not informed of the reasons of the other 10 non-participants.

3. List of Participating Clients

All Clients Interviewed

- Lloyd George Management Ltd
- Invesco Asia Ltd
- HSBC Asset Management (HK) Ltd
- United Overseas Bank
- Franklin Templeton
- JF Asset Management Ltd
- Prudential Asset Management (Singapore) Ltd
- Morgan Stanley Investment Management
- Monetary Authority of Singapore
- Bank of China Beijing
- Credit Agricole Asset Management Hong Kong
- PMA Investment Advisors Ltd
- BOCI Prudential Asset Management Ltd
- ABN AMRO Asset Management (Asia) Ltd
- State Administration & Foreign Exchange (People's Bank of China)
- Colonial First State Investments Ltd
- BT Financial Group
- AMP Capital Investors
- Credit Suisse Asset Management
- HSBC Private Bank
- Vanguard
- OCBC Asset Management Ltd
- AXA Rosenberg Investment Mgt Asia Pacific Ltd
- Bank of Korea
- Schroder Investment Management (Singapore)
- Development Bank of Singapore
- An Asset Management Organisation
- Credit Suisse Private Bank

4. Z/Yen Limited

Z/Yen is the UK's leading risk/reward management consultancy.

Risk/reward management is the application of risk analysis and return incentives to strategic, systems, human and organizational problems in order to improve performance. Z/Yen believes that the intelligent management of risk is the basis of significant reward. By recognizing, understanding and managing risks, more risks can be assumed and performance increased.

Z/Yen applies risk/reward management in the public, private and not-for-profit sectors, with particular expertise in:

- Financial Services
- Technology
- Not-for-Profit Sector
- Professional Services
- Business Intelligence

Within Financial Services, Z/Yen performs Cost per Trade benchmarking studies, operational performance analysis, best practice surveys, strategic planning (outsourcing, re-engineering, relocation) and other market intelligence. Z/Yen's market scope encompass European Securities, US Securities, Asian Securities, Global Treasury

Z/Yen's work has enabled banks and other financial institutions to:

- Understand whether economies of scale efficiencies have been realized;
- Identify in which products or businesses they are either efficient or inefficient processors;
- Identify where in the trade processing lifecycle they have scope for improvement;
- Identify and quantify "best of breed" and determine efficiency targets;
- Analyse progress and trends on a year-on-year basis;
- Monitor relative performance for management.

For more information on Z/Yen, visit our website www.zyen.com or call Jeremy Smith on +44 (0)20 7562 9562.