Are you ready to rise?

The Hunt for Growth Across the Sell Side: Outlook for Risk and Compliance

THE FIS™ READINESS REPORT
Introduction

Sell-side risk and compliance executives have borne the brunt of the work to ensure that their organizations are fit for purpose in today’s demanding regulatory climate and unpredictable market environment. These executives must continue to play a central role in their institutions’ drive for growth. Armed with better access to data and more advanced technology, the onus is on these professionals to enhance compliance efficiency and to deliver faster and deeper insights across multiple risk categories – including credit, investment, market, operational and cyber risk.

At the same time, they must enable their institutions to achieve a more holistic view of risk. Only by strengthening these capabilities can the risk and compliance function fully support their institutions in the pursuit of their growth ambitions.

Our research, based on a survey of 1,042 senior-level decision-makers (see About the research), reveals key insights about how financial services firms must now rethink their operating models to position themselves for growth – and what the industry’s leaders are doing to set themselves apart.

Its message is clear: firms that are closest to achieving operational excellence across the front, middle and back office are reaping the rewards, growing more rapidly than their rivals.

This report discusses our key findings and learnings from sell-side risk and compliance respondents globally.
Industry outlook: The risk and compliance perspective

1. Risk and compliance executives are focused on a broad range of threats, each of which could derail their organizations’ growth ambitions.

No single issue dominates the agenda for risk and compliance executives as they survey the potential threats to their organizations over the next three to five years. Almost a third (32 percent) cite the disruptive threat posed by new market entrants as one of their top three concerns, while 31 percent point to the risk of increasing numbers of countries adopting protectionist policies, and 27 percent say political shifts and accompanying policy changes are a cause for concern.

Risk and compliance executives are also more concerned about the risk posed by cybersecurity (cited as a top-three fear by 25 percent) than executives across all functions (20 percent).

In terms of growth priorities, risk and compliance executives rate improving operating margins, enhancing investment performance and acquiring customers as the top objectives for their organizations over the next 12 months, with each of these goals ranked as a top-three priority.

More than half these executives (58 percent) are confident their organizations will achieve their growth targets, showing slightly more optimism than executives overall (53 percent).

Figure 1. Key threats to growth over the next 3 – 5 years

<table>
<thead>
<tr>
<th>Threat</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disruptive new market entrants</td>
<td>33%</td>
</tr>
<tr>
<td>Countries implementing protectionist policies</td>
<td>31%</td>
</tr>
<tr>
<td>Divergence in central bank interest rates</td>
<td>27%</td>
</tr>
<tr>
<td>Political outlook in my key market(s)</td>
<td>27%</td>
</tr>
<tr>
<td>Brexit - the U.K. leaving the European Union</td>
<td>25%</td>
</tr>
<tr>
<td>Cybersecurity</td>
<td>25%</td>
</tr>
<tr>
<td>Government spending policy in my key market(s)</td>
<td>24%</td>
</tr>
<tr>
<td>Projected economic growth in my key market(s)</td>
<td>22%</td>
</tr>
<tr>
<td>Tax policy in my key market(s)</td>
<td>22%</td>
</tr>
<tr>
<td>Emerging technologies</td>
<td>20%</td>
</tr>
<tr>
<td>Fee pressure</td>
<td>16%</td>
</tr>
</tbody>
</table>

The FIS™ Readiness Report: The Hunt for Growth | Industry Outlook
2. Risk and compliance executives are gloomier than other functions about the regulatory environment.

Only 33 percent of risk and compliance executives believe that the regulatory outlook in their key markets has improved for the next 12 months, versus 44 percent of all respondents.

More than two-thirds (71 percent) of risk and compliance executives believe regulation will remain a significant hindrance to their businesses over the next 12 months, compared to 59 percent of all executives surveyed.

3. Many risk and compliance executives believe their risk management capabilities are in good shape, but cybersecurity is seen as a particular area of weakness.

At least three-quarters of risk and compliance executives describe their capabilities across regulatory and compliance risk management, operational risk management, credit risk management and market risk management as somewhat or very strong. Within this, 40 percent indicate they are very strong on credit risk management. This is unsurprising given the huge resources that sell-side firms have thrown at these areas since the financial crisis.

However, there is less confidence in their liquidity risk management capabilities, where one-third of institutions are not confident that their capability is strong.

The telling admission, however, is that only 58 percent of risk and compliance executives describe their cyber risk management as strong; therefore 42 percent are not confident that their cyber defenses are yet where they need to be.

4. The trend toward multi-asset investment solutions is presenting risk and compliance executives with new headaches.

Risk and compliance executives have concerns around the development of multi-asset strategies. Overall, 79 percent think it’s important they respond to this trend, but nearly 38 percent are not confident that they have the liquidity risk management capabilities to fully support this. They are also more concerned about operational risk management than executives as a whole, suggesting that those with immediate responsibility for risk are more nervous about multi-asset strategies.
Many risk and compliance executives are concerned that their organizations lack the technology capabilities to realize their growth potential.

More than half (53 percent) of risk and compliance executives say their current technological capabilities are not strong enough to fully support their growth plans, compared to 48 percent of executives overall.

Some 38 percent say the same of their operational capabilities, though this is lower than the 46 percent seen across the entire financial services industry.
Risk and compliance executives are more concerned that technology investment benefits their regulatory reporting activity.

Almost a third (31 percent) of risk and compliance executives cite the opportunity to manage regulatory compliance more effectively as one of three key benefits their organization is seeking from technology investment over the next 12 months, versus just 23 percent of all executives surveyed. They’d also like to improve the customer experience (38 percent) and reduce costs (36 percent).

In common with the whole sample, risk and compliance executives are most likely to cite the middle office as the area in greatest need of IT infrastructure strengthening, with 46 percent agreeing.

Figure 4. Benefits sought from technology investment

<table>
<thead>
<tr>
<th>Benefit</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improve the customer experience</td>
<td>38%</td>
</tr>
<tr>
<td>Reduce operating costs</td>
<td>36%</td>
</tr>
<tr>
<td>Manage regulatory compliance more effectively</td>
<td>31%</td>
</tr>
<tr>
<td>Improve data analysis capabilities for business users</td>
<td>29%</td>
</tr>
<tr>
<td>Reduce size/complexity of IT architecture</td>
<td>24%</td>
</tr>
<tr>
<td>Offer new products and services</td>
<td>24%</td>
</tr>
<tr>
<td>Enhance cybersecurity</td>
<td>24%</td>
</tr>
<tr>
<td>Compete with non-traditional/new market entrants</td>
<td>24%</td>
</tr>
<tr>
<td>Speed up time to take products to market</td>
<td>22%</td>
</tr>
<tr>
<td>Increase revenue</td>
<td>20%</td>
</tr>
<tr>
<td>Improve business innovation</td>
<td>20%</td>
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</tbody>
</table>
We view these six operational principles as critical for growth in the years ahead:

**Automation:**
The level of process automation across the transaction lifecycle; artificial intelligence (AI) in combination with exception-based workflow is the highest parameter.

**Data management:**
Data management capability, including integration of data across the organization, predictive analytics and visualization.

**Emerging technology:**
Maturity of emerging technology adoption across mobile, AI and distributed ledger solutions.

**Digital innovation:**
Level of activity directed at strengthening digital innovation and propensity of organizational culture for innovation.

**Customer experience:**
Performance across customer service metrics, including customization of products and services, mobile delivery, responsiveness and transparency.

**Talent:**
Level of digital competencies in data analytics, software development, digital distribution and digital transformation.

This section of the report examines the four operational principles of our Readiness Index that are shaping the risk and compliance outlook for the sell side. It outlines the areas that sell-side institutions need to prioritize to help drive future growth and highlights how leading institutions are adapting their strategies.
Risk and compliance executives are more likely to worry that their organization’s data management capabilities are not yet up to scratch.

While 60 percent of risk and compliance executives say their organizations have effectively unified data sources across the business (in line with the 63 percent of executives overall who say the same), only 49 percent rate their ability to combine external data with internal organizational data as effective (versus 61 percent overall).

There is a similar gap on visualizing and simplifying complex data; it’s seen as effective by 51 percent of risk and compliance executives, compared to 62 percent overall.

“There’s a heavy lift to bring various data sets together to meet the challenges associated with new regulatory reporting standards. But whereas 15 years ago, that could have meant a two-year project with very high costs, the technologies now available within the cloud can enable you to access your data, classify it and start to draw out valuable conclusions at a much faster rate,” says Peter Giordano, managing director and head of trading room operations at Oppenheimer & Co.

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- Peter Giordano, Oppenheimer & Co.

Figure 5. Data management capability
Risk and compliance executives believe emerging technologies can play a crucial role in supporting growth and strengthening risk management.

These executives see clearing and settlement and collateral management as the most likely business applications for their institutions’ blockchain development, cited by 44 percent and 38 percent, respectively. But 34 percent and 25 percent, respectively, also point to regulatory reporting and know your customer (KYC)/anti-money laundering (AML) compliance, two areas that are central to their function.

Similarly, 46 percent of risk and compliance executives see regulatory and compliance work as a key application for AI development, while 37 percent cite risk management and 43 percent cite automation of operations.

“Risk and compliance professionals need to be engaged as machine learning solutions are developed,” says a senior compliance manager at a large U.S. investment bank. “If intelligent systems are seeking out the most efficient trading solution, for instance, there is a risk that it may not be the best solution for the ultimate customer or the best from a compliance or regulatory perspective.”

“Risk and compliance professionals need to be engaged as machine learning solutions are developed.”
- Senior compliance manager, large U.S. investment bank
Risk and compliance executives are more concerned about cyber and regulatory risk standing in the way of digital innovation; 40 percent and 36 percent, respectively, point to these hurdles. So they have a key role to play in helping their organizations to innovate.

The difficulty of working with complex legacy IT systems is the other big barrier to innovation for risk and compliance executives, with 40 percent highlighting this problem.

Risk and compliance executives say cyber risk and complex legacy IT systems are the biggest barriers to digital innovation.

Figure 6. Barriers to digital innovation

- Cybersecurity risk: 40%
- Complex legacy IT systems/inadequate technology: 40%
- Regulatory risk: 36%
- Talent gaps: 18%
- Lack of available capital to invest: 15%
- Organizational culture: 13%
- Insufficient organizational understanding of digital issues: 13%
- Internal silos/lack of internal collaboration: 11%
- Insufficient support from senior leadership: 7%
- Job losses: 7%
Assessing the talent mix

While risk and compliance executives believe a broad range of digital skills will be important to growth, they worry about talent gaps today.

Like other executives, those in risk and compliance see digital skills as crucial drivers of their institutions’ growth objectives: nearly two-thirds (65 percent) say big data and analytics expertise will be a growth enabler over the next 12 months, while almost as many (64 percent) point to the need for digital change skills, and 56 percent cite software development as a key area.

In many cases, risk and compliance executives are especially worried about skills shortages. In those key areas, only 44 percent see their in-house big data and analytics talent as good (versus 48 percent of executives overall), 58 percent say in-house digital change talent is good (60 percent overall), and 44 percent rate in-house software development as good (60 percent overall).

Despite the importance attached to AI (see page 10), only 31 percent of risk and compliance executives rate their in-house talent in this area as good.

Only 44% see their in-house big data analytics talent as good.

Figure 7. Importance of skills for growth

- Big data analytics/data science expertise: 65%
- Digital change/digital transformation expertise: 64%
- Software development/programming expertise: 56%
- Algorithmic and automated trading developers: 55%
- Digital distribution/delivery expertise: 49%
- Artificial intelligence/robotics expertise: 44%
- Distributed ledger technology expertise: 42%
Sell-side risk and compliance executives will play an integral role in their institutions’ pursuit of growth over the coming years. Regulatory complexity is a permanent feature of operating in the market, and it brings not just more burdensome reporting requirements but also a need to understand risk exposures at deeper levels than ever before.

At the same time, risk executives can add fresh value for the business by pairing new analytics technologies with more sophisticated ways of modelling risk, helping senior leaders to make better-informed strategic decisions.

These goals are within reach, but risk and compliance executives can only rise to the challenge if their institutions are prepared to strengthen six key areas of their operating model.
1. DEEPEN AUTOMATION
Institutions must respond to efficiency and data needs by increasing automation across more areas of trading and back-office operations – but also areas of low automation, such as middle-office activities. They need to overlay workflow onto exception management before they can implement AI and machine learning solutions.

2. EXCEL WITH DATA
At a minimum, firms need to draw a line under fragmented systems, moving to a single source of truth on data across the organization. But this is just the first step of a multi-tiered approach. Customized real-time data must be available to business users, while advanced AI solutions should be layered on top to create better predictive insights.

3. ADD VALUE WITH EMERGING TECHNOLOGY
Senior leaders must take a longer-term outlook on embracing enabling technologies such as AI and blockchain to re-engineer risk and compliance activity and to create a compelling new value proposition for customers.

4. ACCELERATE INNOVATION
Responding to regulatory requirements, cyber risk and complex legacy IT is stifling progress on digital innovation. Institutions must find ways to overcome these issues to expedite the process. Teaming up with innovative third parties – and finding ways to make these collaborations more effective – will be an increasingly important part of the solution.

5. REIMAGINE THE CUSTOMER EXPERIENCE
Finding new digitally-driven mechanisms for engaging customers will be a critical driver of growth in the years ahead. Digital and mobile access to services is the industry’s weakest area of customer servicing. New offerings will need to provide greater access to real-time information not only via online and mobile but through direct market access too, such as enabling trading activity.

6. RECRUIT THE SPECIALIST TALENT
The new operating model for growth will be ineffective unless the financial services workforce is re-evaluated. In particular, this means putting new skills such as data science specialists in place, enabling them to work in close collaboration with the front office to drive more value and better outcomes for customers.

WHAT’S YOUR GROWTH READINESS?
ARE YOU READY TO RISE?

Benchmark your growth readiness
FISReadinessReport.com
Appendix

About the research

Survey
Between March and May 2017, in collaboration with Longitude Research, we conducted a survey of 420 senior-level respondents across the sell side of the financial services market as part of a larger survey of 1,042 executives.

Interviews
We also conducted more than 20 in-depth qualitative interviews with industry leaders (see Acknowledgments below for full details).

SECTORS

- Broker-dealers: 37%
- Commercial and investment banks: 63%

SENIORITY

- C-suite: 28%
- Head of business unit/director-level: 72%

REGIONS

- APAC: 22%
- LAMEA: 22%
- North America: 29%
- Europe: 27%

FUNCTIONS

- Trading and investment: 23%
- Risk and compliance: 19%
- Operations: 18%
- Finance and treasury: 13%
- Sales: 11%
- Other: 9%
- IT: 6%

CHARTS MAY NOT ADD UP TO 100 PERCENT DUE TO ROUNDED VALUES.
# Methodology – The FIS Readiness Index

## About
The Readiness Index is based on a survey of 1,042 financial services executives around the world and across different business areas (see About the research).

It collates and measures companies’ self-assessed performance in six operational areas that FIS has identified as being representative of how firms achieve growth:

- Automation
- Data management
- Emerging technology
- Talent
- Customer experience
- Digital innovation

## Scoring
The majority of questions included in the index asked executives to rank their businesses on a scale of 1 to 5, where 5 = highly effective-active, etc., and 1 = highly ineffective (respondents that ticked “don’t know” were given a neutral score of 3).

Several questions, such as those related to innovation, asked respondents to choose from a range of activities or strategies that their companies may be involved in, such as M&A, third-party collaborations or incubator programs. For these questions, companies undertaking at least five activities were awarded a top score, with the remaining responses scaled accordingly.

## Building the FIS Readiness Index
The question scores were aggregated for each individual respondent, first to a category score and then overall. To allow for more refined insights, both category and overall scores were placed on a scale of 1 to 10, where 10 is best. As shown above, as we believe each area accords equal merit, the categories each receive an equal weighting in the Index.

## Sell-side Readiness Leaders
Banks provided 25 percent of respondents in the overall survey yet constituted 29 percent of the Readiness Leader group, showing they are over-represented in the leader group relative to their frequency in the main sample.

Conversely, broker-dealers provided 15 percent of respondents but constituted 12 percent, showing they are under-represented.

### Questions
For each category, executives were asked to respond to a series of self-assessment questions about their company’s performance within each area (for example, how well their company performs in unifying data sources across the organization, or the extent to which it offers customers a tailored service). The questions were tailored to different types of business across the buy and sell side.
Acknowledgements
We thank all of those who participated in our interviews, including:
Peter Giordano, managing director and head of trading room operations at Oppenheimer & Co.

About FIS
FIS is a global leader in financial services technology, with a focus on retail and institutional banking, payments, asset and wealth management, risk and compliance, consulting and outsourcing solutions. Through the depth and breadth of our solutions portfolio, global capabilities and domain expertise, FIS serves more than 20,000 clients in over 130 countries. Headquartered in Jacksonville, Florida, FIS employs more than 55,000 people worldwide and holds leadership positions in payment processing, financial software and banking solutions. Providing software, services and outsourcing of the technology that empowers the financial world, FIS is a Fortune 500 company and is a member of Standard & Poor’s 500® Index. For more information about FIS, visit www.fisglobal.com