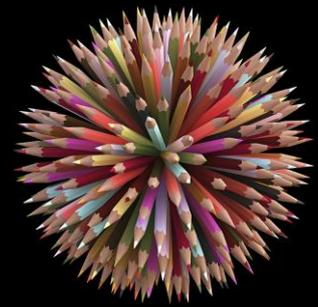


Outsourcing the Traditional Trading Desk

A Modern Solution for Asset Managers



*The asset and wealth management industry will grow faster in Asia Pacific than other regions. By 2025, assets under management (AUM) are expected to double to **US\$29.6trn** from **\$15.1trn in 2017** - PricewaterhouseCoopers (PwC) predicts in its latest report –*

‘Asset and Wealth Management 2025: The Asia Awakening’.

By 2025, the Asia Pacific region is expected to overtake the more developed regions of Europe and North America as the largest asset and wealth management industry¹. The growth will be driven mainly by retail mutual funds and sovereign wealth funds, as well as the escalating wealth of the mass affluent and high net worth individuals. Assets of retail mutual funds are forecast to more than double to **\$11.9trn in 2025 from \$5.5trn in 2017**. Assets of sovereign wealth funds are expected to double to **\$5.7trn from \$2.8trn over the same period**.

Whilst this forecast paints a pretty picture of growth and opportunity, it's underscored by the reality of what's happening right now on a global scale. Being an asset manager in today's market is highly challenging and no easy feat.

Asset owners, including pension, superannuation and sovereign wealth funds are faced with shrinking margins, increased fee pressure, operational challenges, increased regulation and compliance requirements, rapid technology change and a search for greater returns in a persistently low-yield environment.

What are the trends?

Challenging investment environment

Today's investment environment is challenging. We are experiencing persistently low interest rates, increased volatility in market conditions due to geo-political factors, aging populations and active asset managers are routinely under-performing their benchmarks after fees. This is driving asset owners to diversify their investment strategies to mitigate the impact of these trends and making asset managers rethink their internal operational structures to look for cost savings².

Regulatory change and the need for new technology

Regulation is a significant cost for fund managers. With regulatory requirements evolving, asset managers are seeking expertise in interpreting and implementing these regulations. Legal, compliance and the need to upgrade or

incorporate new technology has costs associated with it, which fund managers bear the brunt of.

Increased adoption of ESG and alternative assets

Asset managers in the Asia Pacific region are increasingly shifting their portfolios to international and private markets³. There is also a growing demand for alternative assets and Responsible Investing (RI) strategies, such as Environmental, Social and Governance (ESG) driven investments. To support this shift, funds are actively going external to seek specialised expertise in managing these products and asset classes and the ability to hedge associated FX exposures. Conducted internally, exposure management through currency overlays can be costly, due to maintaining trade simulation and portfolio analytics systems. These capabilities don't really achieve a competitive differentiation and these tools can be accessed via outsourcing.

¹ <https://www.pwc.com.au/asset-management/2018-awm-asia-2025-report-31jan19.pdf>

² Outsourced trading – The Hedge Fund Journal: <https://thehedgefundjournal.com/outsourcing-trading/>

³ Chares River Development: <https://www.crd.com/apac-asset-owners-viewpoints>

Trading cost and opportunity cost

In a holistic sense the financial cost associated with hiring, building, retaining and managing a trading desk is significant. Outsourcing a trading desk to a trusted third party can have huge cost-savings, allowing asset managers to invest elsewhere in their business. There is also an opportunity cost associated with the execution of deals,

particularly in large regional asset managers – which is time taken away from their core competency of picking stock.

These market trends and challenges asset managers face, is creating a strong appetite for outsourcing the front-office trading desk. A fundamental re-think of operating models is occurring, with funds determining the optimal mix of outsourcing versus insourcing to suit their organisation.

At Russell Investments, we help clients stay ahead of the pressures falling on buy-side trading desks by creating an efficient, cost-effective and compliant execution solution. By combining a clients' internal resources with Russell Investments' global capabilities, asset managers can access specialist expertise. This allows for greater portfolio control, reduced costs, reduced risk and can enhance returns.

Here are two examples where Russell Investments has tailored a bespoke solution to meet individual client needs.

Case study 1

Challenge:

One of Australia's largest superannuation funds was seeking to establish an internal fixed income trading capability; however, such a decision requires significant future planning, technological infrastructure development; complex compliance approval frameworks and systems and the establishment of a team of professionals. While the organisation made the decision to pursue the strategy, it required several buildouts and approvals to proceed internally before they were ready to run the mandate independently. The team had two options:

1. Continue to run separate investment management mandates across the suite of fixed income investment options and wait until internal resources were built.
2. Seek out a provider who could deliver a global trading platform to meet their needs.

Solution:

Russell Investments delivered the client an outsourced global trading desk and compliance approval framework, a customised solution that was tailored to the clients' requirements. This allowed the client to satisfy internal constituents for the approval of direct investment, leveraging Russell Investments as their directed investment manager.

The solution that was mutually designed, allowed for the following critical components to occur:

1. the client was able to implement between the groups, the streamlined exchange of information between investment systems and relevant parties while minimising time to market.
2. the client was able to execute a range of investments with varying complexity. Some of the specific solutions

that were utilised were: to enable the clients' systems to exchange information with the trading desk directly and provide the following process to occur:

- Client instruction of daily trades via a secure FTP trade communication protocol
- Russell Investments acceptance, review, and compliance determination
- Russell Investments confirmation of instructed values and quantities of trades to be executed including any special instructions
- A full suite of investment products was traded including global fixed income, spot and forward FX, futures, and interest rate swaps
- Russell Investments conducted daily reconciliation and reporting of positions to client and custodian.

Russell Investments provided a global trading desk for 22 months trading across the full suite of investment solutions including: swaps, futures, spot and forward currencies, and global fixed income.

Outcome:

The client was able to leverage an independent global trading desk for nearly 2 years ensuring all orders were executed as instructed. The greater trading capability enabled the client to evolve their internal investment capabilities and have more targeted exposures in the global fixed income asset class rather than being tied to an external asset manager's views for this portion of the portfolio. The fund was able to gain investment fee savings over the tenure of the mandate resulting in a material savings to the fund and investors.

Case study 2

Challenge:

The client was the first in the industry to implement a new investment structure. The new strategy involved the underlying investment managers providing paper portfolios to an investment adviser, who in turn would provide Russell Investments investment instructions. The timing of the trades in the global markets were critical to match the underlying investment managers as well as producing multi venue trade executions and transaction cost analysis reporting.

The client also approached Russell Investments, to implement their asset allocation strategy using derivatives which were rebalanced on a monthly basis. The derivatives would rebalance the fund back to its benchmark weights. Cash management facilities were also required to be performed. Excess cash was managed and invested in highly rated securities.

Outcome:

Through successful partnering with Russell Investments, the client was able to leverage an independent global trading desk for nearly 7 years ensuring all orders were executed as instructed. The greater trading capability enabled the client to gain greater returns on their portfolio. The fund was also able to gain investment fee savings over the tenure of the mandate resulting in material savings. All regulatory reporting such as DTCC and RG97 was performed.

Each client is unique, and Russell Investments' has a suite of services designed to support in-house investment teams which can be customised in combination or delivered as discreet solutions to tackle individual investment challenges. Our service includes:

- **Transition Management:** Helping manage risks and investment performance when restructuring portfolios or asset classes.
- **Outsourced Trading:** Gain superior access to a deeper set of liquidity, minimising market impact and contributing to improved trading performance through our 24-hour trading desk covering equity, fixed income, foreign exchange and derivatives.
- **Overlay Services:** Control investment exposures and carefully manage risks with a fast and flexible overlay strategy.
- **Currency Management:** Manage Foreign Exchange trading costs and currency risk management. Draw upon our currency investment team and FX trading specialists to help create a solution to efficiently manage your currency exposures.

Why Russell Investments?

RUSSELL INVESTMENTS IN NUMBERS



24 Hour

Trading capability



90+ Global

Investment professionals



35 Years

Experience in implementation services



USD 2.6 Trillion

Traded in 2018



100+ Markets

Available to trade in



USD 1.01 Trillion

Foreign exchange traded
in 2018

Range of markets

USD 2.95BN

USD 11.58BN

USD 4.91BN



Americas

6 Countries



APAC

10 Countries



EMEA

21 Countries



37

Countries



25

Portfolios



62

Brokers

Outsourced trading is likely to become common practice in the future. Compliance was once seen as a function that had to be internalised by asset managers along with front-office dealing desks – but times are changing.

Outsourcing trading execution creates an opportunity to reduce financial costs, reduce risk, manage regulatory compliance and enhance transparency and operational efficiency. By outsourcing trade execution, asset managers can focus on their core capabilities, their clients and their value proposition which positions them more competitively in the battle for alpha.

For more information

Call Russell Investments at **+612 9229 5111** or visit russellinvestments.com.au

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