Workflow Magazine

INDUSTRY INSIGHT AND VIEWS FROM THE STATPRO BLOG AND CONTENT LIBRARY

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CONTENTS

Industry insight and views from the StatPro blog and content library

INTRODUCTION

Planning for uncertainty

There are an increasing number of 'unknowns' in the industry today such as market uncertainty, the return of volatility, updates in regulations and new regulations being implemented.

With the current political and economic instability between the US and China, trade tension is a current reality that many of us are having to keep a close eye on. These movements in the market require us to asses the potential risk we may be exposed to and better understand what impact these downturns may have on our portfolios.

These market stresses combined with global regulations make for an interesting time as an asset manager or asset service provider. With vastly differing attitudes in the European Union compared to those of the United States, participants in financial markets have different levels of cooperation when it comes to dealing with regulators and liquidity risk, for example. However it is important to note that firms wanting to do business in both geographies, or expand from one to the other, will need a firm grasp of what is required and why in both the US and EU.

Firms are also now paying closer attention to information security when it comes to FinTech and maintaining data security in today's current environment is a priority.

Ultimately, firms need to look at their exisiting processes and the solutions they have in place to ensure that they are able to maintain the necessary competitive edge.

We hope you enjoy this edition of Workflow magazine.
To view all our blog content, visit blog.statpro.com

Michelle Earp
Global Head of Marketing, StatPro

GLOBAL RISK OUTLOOK:

Uncovering country risk during market uncertainty

According to the United Nations Conference on Trade and Development, which publishes the World Investment Report yearly, four of the top five countries by foreign direct investment (FDI) are defined as developing or transitional economies.

First on the list, the United States, is developed, followed by China, Hong Kong, Brazil, and Singapore which are developing. Other developing economies making the top 20 are India, Mexico, Russia, Indonesia, and South Korea. It is interesting to note that although these are popular investment regions, these countries are not always the safest or easiest economies to do business in. The World Bank publishes the *Doing Business report* which ranks the world's economies on 10 sub-indices ranging from investor protection to tax rates to the electric grid, and Brazil, Russia, and China do not even crack the top 30. Russia is the 'easiest' of the three, coming in at 35, while China and Brazil fall out of the top 50 at 78 and 125, respectively.

Our Global Risk Outlook portfolio has direct exposures through the Emerging Equities and Global High Yield books, but what are the true all-in exposures to Brazil, Russia and China and are there unintended exposures we are not aware of? How exposed are we to market downturns in Brazil, Russia and China?

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STATISTICS AND PROBABILITY THEORY

The World Cup and randomness

The average American watching the World Cup has less of an appreciation for the intricacies of set piece routines, or the passing skills of a particular team's midfielder, but there is undoubtedly an enthusiasm for watching the tournament. No doubt the nationalistic pride on display has an impact but Americans also like a good elimination tournament.

Soccer, with normally only a low number of shots on goal each game (usually less than 10), makes for an exciting competition where prior experience is as important as getting a few good looks at the goal in a game. In 2018, World Cup fans saw the prior tournament's winner, Germany, leave in the first group stage and 18th ranked Croatia make it all the way to the Final. This is the beauty of the tournament: teams are not playing in a best of N games round where player and team experience can dominate. Instead they are playing exactly one game against each other's team in their group or playoff round.

A good coach would say to win in a tournament like this you have to put your team in a position to take advantage of luck when and if it presents itself. This is exactly what a good financial risk manager does: they make sure that their portfolios are positioned to withstand the randomness of financial markets while also ensuring the core investment thesis remains.

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IT'S BECOMING INCREASINGLY COMMON FOR PROFESSIONAL SPORTS TEAMS TO COLLECT AND MAKE DECISIONS BASED ON DATA. FOR A RISK MANAGER, GATHERING AND INTERPRETING DATA USING PROBABILITY THEORY AND STATISTICAL TECHNIQUE IS CORE TO THE DISCIPLINE.

DIFFERING IDEOLOGIES

Liquidity risk in the US and EU

Stemming from StatPro's inaugural global regulations panel earlier this month, when it comes to the relationship between regulators and financial firms in the European Union versus the United States, it's safe to say attitudes are quite different.

The global regulations panel was made up of Damian Handzy, Global Head of Risk at StatPro, Carl Bacon, StatPro's Chief Adviser and Chair of the GIPS® Executive Committee, and Mattia Prati, EMEA Client Service Director at StatPro. Broadly speaking, the regulatory burden in the US has been lighter than in most other areas of the world. This stems in part from the general US view on government: Americans have long been leery of government interference in many aspects of life. Meanwhile, the relationship between financial firms and regulators in Europe is generally more cooperative and more consultative in nature.

In the EU, the participants in financial markets tend to want to understand the regulations, so they can be in compliance, both in the letter and the spirit of the law. There's more of a two-way, conversational relationship. In America, the relationship tends to be more antagonistic. American fund managers do not generally proactively seek the SEC's input when ascertaining the scope or impact of a new regulation. They will instead interpret the regulation themselves, in cooperation with their legal advisers. The general mindset seems to be "Here's another regulation we have to deal with. What do we absolutely have to do to be in the clear?".

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WITH TWO VERY DIFFERENT APPROACHES WHEN IT COMES TO REGULATORY POWER AND AUTHORITY, FIRMS WANTING TO DO BUSINESS IN BOTH GEOGRAPHIES, OR EXPAND FROM ONE TO THE OTHER, WILL NEED A FIRM GRASP OF WHAT IS REQUIRED AND WHY IN BOTH THE US AND EU.

The GIPS® 2020 initiative is aimed at modernizing the standards to both keep up with market developments and cast as wide a net as possible, making them relevant for all types of managers and investors.

MODERNIZING THE STANDARDS

The impetus behind GIPS® 2020

Like any heavily regulated industry, financial services has many sets of third-party compliance standards and guidelines to follow.

While compliance with some of these industry standards is voluntary and serves as more of a best practices framework, most responsible firms do make an effort to stay in accordance with them, as doing so helps when keeping in compliance with applicable mandatory regulations. Voluntary compliance also tends to illustrate a company's commitment to operating at high levels of competence, safety and professionalism to all stakeholders.

In investment management, one set of industry standards, the Global Investment Performance Standards, or GIPS®, is set for a revision in 2020. GIPS® is the latest evolution in investment management industry-driven standards, which began in 1987 when the Association of Investment Management (AIMR) unveiled a voluntary set of North American guidelines for investment performance reporting. Later, the standards were elevated to a global level when the CFA Institute created GIPS® in 1999. Following the financial crisis, an updated version of GIPS® was introduced in 2010.

Now, eight years later, GIPS® is due for another refresh.

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KEY QUESTIONS

How to tell the difference between cloud native and cloud wrapped software

Cloud computing is changing the way we all consume and interact with technology.

Whether this is at home with Netflix or Amazon Alexa, or at work, with cloud-based services like Office 365 or Salesforce, or other specialist enterprise applications. In business, cloud computing is an enabler, creating strategic change in the way businesses of all sizes work with technology. In short, a real cloud native service will make your life easier, more efficient and less expensive.

With all the benefits and hype that come along with the word 'cloud', many companies claim to have 'cloud' solutions but are merely hosted software services. How can you be sure that you will receive all the benefits of cloud computing, like lower cost of ownership, zero maintenance, frequent product updates, endless and elastic computing power and more?

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Key questions

YOU NEED TO ASK TO ENSURE THE SOLUTION IS THE REAL DEAL WHEN IT COMES TO THE CLOUD

- **How many versions of the solution are in production with clients?**
- **Does the solution use elastic cloud computing for scalability?**
- **How many updates are made available each year?**
- **Is the solution secure? Has it been externally audited?**
- **How does the service interact with other applications, including my on-premises software?**

What do you need to create a security culture in your organization?

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TRANSFORMING THE INDUSTRY

Creating a security culture in FinTech

Many financial institutions are now working with FinTech providers in partnerships that are helping transform the industry.

Instead of seeing this wave of new start-ups and technological innovation as a threat, institutions are recognizing the opportunity, and young FinTech businesses are discovering potential buyers for their business. As this mashup continues, how can smaller FinTech businesses bring the required level of information security to partnerships or contracts with financial services Goliaths?

Creative freedom

Something FinTech providers are good at, is the level of innovation and creative freedom they encourage their staff to adopt. Rapid cycles of product development and change help improve solutions and bring them to a level where they can be taken seriously by larger firms. This is great for functional development, but in cultures of high innovation and change, how can you ensure there is room for security best practice when it can often be seen as bureaucratic red tape?

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Adoption is key

People and culture are central to information security. You can have all the best technology and policies in place, but if your people are not highly aware of information security and don't adopt that awareness as part of their work culture, then security incidents and breaches are more likely to occur. Many smaller FinTech businesses don't have the budgets for layer upon layer of sophisticated security solutions, and certainly don't have the budget for teams of InfoSec professionals. The beauty however, is that adopting a high awareness people approach is cheap.

MASS VOLUME

Dealing with the deluge of data in fixed income

It's essentially a fact of life: a massive volume of data flows through fixed income trading desks every day. But, despite the increasing influx of data, most portfolio managers still rely on manual, outdated methods of extracting intelligence from the growing supply of information.

Many firms in the financial markets sector still grapple with manual, Microsoft Excel-based spreadsheets, lagging behind their peers who use streamlined digital processes to collect, aggregate and analyze data in an efficient and, therefore, revenue-enhancing way. So much so, that as Bloomberg recently noted, data scientists for fixed income markets are becoming one of the in-demand jobs in financial services, with one trader noting that "the fixed income investment industry is far behind the curve in terms of data."

The sheer volume and complexity of data inputs managers need is unwieldy, slow and limited in scope. The amount of market data itself continues to skyrocket – derivatives are commonplace, while many fixed income benchmarks have more than 20,000 holdings (compared to 500 in the S&P 500 index). This fact alone makes manual calculations of data points, like relative attribution, very difficult at best and nearly impossible at worst. In fact, in our surveys with clients, managing the volume of the data is routinely ranked as a top challenge.

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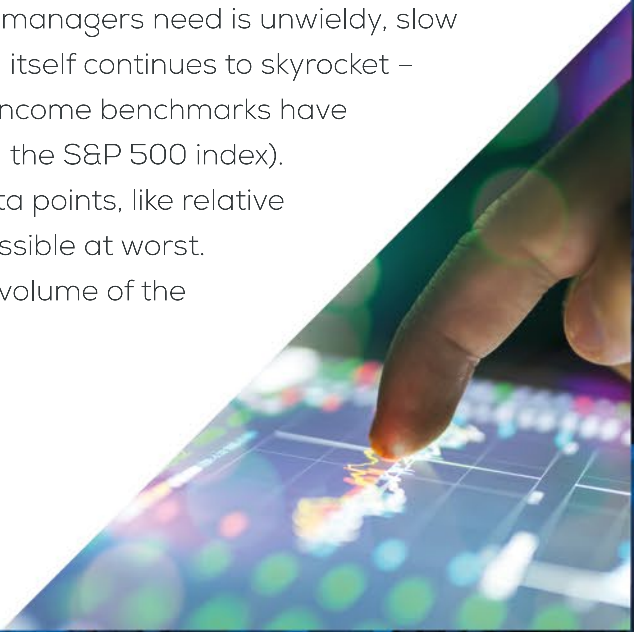

Data analytics technology has advanced to the point where it can now effectively support fixed income managers' ability to consume large amounts of data in an automated fashion.

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