



**OPERATIONAL
PERFORMANCE OF BROKERS
Market Survey
European Securities
2004**

Summary of Findings

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

**(44-20) 7562-9562 (telephone)
(44-20) 7628-5751 (fascimile)
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 2004 Operational Performance of Brokers - European Securities Survey, carried out by Z/Yen Limited for a consortium of 13 major Banks ("the Brokers").

The study was performed based on individual, predominantly face-to-face interviews with clients using a structured questionnaire, as developed by Z/Yen and the participating Banks. 71 leading Investment Management companies, ("the Clients") and/or in some cases, their Outsource Agents were interviewed between 1st September and 10th November, 2004.

The Sponsoring Brokers were as follows:

- ABN AMRO
- Citigroup Global Markets
- CSFB
- Deutsche Bank
- Goldman Sachs
- HSBC Bank plc
- ING
- JP Morgan
- Merrill Lynch
- Morgan Stanley
- Nomura International
- Royal Bank of Scotland
- UBS

This report may be read in conjunction with the reports from the corresponding Operational Performance of Brokers surveys:

- US Securities 2004
- Asian Securities 2004

A list of the Clients interviewed can be found in section 5.

1.2 Approach

The approach adopted for this study was:

- Z/Yen set up and facilitated a series of workshops with the Brokers to agree and finalise scope, structure, format and questions;
- The Brokers selected the Clients who they wished to be interviewed and introduced Z/Yen to appropriate senior operations personnel;
- Z/Yen performed the interviews and documented responses and additional comments. Z/Yen re-iterated to clients that rankings should cover the calendar year, and not only recent performance;
- Z/Yen published the findings and presented these to the Brokers.

1.3 Detailed Report

A further detailed report of the survey is available and has been distributed to the Brokers and Clients.

2. Executive Summary

2.1 Overall Summary of Findings

2.1.1 Background

71 Clients were interviewed between September 1st and November 10th 2004. The Clients interviewed were predominantly Investment Managers (76%). The remainder, (24%) were Pension Funds or Insurers (or indicated that they had Pension/Insurers as end Clients).

46 Clients were based in the UK and 25 were elsewhere in Europe. Some Clients had solicited feedback from their overseas offices to ensure global and/or appropriate product coverage. Almost all Clients had a global focus of investment, and 70% are responsible for managing over US\$50 Billion of Assets).

2.1.2 Key Messages

There were a number of messages that emerged from the interview stage of the survey, which Clients were very often quite passionate about. To help illustrate these, we have included numerous quotes in Section 3 of this report. The key messages were:

- **Importance of Core Processing Functions:** The Operational Performance of Brokers continues to be an important factor in the choice of Brokers, both in the allocation of new business and in the protection of existing business levels. In particular, Clients place a high degree of emphasis on timely, accurate and effective transaction management, particularly the confirmation and settlement process.

Following a suggestion from one client during the interview process, we asked a number of Clients to provide an additional weighting, distinguishing between Core Processing functions, i.e., the Day to Day service, and Added Value functions such as Client Relationship Management (CRM). The results showed a 70% - 30% split in favour of Day to Day servicing.

- **Effective Relationship Management:** While Clients see Core Transaction Processing (and related day-to-day Client Service) as key, most observe that Client Relationship Management is also a distinguishing factor in the perception of Operational Performance. Clients often reflect this in their internal ranking processes, particularly where the CRM is a point of escalation, a **provider** of information on market and industry changes, and/or an **advisor** on how these changes can impact the client.

Clients that have relationships with CRMs, want them to be "*effective*" in that role, not simply being a "*figurehead*", a "*mailbox*" or someone who arranges semi-annual visits "*for the sake of it*".

- **Growth of Outsourcing:** The extent to which Clients are Outsourcing some or all of their Operations has increased significantly over the last year. 9 of the interviews this year were with Clients that had outsourced, or with outsource agents on behalf of specific Clients. The large organisations that are now providing outsource services all expect their Client base to grow, and several Clients interviewed are considering outsourcing as an option for their future strategy.

Brokers should be aware of the growth of these 'tri-partite' arrangements, and look to work with the major providers as well as Clients in developing appropriate structures.

- **Increased Focus on Broker Ranking:** Clients are increasingly investing in systems, processes and people to monitor and subsequently rank Broker performance. **Over 50% of the Clients now formally rank brokers (compared to 25% last year).** This increase is across the board, and is not limited to Clients of a particular size (of assets under management), or in a particular location.

Many Clients have built (or are developing) complex tools for measuring objective criteria, e.g., statistics, on Confirmation Timing and Accuracy, Settlements and Fail rates. Additionally, Clients are capturing subjective Operational input, e.g., human perspectives, into the ranking process. Several Clients have established full or part time Broker Liaison roles to support this strategy.

- **Benchmarking:** Clients are hungry for accurate benchmarking to support their ranking initiatives. 20% of those interviewed use OMGEO benchmarking, but many Clients have developed their own systems, which they are finding increasingly useful. Clients want more from the Brokers (by way of MIS) to help them in this objective.
- **"Know your Client":** There is no 'One Service Fits All' model. While Clients in general expect operational excellence from Brokers, they also generally understand that there may be processing and/or relationship issues from time to time. Clients expect a similar understanding from Brokers that most Clients are different, having varying degrees of volume, expectations, speed of change and automation (very often with well founded historical reasons for their status - sometimes even by region).

This point was made quite clear in the question that asked how Brokers can demonstrate Operational Excellence. While the perceptions of CRM were fairly standard in this regard, day-to-day Client Service requirements differed significantly - highlighting a real need for brokers to be flexible and tailor the relationship accordingly.

- **Global Coverage:** While the location of the client did not demonstrably impact the expected (or perceived) service levels, a common issue was the inability (in most cases) for Brokers to interrogate systems, or answer queries in a timely fashion, for trades executed in Asia or the U.S.

On a related matter, there were also many requests for brokers to reduce the number of Entities and/or Acronyms, to make SDI maintenance easier for Clients.

- **MIS:** Clients are increasingly demanding (and generally not entirely satisfied with) higher levels of MIS from Brokers. Clients are increasing their focus on broker ranking and need the data to support this. Also, Clients are becoming more interested in (their) Peer performance. Over 90% expressed an interest in a potential 'reverse' survey; whereby brokers would have the opportunity to rank Clients' performance.

2.1.3 Core Transaction Management (Operations Best Practice)

Clients were asked to apply a weighting to 5 categories of Core Transaction Management (Operational Performance). The results were as follows:

	Equities	Fixed Income
Confirmation Timing	30%	30%
Confirmation Accuracy	28%	28%
Settlement Performance	25%	26%
Interest Claim Management	5%	6%
Static Data Management	12%	11%

As in 2002 and 2003, the key requirement is for timely and accurate confirmations, though the combined weighting (58%) has increased from 52% in 2003. The benchmark remains 'same day', and for many Clients, within 2 hours. Clients are increasingly monitoring brokers' performance for confirmation timing. Settlement is also seen as important with emphasis shifting away from interest claims. As with Client Service expectations, there are no material differences in the weightings between Equities and Fixed Income.

With more and more Clients monitoring broker performance and ranking brokers, Clients have a more informed view of specifically where brokers are under-performing. These areas, where identified, were often ranked poorly.

Clients were also asked for their "single most important" requirement from a broker's operations. Responses were:

Just over half the Clients responded that **Confirmation Timing and Accuracy were the key service components**. Most opted for Timing, as this then allowed Clients a greater window in which to address Accuracy issues with Brokers.

No other criteria received more than 5 'votes', but areas that are critical for certain Clients included:

- General Core Transaction Management;
- Understanding the nature of an Outsource Business Model;
- The overall Settlement process;
- Static Data Maintenance;
- Single Settlement Instruction/Acronym;
- Better MIS;
- Response Time on Queries.

2.1.4 Client Management

For the purposes of this survey, the participating brokers agreed the following terminology (which was presented to Clients during the interview):

- **Client Service (CS):** An individual or team who is/are the Day-to-Day contact for operational issues.
- **Client Relationship Management (CRM):** An individual or team who is/are responsible for the overall operational relationship (including single point of contact for escalation, bank/broker review meetings, new operations/process implementation etc.

Clients were asked to apply a weighting to 5 categories of Client Management. The results were as follows:

	Equities	Fixed Income
Client Service	43%	43%
Client Relationship Management	26%	25%
Linguistic Skills (Non UK)	7%	6%
Product / Market Knowledge	14%	16%
Regular MIS	11%	10%

Since 2003, the weighting for Client Service has increased by approximately 3%, with less emphasis generally being placed on Linguistic skills.

Clients generally re-enforced their expectations of last year, highlighting pro-activeness, availability, product knowledge and a quick response time to queries. Also, the majority of Clients want/expect Client Service representation at Relationship Review meetings - either to add validity to detailed discussions, or to meet up with their operational counterparts.

For CRM, Clients stressed that single point of contact and a point for escalation are the key expectations of the CRM function. There was additional emphasis placed on the CRM as a provider of information on market and industry developments, and also as the Clients' voice' at the broker. While some Clients see no significant difference between effective CS and CRM, many more Clients expect the CRM to be senior, empowered and professional but also easily contactable.

2.1.5 Linkage of Operational Performance to Business Allocation

The number of Clients that formally rank Brokers' Operational Performance has increased significantly (over 55% of clients interviewed this year, compared with 25% in 2003). Client's Operations groups are increasingly tracking performance and distributing the findings internally, to Dealers, Fund Managers and underlying Clients.

The number of Clients that now have a formal broker vote has also grown significantly from 12 in 2003 to 24 in 2004. The proportion of the Broker Vote given to Operations has, however, remained fairly static with a 2004 median percentage of 15%.

Program Trading remains the area where Operations feedback and advice is most often valued, but close relationships generally (between Clients' Operations and Front Office) has led to Operations often believing that they have a greater say in the allocation of business.

2.1.6 Penalisation of Brokers for Poor Operational Performance

Approximately half the Clients interviewed are prepared to penalise brokers for poor operational performance. Ultimately, this can often take the form of reduced or suspended trading. Many Clients were keen to point out however that penalisation can take several other forms, including escalation to front office, probationary periods, downgrading of rankings or seeking regular updates from the brokers as to their 'fixes'. The practice of suspending brokers for certain types of trades, or in certain markets only, seems to be increasing.

The main reasons for a reduction in trading or even suspension are typically confirmation and/or settlements related. With an increasing number of Broker Liaison roles and close relationships between front and back office, Clients' Operations areas are feeling more empowered to make recommendations to suspend. This is despite the fact that Clients recognise this action may set back the overall relationship.

2.1.7 Internet Portals

There was a significant increase in the number of Clients that would be prepared to use direct access to brokers' websites. In almost every case however, Clients required on-line access as a back up to either reporting or proactive CS/CRM communication. Many Clients want on-line back-up access to time critical elements such as Fail and Settlement status. There is also greater demand generally for MIS, and website access was one of several routes of supply identified by Clients.

2.1.8 Top Clients/Overall Differential

In most cases, individual Broker "Top 20" Clients results produced higher rankings than the average of all 71 Clients. This may indicate that service tier differentiation has been implemented and/or that Brokers Top Clients have a historically higher level of service from that Broker. There is generally a higher proportion of 'Excellent' or 'Good' rankings offered by Brokers' Top 20 Clients - perhaps reflecting the 'Platinum or Gold' status that many Clients have been given.

2.1.9 Strategic Direction - Initiatives Planned

Clients are focusing on improving their own Straight Through Processing (STP) models in conjunction with (and as well as) monitoring and improving Broker performance in this regard.

Additionally, Brokers will need to be sensitive to the (sometimes significant) changes within Clients' organisations. For example, 10 Clients surveyed, are likely to be impacted by outsourcing over the coming year, either by way of moving functions out (or in), reviewing processes for potential outsourcing, or changing their structure to accommodate current outsourcing. Other logistical changes that Clients are planning (and/or currently managing) include mergers, globalisation, volume changes and product diversification.

From a systems perspective, there is generally a 'wait and see' approach with regard to OMGEO CTM. In many cases, Clients were looking for greater guidance from Brokers in regard to possible alternatives.

2.1.10 Equities vs. Fixed Income

As with last year, average Equity rankings tend to be slightly higher than for Fixed Income, with particular differentiation in Core Transaction Processing. Some Clients commented that the 'gap' between Equities and Fixed Income had closed a little since last year, but most still identified a significant difference in the levels of service received. Some interesting observations included:

- *"In general. Equities are better processed than Fixed Income. It seems that Equities have had greater investment (systems, MIS etc) and also, the volume and the history. Fixed Income is catching up but volumes are still lower so it is taking time."*
- *"FI vs. Equities: The gap has not closed, but more FI brokers are using enhanced electronic processing."*
- *"FI needs to be looked at big time - why does it take so long to get confirms? FI has not changed over the last year so maybe it's more the 'gentleman's agreement' thing...Equities are more snappy!"*
- *"FI is still piggy backing off Equities in terms of service (STP issues at review meetings are always FI related). A lot of brokers still trade as 2 separate entities for FI vs. Equities (buildings, people, systems)."*
- *"EQ / FI: Equity fails 5%, FI fails 28% - but FI have less trades so the fail rate is exacerbated."*

2.1.11 Most Improved Areas

Clients observed an improvement in almost every criteria covered by the survey. There were only 2 criteria where scores did not rise (Equities Linguistic Skills was the same as 2003, Equities Product Knowledge dropped by 1.5%).

Overall, Client Service and CRM average ranks improved between approximately 5% to 8%, but the most notable improvement was in Equities Settlement performance, where Clients reported a 9% increase in performance across the market.

Additionally, at the weighted summary level, in Equities Client Management, FI Core Transaction Management and FI Client Management, there was a much narrower spread of results between top and bottom rated brokers than in 2003. This indicates the focus and effort that last year's "poorly ranked brokers" have put into improving their services.

Key Changes since 2003

Ranking Criteria	2003 Average	2004 Average	% Inc.
Equities: Confirmation Timing	3.49	3.66	3.7%
Equities: Confirmation Accuracy	3.52	3.67	4.4%
Equities: Settlement (Pre-matching)	3.49	3.70	6.0%
Equities: Settlement (Value Date / Fails)	3.34	3.64	9.1%
Equities: Client Service	3.34	3.60	7.8%
Equities: Client Relationship Mgt.	3.44	3.61	4.9%
FI: Confirmation Timing	3.14	3.42	8.9%
FI: Confirmation Accuracy	3.29	3.46	4.9%
FI: Settlement (Pre-matching)	3.42	3.47	4.6%
FI: Settlement (Value Date / Fails)	3.34	3.61	8.2%
FI: Client Service	3.26	3.52	7.9%
FI: Client Relationship Mgt.	3.25	3.48	7.0%

2.1.12 Client Feedback on the survey

A small number of Clients (7) who participated in last year's survey were unable to take part this year, mostly due to logistical difficulties (Fund mergers, Organisation mergers or indeed imminent (or recent) outsourcing). Most of these however suggested that they would be able to participate next year. On a very positive note, many Clients (21) participated in the survey for the first time.

Clients were generally happy to take part in the survey and were enthusiastic and constructive in their input. Some did observe however that the Settlements ranking criteria could be amalgamated and/or that they could make no distinction between Equities Single Stock and Program Trades. There was significant interest (approx. 90%) in a peer ranking of Investment Manager's Operational Performance (i.e., a 'reverse' survey). Additionally, Clients were keen for Z/Yen to arrange a follow up workshop.

Comments and suggestions to enhance the survey process included:

- *"We were pleasantly surprised by the extent of broker follow up to the last years survey."*
- *"We would be interested in a peer comparison - versus other outsource agents."*
- *"Z/Yen survey is a valuable exercise and the workshop is very good. How about having another one 3-4 months later to follow up on issues. Do something more regarding trends."*
- *"It took us time to complete this survey, but we see it as a positive investment."*
- *"Our first time in the survey and we really like the idea. Maybe you could conduct similar surveys for FO criteria and also Prime Brokerage?"*
- *"Survey is quite an effort, but we will do next year as well (we cannot differentiate between types of settlements - can we merge Single Stock and Programs?) YES - Most definitely for reverse survey!"*
- *"The Z/Yen survey comes up at all the CRM meets. Results last year didn't tell us anything we didn't know. However, for those brokers not participating - tell them they should !"*
- *"Excellent survey ! We think this kind of thing can only help (increase competition amongst the brokers and therefore performance)."*
- *"A lot for us to complete but we do see the benefit....any chance of a workshop for Clients in Scotland ?"*
- *"How about a Custodian survey ? Yes to reverse survey - especially as we (as outsourcer) are now the client of the client. We would also be interested in an outsourcer survey."*
- *"We do still get some requests for individual broker ranking, but the number is decreasing. A lot of brokers tell us how important the Z/Yen survey is to them."*
- *"Can we have a country specific survey, to look at domestic issues, and involve more Local brokers?"*

2.1.13 Next Steps

Z/Yen will arrange 1-1 feedback sessions with the each of the sponsoring Brokers.

The Clients who participated in the survey will be sent a summary copy of the report and also be invited to attend a workshop/presentation of findings. We are planning a separate meeting in Scotland.

This survey will be repeated in Q3/Q4 2005. We will also look to initiate a "reverse survey" early in 2005

3. Overall Summary of Rankings

The individual activity Rankings of each Broker were made by the Clients and are based on overall 2004 performance for each activity. The individual activity Rankings were then multiplied by the Activity Weightings (also Client-supplied) to give overall Equity and Fixed Income Ranks.

Overall Performance scores have been calculated by adding the Core Transaction Management and Client Service ranks.

Most Improved scores have been calculated by the overall difference between the 2003 total score and the 2004 total score.

For 2004, the overall Top 3 banks in each category are as follows:

Equities

Core Transaction Mgt. (CTM)

1. DRKW
2. Merrill Lynch
3. CSFB

Overall Performance (CTM + CS)

1. CSFB
2. Merrill Lynch
3. DRKW

Client Service (CS)

1. CSFB
2. Merrill Lynch
3. Citigroup

Most Improved since 2003 (CTM + CS)

1. Deutsche Bank
2. UBS
3. ABN AMRO

Fixed Income

Core Transaction Mgt. (CTM)

1. DRKW
2. Merrill Lynch
3. ABN AMRO

Overall Performance (CTM + CS)

1. DRKW
2. Merrill Lynch
3. CSFB

Client Service (CS)

1. CSFB
2. DRKW
3. Merrill Lynch

Most Improved since 2003 (CTM + CS)

1. Royal Bank of Scotland
2. Deutsche Bank
3. UBS

4. Broker Ranking - Summary of Top 3 Banks

Equities Core Transaction Management	First	Second	Third
Confirmation Timing - Single Stock	DRKW	ABN AMRO	Merrill Lynch
Confirmation Timing - Program Trading	Nomura Int.	ABN AMRO	Merrill Lynch
Confirmation Accuracy - Single Stock	DRKW	CSFB	Merrill Lynch
Confirmation Accuracy - Program Trading	CSFB	Merrill Lynch	Lehman Brothers
Settlement Performance - Pre-Matching	ABN AMRO	DRKW	CSFB
Settlement Performance - On Value-Date	CSFB	DRKW	Merrill Lynch
Settlement Performance - Fail Management	DRKW	Lehman Brothers	CSFB
Interest Claims Management	Deutsche Bank	CSFB	Nomura Int.
Static Data Management	DRKW	CSFB	JP Morgan

Equities Client Management	First	Second	Third
Client Service	Merrill Lynch	Citigroup	CSFB
Client Relationship Management	CSFB	Merrill Lynch	Deutsche Bank
Linguistic Skills	Morgan Stanley	Citigroup	CSFB
Product Knowledge	CSFB	Citigroup	DRKW
Regular MIS	CSFB	DRKW	ABN AMRO

Fixed Income Core Transaction Management	First	Second	Third
Confirmation Timing - Cash Bonds	DRKW	Merrill Lynch	Nomura Int.
Confirmation Timing - Repo	DRKW	ABN AMRO	Citigroup
Confirmation Accuracy - Cash Bonds	Nomura Int.	Citigroup	Lehman Brothers
Confirmation Accuracy - Repo	Lehman Brothers	DRKW	Citigroup
Settlement Performance - Pre-Matching	Goldman Sachs	Merrill Lynch	ABN AMRO
Settlement Performance - On Value-Date	Goldman Sachs	ABN AMRO	DRKW
Settlement Performance - Fail Management	Lehman Brothers	DRKW	Merrill Lynch
Interest Claims Management	ABN AMRO	CSFB	Nomura Int.
Static Data Management	CSFB	DRKW	RBoS

Fixed Income Client Management	First	Second	Third
Client Service	Merrill Lynch	DRKW	Citigroup
Client Relationship Management	CSFB	Morgan Stanley	ABN AMRO
Linguistic Skills	ABN AMRO	JP Morgan	DRKW
Product Knowledge	CSFB	DRKW	Citigroup
Regular MIS	CSFB	ABN AMRO	DRKW

5. List of Participating Clients

- Bank for International Settlements
- Morley Fund Mgmt. UK
- Schroder Investment Mgmt. Ltd.
- JPMorgan Fleming Asset Mgmt.
- Bank of New York (Merrill Lynch Asset Mgmt.)
- Goldman Sachs Asset Mgmt. International
- Henderson Global Investors Ltd.
- Morgan Stanley Investment Mgmt. Ltd.
- CDC IXIS Asset Mgmt.
- Ferox Capital
- Crédit Agricole Asset Mgmt.
- Allianz, Frankfurt
- Threadneedle Asset Mgmt. Ltd.
- Bank Of New York (JP Morgan Fleming AM.)
- Swiss Re-Insurance
- Deutsche Asset Mgmt. Group, UK
- Nextra Investment Mgmt.
- State Street (Scottish Widows Inv. Part. Ltd.)
- UBS Asset Mgmt., UK
- Deka Investment
- Credit Suisse, Switzerland
- ABN Amro Asset Mgmt., UK
- ING Investment Mgmt.
- ISIS Asset Mgmt. plc
- M&G Investment Mgmt.
- Deutsche Asset Mgmt. Group, Germany
- Invesco
- AXA France
- Allianz, Munich
- BNP Paribas Asset Mgmt.
- BNP UK (Hendersons)
- Legal & General Investment Mgmt. Ltd.
- Insight Investment Mgmt. Ltd.
- Pictet & Cie, UK
- Templeton Emerging Markets
- HSBC Asset Mgmt.
- Alliance Capital
- Credit Suisse Asset Mgmt. UK
- Banque D'Orsay
- BlackRock International Ltd.
- Citigroup Asset Mgmt.
- Fortis, Belgium
- Monte Paschi Asset Mgmt.
- Aegon Asset Mgmt., UK
- Baring Asset Mgmt.
- Baillie Gifford and Co.
- State Street Global Advisors
- Newton Investment Mgmt.
- GLG Partners LP
- Allianz Dresdner RCM, UK
- State Street (Norges Bank)
- Dexia Brussels
- Hermes Investment Mgmt.
- TT International Investment Mgmt.
- Bank of Ireland
- Capital International, Switzerland
- Royal London Asset Mgmt.
- Britannic Asset Mgmt. Ltd.
- Martin Currie Investment Mgmt.
- State Street (ABN Amro AM. Holland)
- Nomura Asset Mgmt.
- Societe General Asset Mgmt.
- Pictet et Cie, Switzerland
- Aegon Asset Mgmt., Holland
- T. Rowe Price
- Mellon Bank (F & C Mgmt. Ltd.)
- Fidelity
- Banco Bilbao Vizcaya
- Arca
- Alecta
- SEB