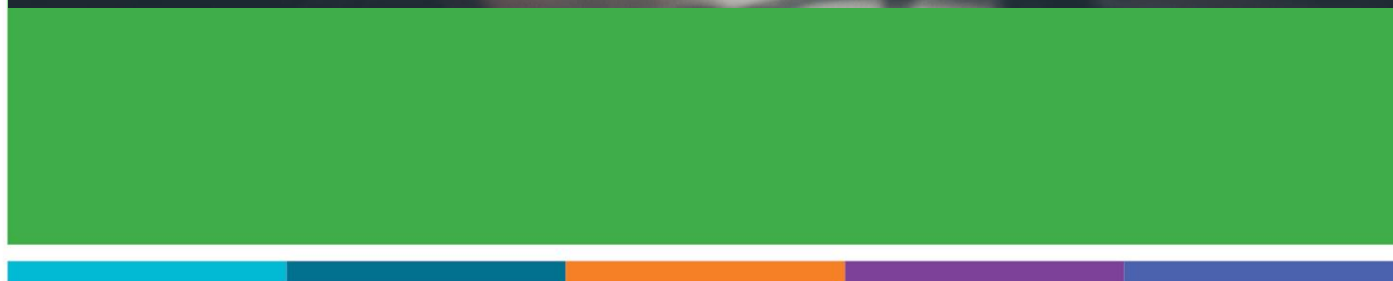


Asset Servicing 2030

Irish Funds FinTech Working Group

October 2020



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Introduction

This report outlines the challenges facing asset servicers as we move into the new decade, considers how firms can avail of the new wave of technologies and explores how Fintech firms can survive and thrive in this new world.

Where are we now?

The Irish Funds Industry Association is the representative body for the international investment fund community in Ireland. Founded in 1991, Irish Funds represents fund managers, depositaries, administrators, transfer agents, professional advisory firms and other specialist firms involved in the international fund services industry in Ireland.

Irish Funds' has more than 150 members which service or manage in excess of 14,000 funds with a net asset value of €5.2 trillion, of which more than €3 trillion are in Irish domiciled funds. Irish Funds objective is to support and complement the development of the international funds industry in Ireland, ensuring Ireland continues to be a location of choice for the domiciling and servicing of investment funds.

Irish domiciled funds have investors from 90+ countries across Europe, the Americas, Asia and the Pacific, the Middle East and Africa. Over 900 fund promoters from more than 50 countries have funds domiciled or serviced in Ireland. There are 38,000 people employed in the financial services industry and in excess of 16,000 directly in investment funds industry.

Over 500 fund promoters from across the globe have used Ireland to set up regulated investment funds distributed to investors and savers throughout the world. Fund promoters can rely on expert service supported by 16,000 skilled employees across the entire service provider community, including fund administrators, trustees, legal advisers, Fund Auditors, tax advisers, compliance, listing and other industry specialists.

Why focus on asset servicers?

Ireland has a global reputation for providing asset servicing for investment firms from around the globe and while there is a lot of focus on the impact of market changes on investment managers there is less focus on the specialist firms that support these investment managers.



What challenges face Asset Servicing firms in 2020?

Asset Servicers operate in an industry which continues to face complex challenges both for themselves and their clients:

Cost Pressures	Continuing migration of investments to passive funds and ETFs, and reduction of commissions and fees to investment managers creates new growth opportunities for service providers who can deliver quality services more efficiently.
Increasing Investor Sophistication	Increased Investor sophistication for new products and services in the search for higher returns and diversification; implies increasing use of a wider range of investments including alternatives, infrastructure assets and exotic assets.
Client Service and Personalisation	Investors demanding more personalized services from their suppliers: including real time access to their holdings & performance data with instant allocation of capital all provided through multiple platforms and increasingly via mobile devices.
Regulation	Drives huge demands on investment firms including the tail end of Mifid2, ESG, SFTR etc all require development and change resources.
Alternatives and the hunt for Alpha	The combination of low interest rate environment, low investment returns and Increasing investor demand is leading to an increase in demand for access to alternative assets to increase returns and decrease risk.

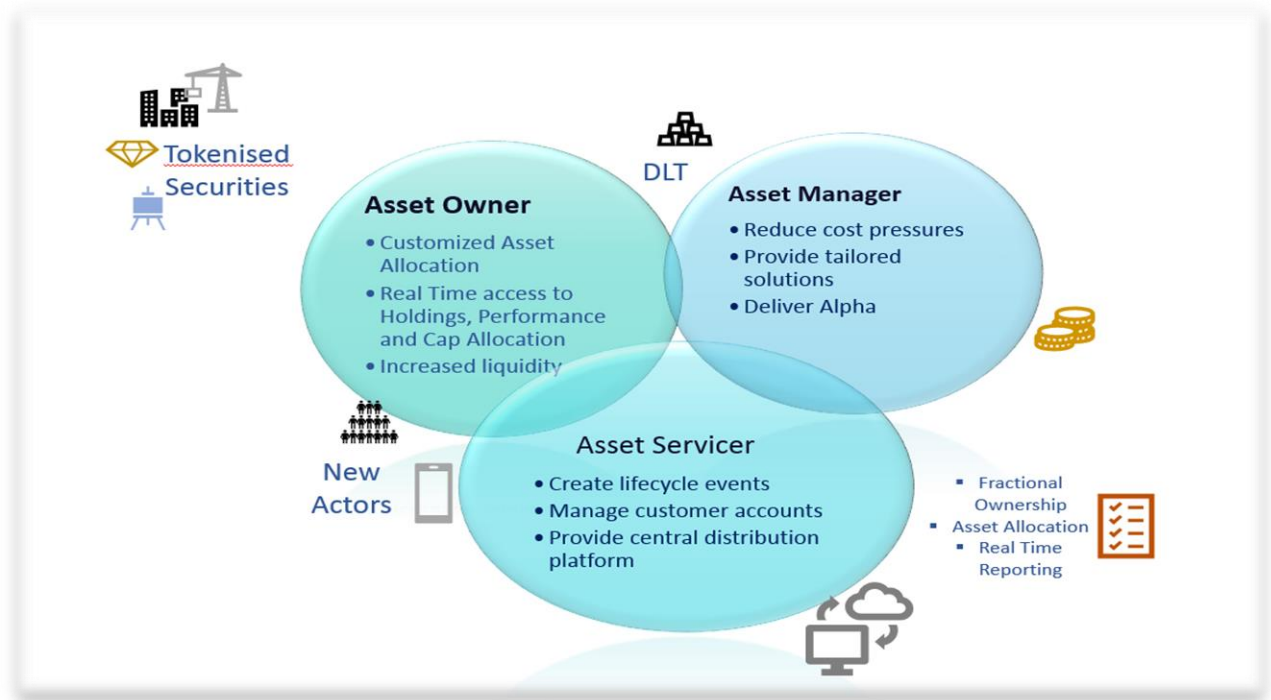
What does this mean for Asset Servicers?

As Investors demand more personalized investment opportunities, the emergence of new technologies such as Big Data and Distributed Ledger platforms enable firms tailor investment solutions and facilitate direct asset allocation to investors more cost effectively than through traditional fund structures.

This shift is driving asset managers, and the asset servicing firms that support them to evaluate how asset tokenization might address the pressures they face. A token is a representation of the legal title to an asset recorded on a distributed ledger, or similarly immutable record. Purchase and transfer of a token is a purely electronic process and whilst this is not new, tokenization provides for significantly simpler, faster and less costly purchase and transfers than occurs in the traditional securities market today.

The concept of a tokenized asset certainly solves the challenge of faster, easier and greater access to a diversified range of assets from fine wines to infrastructure and by leveraging Distributed Ledger Platforms, the facility now exists to support the micro allocation of any real world asset through a tokenised economy.





The operational and technical disruption which tokenisation presents to traditional Asset Servicers will be significant. They must consider how to future proof their business models and evaluate investment in technology solutions to prepare for a new era in asset allocation.

The impact to legacy operating models and infrastructure as well as understanding the role they want to play and their position in the value chain will be key in ensuring they retain market share in this space. The question right now is how quickly they will need to react to this shift and the pace of uptake that might occur in the market.

Operational & Technical Considerations for the Asset Servicers in a Tokenized Market

Settlement & Liquidity Processing	<ul style="list-style-type: none"> ▪ Evaluation required to manage real time settlements and the requirements for liquidity and collateral management ▪ Regulatory & jurisdictional considerations
Internal Data Management	<ul style="list-style-type: none"> ▪ The industry requires delivery of real time data faster and more securely, expand outsourcing solutions and deliver value-add services demanded by an ever-changing investor demographic, firms must have a clearly defined data strategy combined with robust data governance and security protocols established



<p>External data Distributed Ledger Technology -(DLT)</p>	<ul style="list-style-type: none"> ▪ The market will move towards an environment supporting seamless sharing of data on a real time basis enabled by industry based DLT. DLT offers the prospect of fund managers, distributors and asset servicers all contributing to a shared, immutable record of holdings and orders deliver a single version of the truth of all transactions. DLT offers Asset Servicers significant operational benefits but also significant integration challenges: <ul style="list-style-type: none"> ○ Lower cost ○ Lower complexity ○ Removal or errors and reconciliations <p>The opportunity for DLT in funds distribution is so impactful that there are already a number of significant initiatives underway in the European market</p>
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Benefits of Tokenisation

The ability to represent an asset holding in this way has many advantages outlined below. Principally it is around achieving consensus & certainty, removing reconciliation risk which achieves a highly efficient market. New actors will also be necessary to ensure independent governance and control exists on the ownership of assets in the real world and the valuation of same.

Benefit	Description
Fractional Ownership	<ul style="list-style-type: none"> ✓ For example, the ownership of an infrastructure asset such as a toll road or a bridge can be broken down into thousands or millions of fractions to be allocated to individual investors
Flexibility	<ul style="list-style-type: none"> ✓ Allows retail investors to access a wider range of investments than currently available including infrastructure, alternatives and exotics where regulation allows
Liquidity	<ul style="list-style-type: none"> ✓ Using a DLT or similar technology to manage these tokens means you can aggregate, and split holdings as required allowing investors the ability to buy and sell in any size
Certainty	<ul style="list-style-type: none"> ✓ The ability to buy and sell tokens without changing the underlying assets allows investors to access a secondary market for assets, thereby increasing liquidity for these assets ✓ The ability to offer fractional ownership could also dramatically increase liquidity for current illiquid assets such as infrastructure assets by making these available to a wider pool of investors
Security & Resilience	<ul style="list-style-type: none"> ✓ DLT platforms offer the potential to deliver immutable shared records allowing all stakeholders the same visibility to the state of any transactions and holdings ✓ The use of a DLT ensures that all parties have certainty over their positions at any point in time
Total Cost	<ul style="list-style-type: none"> ✓ DLT platforms offer the security of a consensus mechanism to reduce fraud and manual errors ✓ Decentralised platforms such as DLT platforms offer the potential to be highly resilient via the use of multiple nodes rather than single points of failure ✓ Managing the ownership of an asset via a single shared platform means that firms do not need to maintain their own independent records of this data and removes the need to constantly reconcile this data with other parties.



Costs of Tokenisation

While the potential benefits of tokenisation highlight why there is increasing interest in this area there are a number of costs which asset servicers should be mindful of, including:

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| Complexity | <ul style="list-style-type: none"> • Tokenisation will require new platforms and investment to ensure that current levels of asset protection and controls are supported |
| Increased Client Expectations | <ul style="list-style-type: none"> • Tokenisation will be implemented over a period of time, but the availability of real time trading and T+Instant settlement that is associated with tokenized markets means trades may have to be pre-funded and thus could create liquidity constraints. These operational challenges drive changes faster than firms may be able to support. |
| Opportunity for New Competitors | <ul style="list-style-type: none"> • Tokenisation will allow new players with advanced system capabilities to compete for asset servicing business. At present the tokenized market is in its infancy so whilst there is opportunity, it would come with significant investment costs. |

Tokenisation and Innovative Investment Structures

The ability to use a DLT to manage fractional ownership of assets allows for collective investments to work very differently and gives rise to many new potential investment structures including:

Model	Description
Fully Electronic Share Classes	<ul style="list-style-type: none"> i. Like a standard share class today but all distribution is done via the DLT ii. The register is also held on the DLT and facilitates a secondary market of investors buying and selling directly with each other iii. This results in reduce costs and greater liquidity and flexibility for the investor
Illiquid Asset Share Classes	<ul style="list-style-type: none"> i. Like a standard share class today but supports a greater level of illiquid assets ii. Has all the benefits of the fully electronic share class above but gives investors access to a wider range of assets
Managed Direct Holdings	<ul style="list-style-type: none"> i. Removal of the concept of a fund structure giving reduced complexity, cost and liquidity overheads ii. Fund manager determines investment model and the Asset servicer allocates actual asset holdings via tokens to the investor's accounts iii. This is direct investor holdings managed by the fund manager iv. Individual allocation of assets reduces the regulatory overheads on the fund structure v. Has all the benefits of the fully electronic share class, with the access to illiquid assets but with reduced fund overheads



Investor Managed Holdings

- i. Removal of the concept of a fund structure giving reduced complexity, cost and liquidity overheads
- ii. Fund managers publish investment models and the investor allocates sums to this model
- iii. The Asset servicer allocates actual asset holdings via tokens to the investor's accounts
- iv. This is direct investor holdings managed by the fund manager
- v. Individual allocation of assets reduces the regulatory overheads on the fund structure
- vi. Has all the benefits of the fully electronic share class, with the access to illiquid assets but with reduce fund overheads

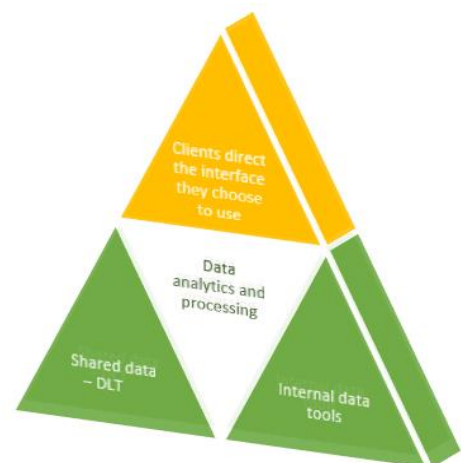
There are technical, legal and regulatory hurdles to be overcome but the benefits of tokenisation are aligned to the core regulatory goals of security and improved investor outcomes, and therefore the concept of tokenisation is gaining momentum in the marketplace.

Conclusion

What does the Asset Servicer of the future look like?

To thrive in this new world the asset servicer of the future must:

- Manage data as a core strategic asset (DLT, AI, Data Management)
- Fully automate processing with real time data delivery
- Support client serving through a range of channels that suit the investor preferences (24/7 access via all mobile devices)
- Be flexible and allow the end investor to customize the interface to suit themselves
- Support the full range of assets required with the same level of service



What does this mean for Asset Servicing in Ireland?

The opportunity for Ireland to lead the transformation of traditional asset servicing functions is clear. The depth of experience amongst the workforce is extensive with deep processing & technical knowledge coupled with a client centric mindset provides a valuable perspective for global organisations to leverage as they build platforms of the future.

Aligned to the Financial Services expertise, Ireland is a recognised leader in ICT (Information, Communications & Technology) with not only large multi nationals based here but also a wealth of homegrown Fintech's who possess the skills to support firms in advancing their data transformation, DLT and cyber security programs.

Academia also plays a key part with many of Irelands University institutions establishing Innovation centres in emerging technology.

Asset Servicing firms will need to survive major changes in the next decade and those that fail to prepare will face fierce competition from new entrants who are establishing the infrastructure to meet the needs of a 24/7 tokenised, digital trading environment.



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