A MEETING OF MINDS

Graham Ray of Deutsche Bank explains about why the funds industry must collaborate to find a way to meet the growing demand for segregated accounts versus omnibus accounts.

THE EUROPEAN INVESTMENT management market is seeing unprecedented demand from investors for individually segregated accounts, rather than the omnibus accounts favoured by service providers for many years. This demand is driven by two themes – transparency and investor protection. Regulators want more insight into the life-cycle of investments and to be able to identify them at all stages, including settlement. Similarly, investors want reassurance that assets will be ring-fenced by settlement providers, such as central securities depositaries (CSDs), so in the event of a default, they can be safely and easily retrieved.

“Deutsche Bank has always offered segregated accounts for our clients and where appropriate taken advantage of the benefits of omnibus accounts at the CSDs,” says Graham Ray, global head of Investor Services Product Management at Deutsche Bank. “But now the trend is evolving whereby clients are looking for a variety of segregated accounts at the CSD level and different component products.”

For the CSDs, this will be a complex task. “Securities service providers have to recognise and reconcile the many to one accounts between segregated and omnibus which requires a robust infrastructure to provide safety and soundness to investors.”

A concurrent development – the introduction of the T2S initiative, a single platform for settling Euro-denominated securities – makes the task all the more challenging. The launch of T2S, now entering its third phase, along with harmonised settlement initiatives like CSDR, has enabled more cross-border investment within Europe and made fund assets more mobile than ever before. For collateral management purposes the mobility of fund assets and other securities is a key benefit, but to provide segregated accounts at all stages in such a cross-border environment is more complex and less cost-efficient, potentially impacting whether collateral is made available via lending programs.

“What has come to the forefront during the journey of T2S is the complexity of the value chain.”

“A competitive landscape provides the marketplace with choice but what has come to the forefront during the journey of T2S is the complexity of the value chain and, with this, the magnitude of operational risks in the process,” says Ray. Consequently, investors will have to weigh up the reassurance of safety and soundness with service providers that have managed custody of assets for years against the possible benefits created by new business models.

Deutsche Bank has developed a number of options for its clients, such as the Account Operator model, which provides a direct settlement link and segregated account structures within a CSD, or an asset servicing only model. “There will not be one account model that fits all clients,” says Ray. “The key is to offer clients a range of options based on existing products and new solutions through collaborations with other providers that make sense in terms of operational efficiency and investor protection and are commercially viable to all parties.”

Greater collaboration between asset servicers and CSDs was not anticipated in the early days of T2S. The changes to the market structure would allow CSDs to become asset servicers and vice versa, and this was expected to herald a new competitive landscape and a blurring of the lines between custodians and infrastructure providers. “A competitive landscape provides the marketplace with choice but what has come to the forefront during the journey of T2S is the complexity of the value chain and, with this, the magnitude of operational risks in the process,” says Ray. Consequently, investors will have to weigh up the reassurance of safety and soundness with service providers that have managed custody of assets for years against the possible benefits created by new business models.

Deutsche Bank has developed a number of options for its clients, such as the Account Operator model, which provides a direct settlement link and segregated account structures within a CSD, or an asset servicing only model. “There will not be one account model that fits all clients,” says Ray. “The key is to offer clients a range of options based on existing products and new solutions through collaborations with other providers that make sense in terms of operational efficiency and investor protection and are commercially viable to all parties.”

The market has recognised there are many components within the transaction life-cycle that add value. For Deutsche Bank it is a case of looking horizontally at the marketplace – across the regulatory landscape, our client base and their demands and our own product portfolio – and finding the future models that fulfil all of those needs.”