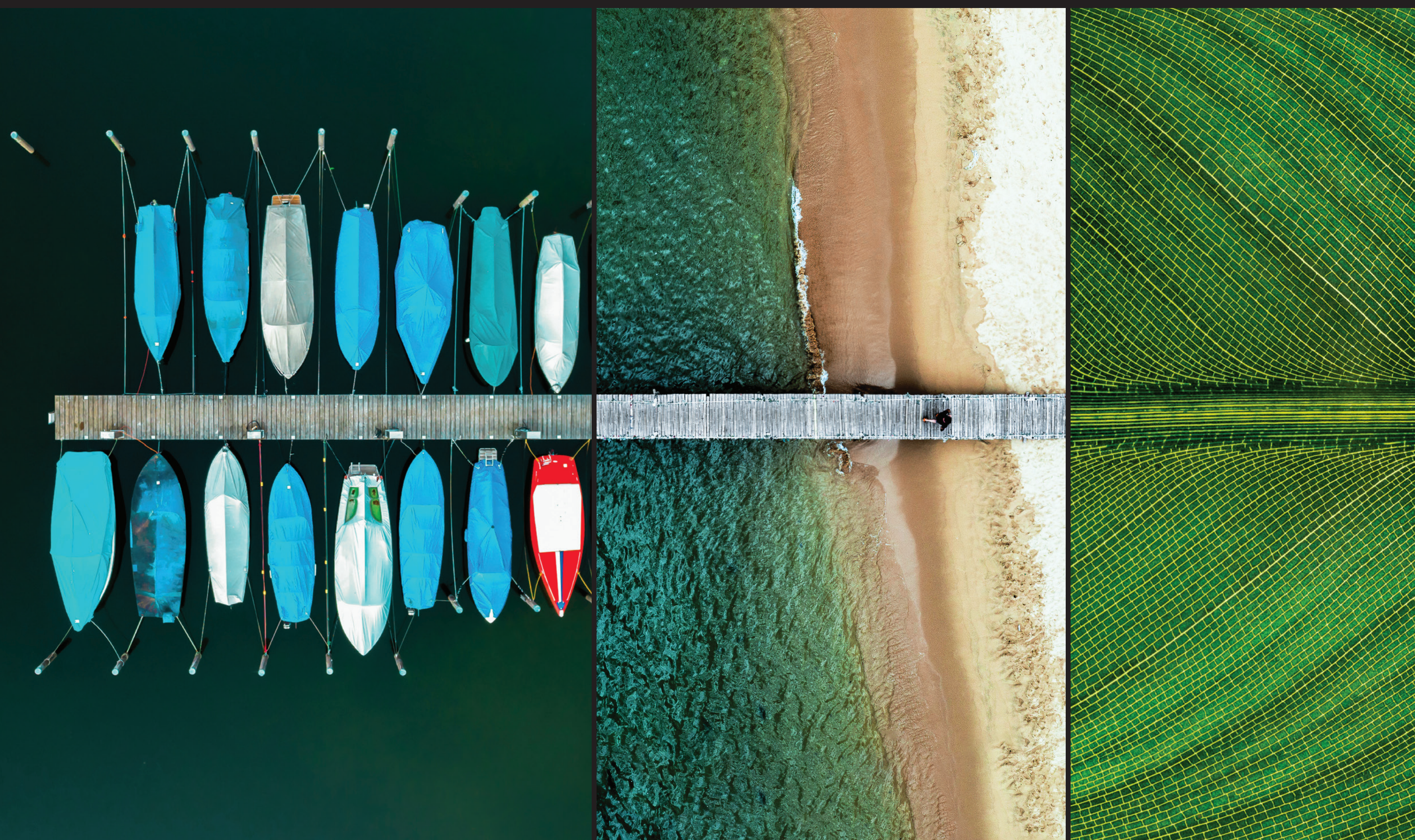
# Demystifying Managed Services

## for Financial Institutions



S&P Global
Market Intelligence

# Executive summary

The rapid evolution of the financial services sector and continued change in market conditions have increased the popularity, viability, and adoption of managed services, a service model that is forecast to reach more than 200% of today's market capital by 2028.

For financial institutions, the growing reliance on managed services is driven by increasing cost pressures and ever-changing regulatory requirements that have created new urgency in the search for solutions that enhance operational efficiency and service quality.

But before taking the leap, business leaders need answers to crucial questions: What do managed services look like today for financial institutions? Which operational challenges can they solve? And how do organizations evaluate their options?

This whitepaper explores the market conditions driving the growth of managed services, the evolution of service models, and top factors to consider when selecting a solution.

**Market factors disrupting buying habits**

- Remote work
- Labor shortages
- Digital transformation
- Customer expectations
- Regulatory pressure
- Workload variability
- Market volatility

**Service innovation transforming the possibilities**

- Smaller engagements
- Technological advancement
- Faster deployment
- Output-based pricing
- Flexible support
- Modular options

**Service models and selection criteria**

- Capacity creation
- Managed process

# Myths and realities

When change is the only constant, financial institutions must seize every advantage to stay relevant and competitive. Yet many ignore managed services because of mistaken assumptions about what it is, who it's for, and what it can do.

For decades, managed services have been a driving force behind the growth of the world's largest banks. As regulatory compliance, onboarding, and operational due diligence became more complex, banks began offloading these processes to service partners to streamline operations and augment internal capabilities on demand.

But for smaller financial market participants, this model has seldom been seen as a viable solution. The size and cost of these engagements and the risk of disruption to Business as Usual (BAU) made managed services an unfeasible option for all but the largest financial entities.

However, the past five years have changed the service landscape dramatically. Advances in technology, the maturation of service delivery models, and a host of new industry pressures have changed the stakes for financial service providers that have made managed services simultaneously more accessible and more urgently needed than ever before.

Yet many smaller financial entities continue to dismiss managed services because the perception has not caught up to reality. Deflected by outdated information and baffled by a maze of complex terminology, financial institutions mistakenly assume this resource is not a fit for their needs or budget.

In this white paper, we'll explore the challenges straining the capacity of service-driven financial organizations, examine the rapid evolution of managed services, and demystify the key terms and concepts that operational decision-makers need to know.

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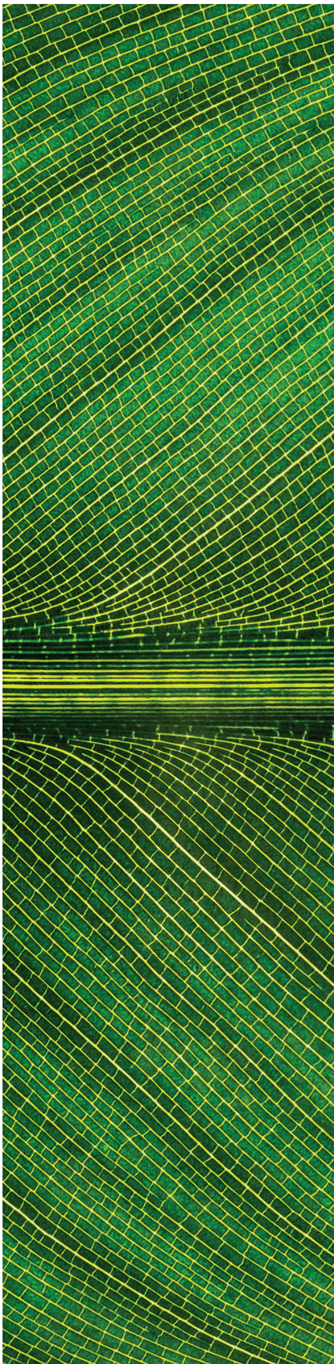
# Market factors disrupt buying habits

Market volatility has increased to levels not seen in more than a decade. Regulatory requirements are proliferating and competition for capital has never been fiercer. We're living in a time of unprecedented change for the financial markets, and of extraordinary opportunity for the financial institutions that help to mobilize and capitalize on them.



**Amid the many rapid developments in the financial markets, the trends outlined below will significantly impact financial organizations in the coming years.**

### Remote work

The shift to remote work created new risk and regulatory operations stress points. The pandemic showed how fragile BAU could be, and how essential it is to safeguard business continuity—even in the face of lockdowns, travel restriction, and other unpredictable events—by finding creative ways to build more resilience, flexibility, and capacity into the system.

### Labor shortages

Talent is more challenging to attract and retain than ever before. The Great Resignation, a wave of early retirements, and a recalibration of work-life balance have all taken their toll. In the European Union, there were 2.6 million job vacancies as of Q1 2021. In the United States, job vacancies consistently passed 10 million between July 2021 and January 2022. And in Asia-Pacific, 85% of employers faced challenges in building their workforce, while 58% turned to a contingent workforce to overcome shortages.

### Digital transformation

As digital transformation matures and the adoption of next-generation technology spreads across the financial service industry, it has raised the stakes in terms of the levels of responsiveness, transparency, and efficiency that are now within the realm of the possible. However, a technology landscape fragmented by tens of thousands of start-ups and niche providers is creating significant challenges for the organizations that must evaluate, select, and integrate these technologies into legacy environments.

We're living in a time of unprecedented change for the financial markets, and of extraordinary opportunity.

## Customer expectations

Technology advances and drastically reduced payment timings in retail banking have transformed the user experience, which has had a knock-on effect on investment banking. Investors and other financial stakeholders demand greater visibility into workflows and data, while expecting the movement of (and access to) assets to be near instant. The ability to deliver secure, transparent, accelerated service is now integral to operational due diligence, signaling to prospective customers and investors that the service organization can be trusted to meet and continuously evolve with market expectations.

## Regulatory pressure

The expectations among global regulators also continue to rise. It took many on the buy-side years to pare average settlement dates from T+3 to T+2. Today, they may be required to go from T+2 to T+1 or even T+0 in a fraction of the time. And given the rapid advancement in processing technologies, the regulatory expectations surrounding these timelines are unlikely to diminish. This is evidenced by upcoming global initiatives such as the European Market Infrastructure Regulation (EMIR) Regulatory Fitness and Performance program (Refit), the Commodity Futures Trading Commission (CFTC) re-write, Australian Securities and Investments Commission (ASIC), and many more.

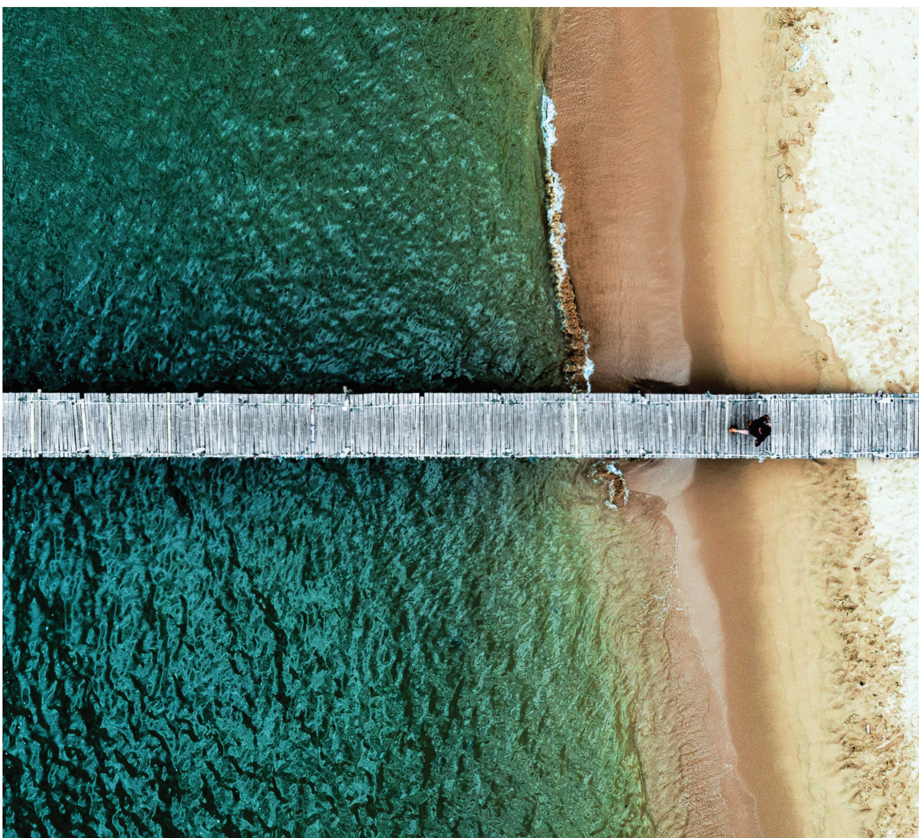
## Workload variability

The workload for financial services has never been consistent, but as regulations become more comprehensive and prescriptive, the effect has been exacerbated. Increasingly, the need to meet high-intensity, cyclical regulatory requirements, such as Know Your Customer (KYC) periodic review or stand up new processes to accommodate a regulatory change, can stretch internal teams far beyond their capacity.

## Market volatility

A volatile market is creating new opportunities for sell-side institutions and the potential for greater returns for the buy-side. By imposing more urgency around the ability to onboard quickly and securely whilst slashing time to market, the past two years have shifted organizational priorities from cost-cutting and austerity to growth mandates and revenue optimization.

As the financial markets enter a period of intense regulatory, operational, and cultural change, the organizations that serve them must adapt and evolve. To do so, they must remain vigilant and open-minded in searching for solutions—including managed services engagements—that can help them anticipate and capitalize on these dramatic and unprecedented changes.



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# Evolved service models transform the possibilities

Managed Services is not a new concept. It has been utilized across multiple sectors as a tool for operational support for decades. It began to gain real traction within the financial services industry in the early 2000s and has been continually evolving ever since, providing a way for global banks to reinvigorate legacy systems and processes. As disruptive fintech, rising transaction volumes, and burgeoning regulatory requirements began to exert pressure, managed services gave tier-one banks an advantage, but left many smaller market participants behind.

However, much has changed in the intervening years. Modular, agile technology and flexible, lightweight service options have made managed services a feasible option for regional banks, investment managers, and even corporates. As a result, the adoption of managed services across the spectrum is accelerating: the global managed services market is projected to grow to $557.10 billion in 2028 (up from $243.33 billion in 2021).

## Six key trends are driving the adoption of managed services across a broader and more diverse portion of the market.

### 1. Smaller engagements

Whereas the scale of service delivery used to require a high head count, new service models enable providers to tailor engagements to the needs (and budgets) of smaller organizations—even those that may need only a fraction of a Full Time Equivalent (FTE) in a specific operational area.

### 2. Technology advancement

The rapid maturation of secure, cloud-based technologies has enabled institutions to locate data centers worldwide and satisfy the most stringent local regulatory laws. As a result, the roadblocks and risks involved in sharing data with managed service providers—or even shifting the responsibility for data management onto an external partner—have been virtually eliminated.

### 3. Faster deployment

Streamlined service models and lightweight, proprietary Software as a Service (SaaS) technologies allow technology-enabled managed service providers to support engagements that ramp up in a fraction of the time, minimizing disruption to BAU, returning quicker wins, and delivering greater long-term value than older service models could promise.

### 4. Output-based pricing

Early service models focused on pricing based on the number of FTEs required to fulfill the service obligation. When sick days, vacations, and alternative coverage arrangements were factored into the equation, the costs became prohibitive for smaller institutions. This incentivization structure also prioritized hours spent over deadlines met, and as a result, output was difficult to manage. As these service models evolved, the emergence of an output-based pricing model offered an accountable and more affordable fixed pricing structure based on guaranteed outcomes rather than headcount.

### 5. Flexible support

The flexible commercial model revolutionized how managed services were priced and how they could be applied to a variable workflow. Responsibility for delivering specific outcomes can now be distributed across a broader managed services team, enabling consistent coverage that can be scaled up or pared back rapidly to cover seasonal or cyclical fluctuations, or even provide coverage for a less-than-full-time role.

### 6. Modular options

Early managed service models required an investment in a complete package of proprietary technology, processes, and services. Today, many service providers break these offerings into modular components that can be combined to provide tailored support with service-only engagements, tech-plus-service options, or business transformation engagements that leverage technology, services, and process enhancement.

# Evaluating the feasibility of managed service models

Managed services have become more accessible to a broader range of financial service providers than ever before, and the need for the operational speed and flexibility they support has never been more urgent.

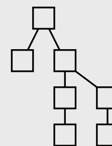
So why have so many small- and mid-sized financial institutions been slow to adopt them?

Some of the reluctance is due to the outdated perception that managed services are a large-scale solution calibrated to the needs of global banks. But the hesitation can also be traced to an understandable confusion around the definitions and labels applied to this service model. "Operational due diligence," "operational support," "outsourcing," "team augmentation"—these and a dozen other terms are all variously used to describe managed services, which cloaks a fairly straightforward offering in unnecessary complications.

While each term correlates to a specific location strategy, technology usage, and commercial and governance framework, anatomizing these details is less important than understanding the two different service models of managed services. By doing so, organizations can evaluate their options based on each model's unique advantages. All service provisions from an external resource fall into one of these two models:

### Capacity creation

A "people-based" service in which team augmentation focuses on providing the headcount needed to perform specific roles and tasks.



### Managed process

An "output-based" service in which human resources are blended with process improvements and technology enablement to achieve specific service levels or deliverables.

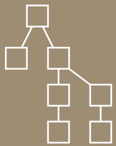
Which of these two models an organization chooses will depend on its culture, short- and long-term objectives, technology ecosystem, and other factors.

Capacity creation supports an expansion of the status quo and assigns ultimate responsibility for outcomes and risk mitigation to the organization rather than the vendor.

## Capacity creation

Capacity creation fits the needs of organizations that prefer to add capacity by augmenting their team with on-site or remote workers whose efforts are integrated into their existing processes and technologies. While the vendor finds and places the required talent, the client remains responsible for ensuring that adequate resources are allocated and service goals are met. This service model is a better choice for organizations that:

- Want to maintain responsibility for managing the organization's resource requirements
- Are not seeking to change or optimize existing processes and technologies
- Prefer not to pause or disrupt BAU when implementing updated processes
- Can project the added capacity they will need based on predictable workload requirements
- Are comfortable with pricing that fluctuates based on the number of people-hours required to perform the work
- Are more comfortable measuring value in terms of people-hours than outcomes or other success metrics
- Are reluctant or unable to share data with external service partners



A managed process not only supports growth and agility, but helps the organization establish service levels that enable them to increase revenue and differentiate themselves in the market.

## Managed process

A managed process supports organizations that need to increase capacity while enhancing their service's speed, efficiency, and agility, and the experience they deliver to customers and investors. The vendor is responsible for orchestrating all resources required to meet service goals, including processes, technologies, and a global pool of workers. The vendor is also fully accountable for all deliverables and is incentivized to maximize efficiency. This service model is a better choice for organizations that:

- Prefer the predictability of a fixed, transparent pricing model that is based on measurable output rather than people-hours
- Need a stable, predictable output based on a service structured to accommodate unexpected capacity surges or labor volatility and scarcity
- Are motivated to improve efficiency and profitability through proven, proprietary technologies and processes supported by the vendor
- Are confident that cloud technology will meet their security, privacy, and regulatory requirements and motivated to benefit from leading, proprietary technology supplied by the vendor
- Are willing to share data with the vendor and adjust existing processes in exchange for greater efficiency and cost savings
- Seek to integrate managed services to enhance their competitive position in the market, rather than increase capacity
- Prefer to measure ROI in terms of measurable output and performance improvement

# Customer onboards entities up to 3X faster

Whether the goal is to optimize existing processes or implement new functions, choosing the right solution provider is rarely straightforward—particularly when factoring in regulatory change, talent attrition, and changing market conditions. The following scenario demonstrates how technology, data, and expertise can be combined to drive successful outcomes.

## Challenge

When a global asset manager decided to sell its legacy business as a separate trading entity, the new business needed to establish its own operations and regulatory management team. The deal could not close without a reliable compliance infrastructure in place, so time was of the essence.

## Solution

After evaluating the option of building its own compliance technology and operations team, the trading entity decided to entrust KYC and Third-Party Risk Management (TPRM) functions to S&P Global.

## Approach

S&P Global Market Intelligence used proprietary technology and data to design a new KYC and TPRM infrastructure.

**For KYC**, S&P Global Market Intelligence built an end-to-end screening solution that included a combination of data automation, rules-based workflow, and a centralized client engagement platform.

**For TPRM**, risk assessment and monitoring were managed through Know Your 3rd Party (KY3P®), an integrated third-party and vendor risk management solution suite. The vendor population was assessed using near-real-time data for cyber ratings, financial stability, vendor sanctions and screening, and ESG, as well as analysis of global news.

Once the new operational processes were in place, a dedicated S&P Global Market Intelligence team assumed responsibility for managing KYC and TPRM processes and delivering the required outputs on an ongoing basis.

## Result

After implementation, the new trading entity had a compliance infrastructure that enabled them to meet the regulatory requirements surrounding customer and vendor risk.

With the operational function shifted to a service partner, the new business can focus on attracting new customers and optimizing returns for its clientele. The managed process approach has enabled the business to onboard customers three times faster than with their legacy process.

# Volatility creates opportunity

Financial institutions have faced various challenges in recent years, including unpredictable markets, regulatory stringency, and talent shortages. But those that move quickly enough can turn a volatile market to their advantage. The ability to onboard faster and slash time-to-market gives these organizations a competitive edge and an opportunity to generate more revenue.

Managed services can play an integral role in enabling financial service organizations to acquire new levels of speed, resilience, compliance, and customer service. Advances in workflow technology, flexible, modular service delivery, and output-based pricing models have brought these supportive services within reach for the buy-side, sell-side, custodians, and even corporates.

By clearing the misconceptions and gaining familiarity with the realities and unique advantages of capacity creation and managed process, financial institutions can evaluate their options wisely and make choices that best position them to turn market volatility into a business opportunity.

Learn more about how Managed Services for Network and Regulatory Solutions can help your organization become more agile, efficient, compliant, and competitive. Speak to one of our experts today.

### About Managed Services for Network and Regulatory Solutions

For decades, financial market participants, including global and regional banks, sell-side, and corporates, have relied on Managed Services for Network and Regulatory Solutions to help them scale operations flexibly, enhance revenue enablement, and manage financial and reputational risk.

From on-demand capacity creation to robust managed process, our client onboarding, tax, regulatory reporting, third-party risk management, and corporate actions solutions are supported by ground-breaking workflow technologies, a global network of 500+ domain experts, one of the world's largest sources of transactional data, and the largest network of cross-asset-class market participants.

### In 2021 alone

**500+**
domain experts deployed

**300,000+**
client communications sent

**600,000+**
IRS tax forms validated

**15,000+**
KYC profiles completed

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