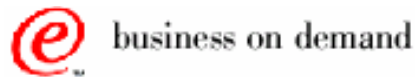




Securities Industry Services

# IBM – IDA STP Update

September 12, 2003  
Greg A. Lee



## *Agenda*

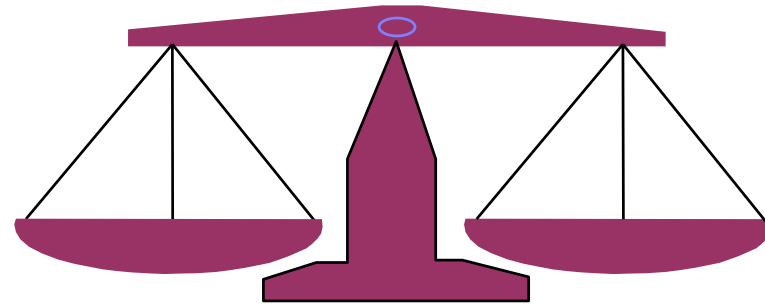
- ➔ **STP – Industry Context**
- **What STP is and why it is important**
  - **Process**
  - **Problem areas**
- **What areas to focus on for STP readiness**
- **What is IBM doing**

## STP may be a bigger challenge than Y2K: Milestones / Dates

- Y2K was technically inevitable, whereas STP is an industry direction
- June 2004 roll-out in the US and Canada: this date has changed once already, some participants think it will do so again
- T+1 is no longer the impetus
- Incremental improvements of T+5 to T+3 won't be enough
- Impacts all market participants
- **CCMA Milestones**
  - 12/2003 – Publication of best practices and standards
  - 12/2004 – Legislative and Regulatory changes enacted
  - 6/2005 – Industry wide STP implemented
- **SIA Milestones**
  - 7/2003 - Stock Loan Recall System goes live
  - 6/2004 – all institutional trades matched on T (trade date)
  - 6/2004 – Corporate Actions liability hub implemented at DTCC
- **Securities Commissions (CSA)**
  - 6/2003 – Issues STP e-survey to market participants
  - 9/2003 - Publicize results to industry



# Pain versus Priorities



## ■ Pain Points

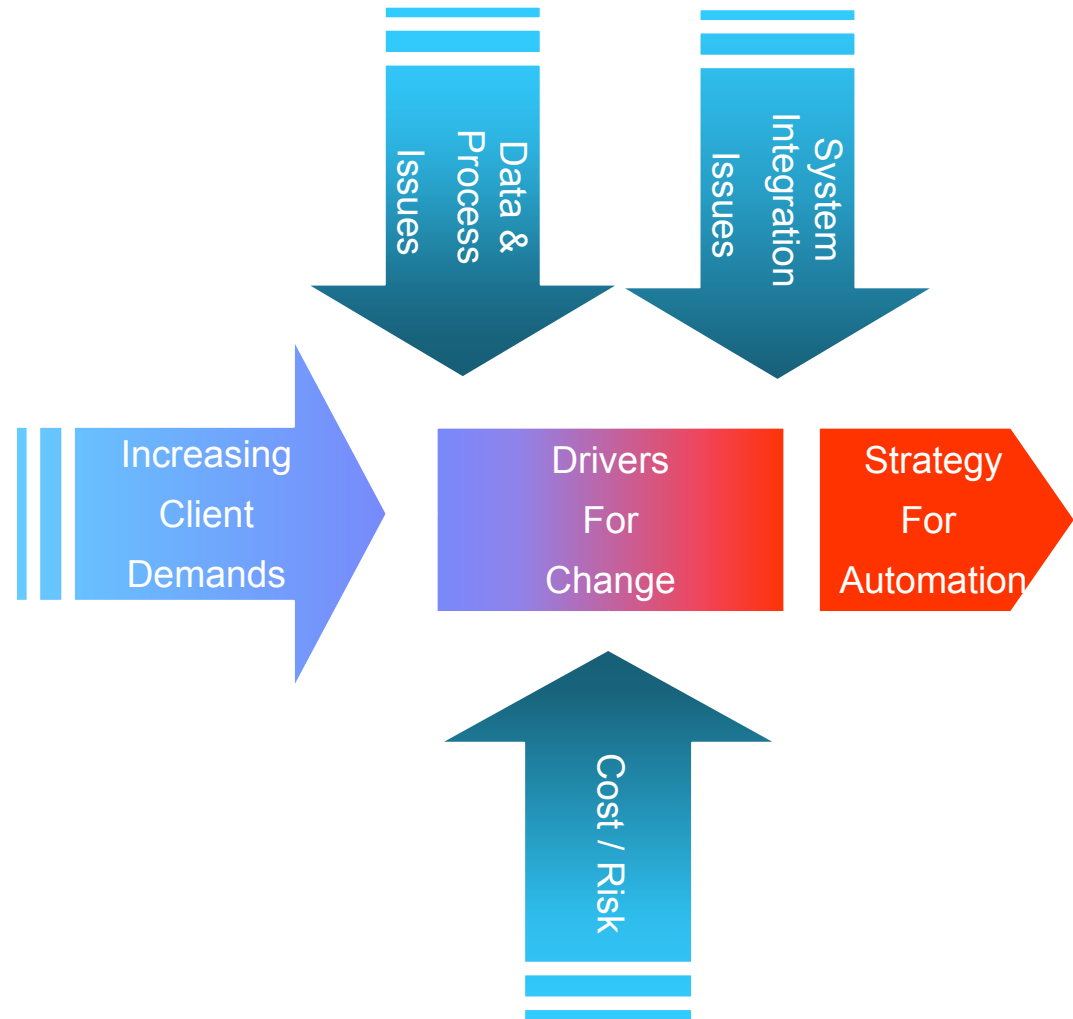
- ✓ Unprecedented market growth followed by significant downturn
- ✓ Increasingly complex operating environment
- ✓ Increasing operational costs
- ✓ **Consolidating Industry**
- ✓ Changing industry initiatives

## ■ Priorities

- ✓ Manage operational expenses
- ✓ Identify new areas of revenue opportunities
- ✓ Business recovery challenges
- ✓ Changing Market Conditions
- ✓ Consumer Demands
- ✓ Alignment to industry initiatives

# Industry developments and pressures are driving participants to change...

- **Data Demands**
  - ✓ customer/ regulatory for near-real time access to trade/position data
- **Cost Containment**
  - ✓ absolute/unit costs as margins narrow
- **Processing time compressed**
- **Risk Demands**
  - ✓ reduce operational, market, credit risk
- **Increasing Client demands**
- **Complex Systems Integration**

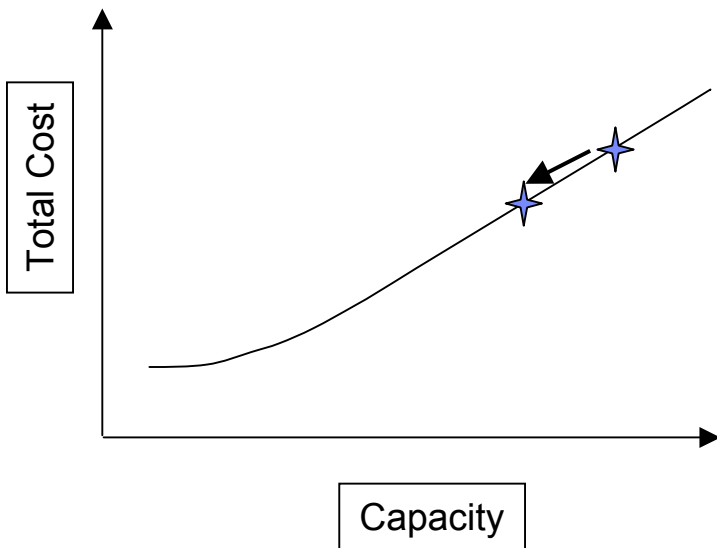


## ...but industry circumstances have slowed down the momentum towards an aggressive STP movement in Canada

- ✓ Market has been soft over the last few years
  - Budgets for financing STP initiatives have shrunk
- ✓ Without the impetus of T+1, industry is slow to move forward
  - June 2005 move towards STP in the US and Canada: movement as an industry has lost some momentum
- ✓ Consensus is required amongst multiple market participants (b/d, money managers, custodians, depository). Key decisions remain outstanding:
  - Cross-border settlement model
  - What solution(s) is chosen for the Canadian marketplace (recommended domestic model, custom solution, etc.)
- ✓ Other priorities (front-office, wealth management, order entry/management)
  - Focus on immediate return on investment
  - Other tactical plans may be considered higher priority for investment
  - Sense of urgency / benefit versus cost

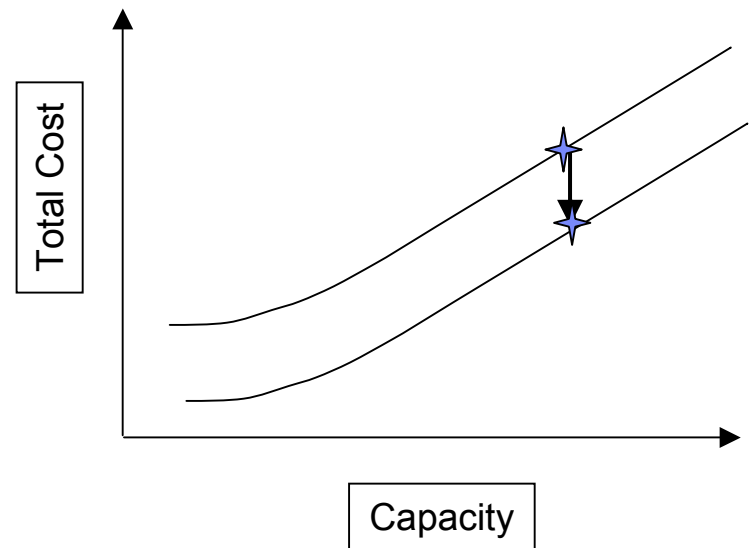
# Cost cutting alternatives firms are considering

**Type I: Move Down Cost Curve**



**Cost savings derived from initiatives that reduce capacity**

**Type II: Shift the Cost Curve Down**



**Cost savings derived from initiatives that increase the efficiency of operations**

# Some approaches to operational efficiency

	<b>Definition of Cost-Cutting Initiative</b>	<b>Potential Benefits</b>	<b>Potential Cost Savings</b>
<b>Straight Through Processing</b>	<ul style="list-style-type: none"> <li>STP is the optimization and automation of processes related to the performance and confirmation of securities trades and other financial products</li> </ul>	<ul style="list-style-type: none"> <li>Cost savings</li> <li>Increased capacity</li> <li>Risk mitigation</li> </ul>	<ul style="list-style-type: none"> <li>10%-20% of back office expense</li> </ul>
<b>IT Delivery Optimization</b>	<ul style="list-style-type: none"> <li>IT delivery optimization is inventorying the IT infrastructure, identifying redundancies and redesigning the IT organization, processes and technology to minimize costs without sacrificing flexibility or functionality</li> </ul>	<ul style="list-style-type: none"> <li>Cost savings</li> <li>Improved service</li> <li>Increased flexibility</li> </ul>	<ul style="list-style-type: none"> <li>20%-30% of IT delivery spend</li> </ul>
<b>IT Outsourcing</b>	<ul style="list-style-type: none"> <li>IT outsourcing is the practice of using third-party vendors for the development, management and maintenance of technology systems and personnel in order to lower costs, provide increased functionality or both</li> </ul>	<ul style="list-style-type: none"> <li>Cost savings</li> <li>Increased flexibility</li> <li>Increased financial flexibility</li> </ul>	<ul style="list-style-type: none"> <li>0%-5% of IT spend</li> </ul>

## Agenda

- STP – Industry Context
- ➔ ▪ **What STP is and why it is important**
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## A simple definition of STP...

- ✓ A set of fully automated processes that...
  - Seamlessly pass financial information electronically, on a system-to-system basis, to all parties in the end to end securities transaction process without manual handling or redundant activities
  - Data is entered once with no re-keying
  - Designed to eliminate human or manual intervention
  - Manual interventions are only for exceptions - focused on exception based processing

## STP-enabled T+1 models offer considerable benefits to Canadian securities firms

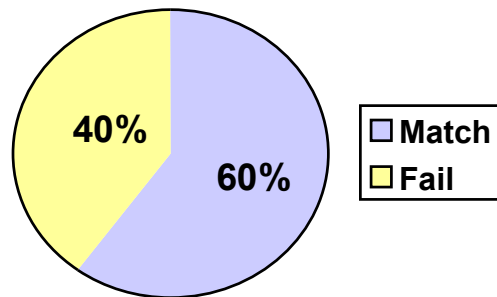
- STP addresses increasing complexity in the marketplace
- Fewer trade fails
- Reduced manual processing costs
- Concentration by each party on what it does best
- Risk reduction precipitated by an efficient settlement cycle
- Promulgation of information timeliness and accuracy
- Increased capacity and increased productivity in settlement will reduce opportunity for error



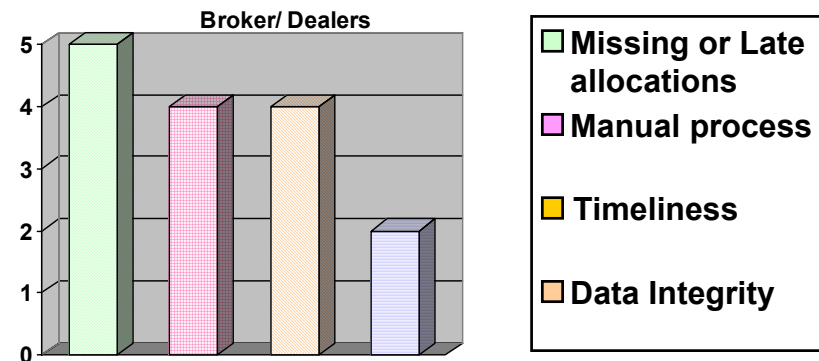
## Why is it important .... Problems with the current process

- **Manual processing; lack of automation**
- **Batch processing; lack of real time processing**
- **Lack of standard interfaces**
- **Missing or late messages (e.g. notices of execution, allocations)**
- **Lack of data integrity; lack of data standards**
- **High trade failure rate; costly trade repairs**

### Trade Matching Rate



### Problem Area

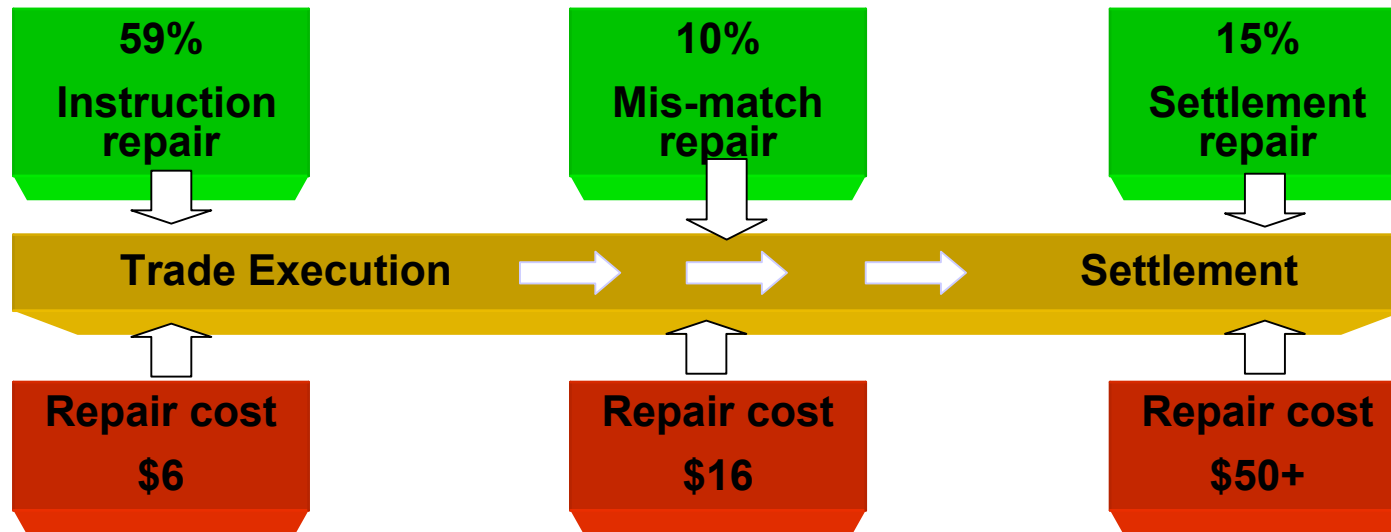


# The impact of settlement risk....

## The cost of failure

- 20% of cross-border trades fail to settle on T+3 and over 65% require repair
- Average operational cost per clean securities trade \$10

(source: SWIFT)

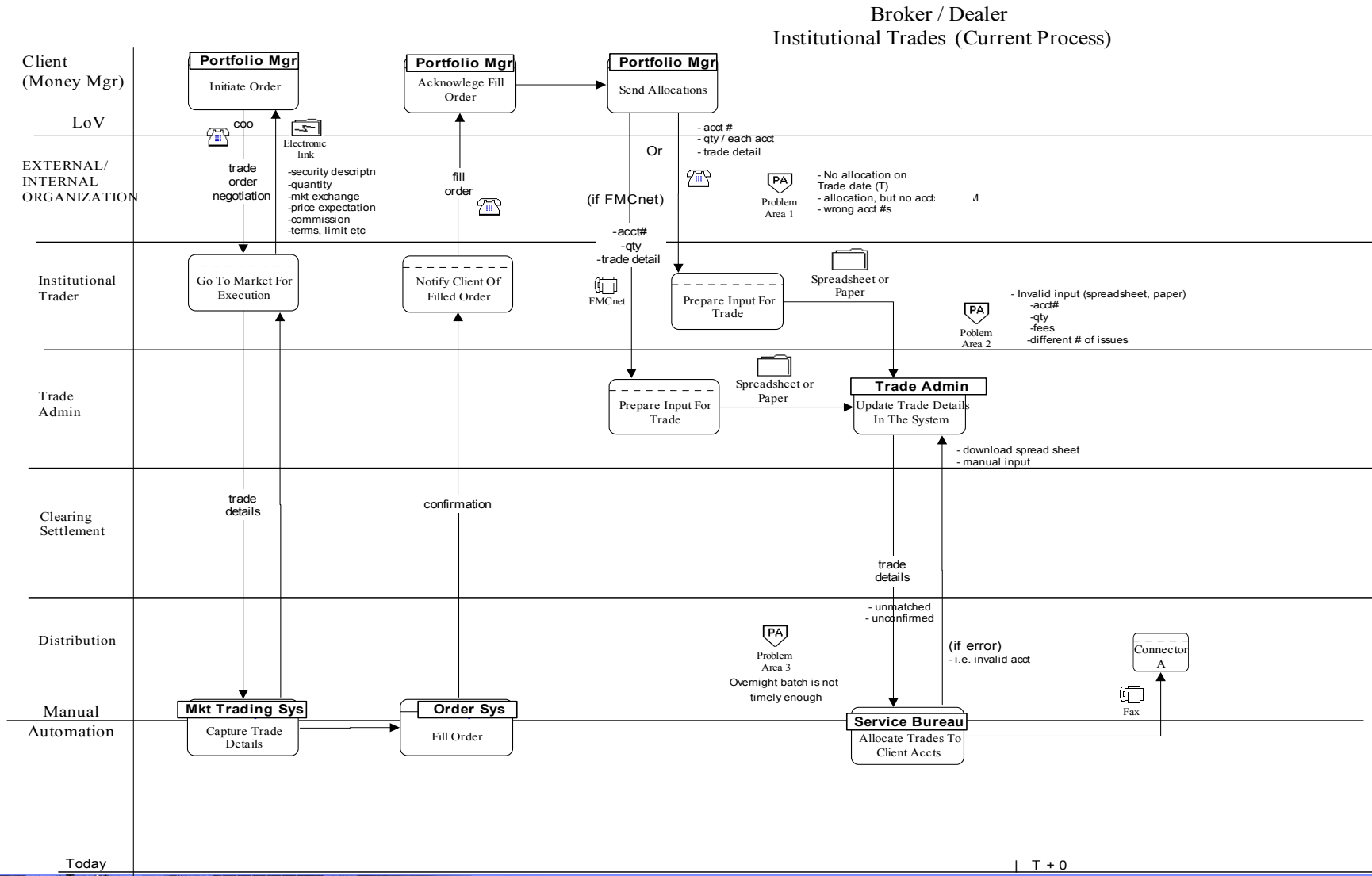


## The Impact of failure

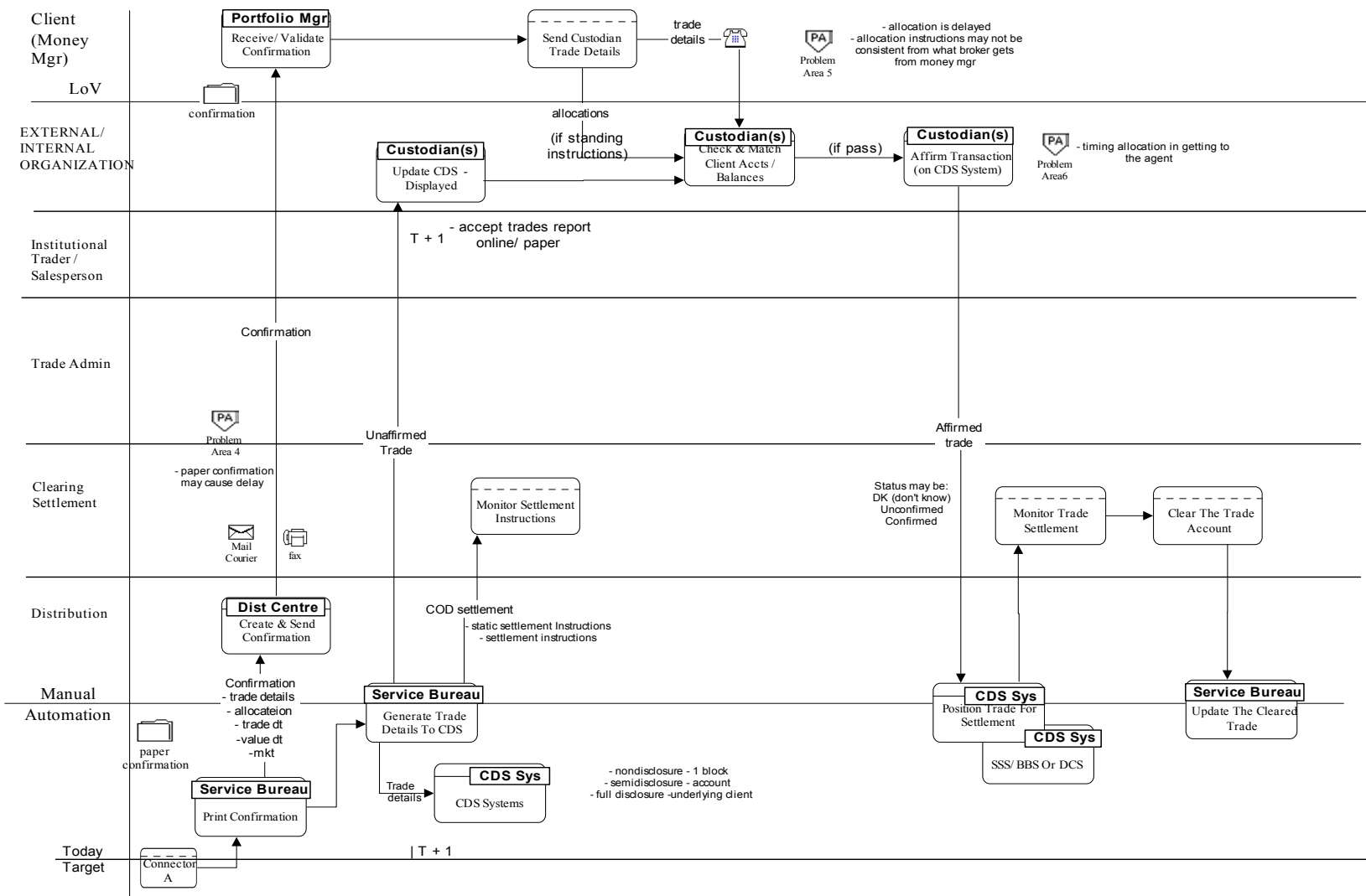
- Increased penalty costs
- Increased transaction unit costs
- Potential capital requirements
- Poor customer service
- Increased operations risk
- Increased “reputational” risk



# To determine key opportunity areas to focus on for STP, it is important to understand your 'As-Is' process...




# ... and identify the problem areas and opportunities for improvement



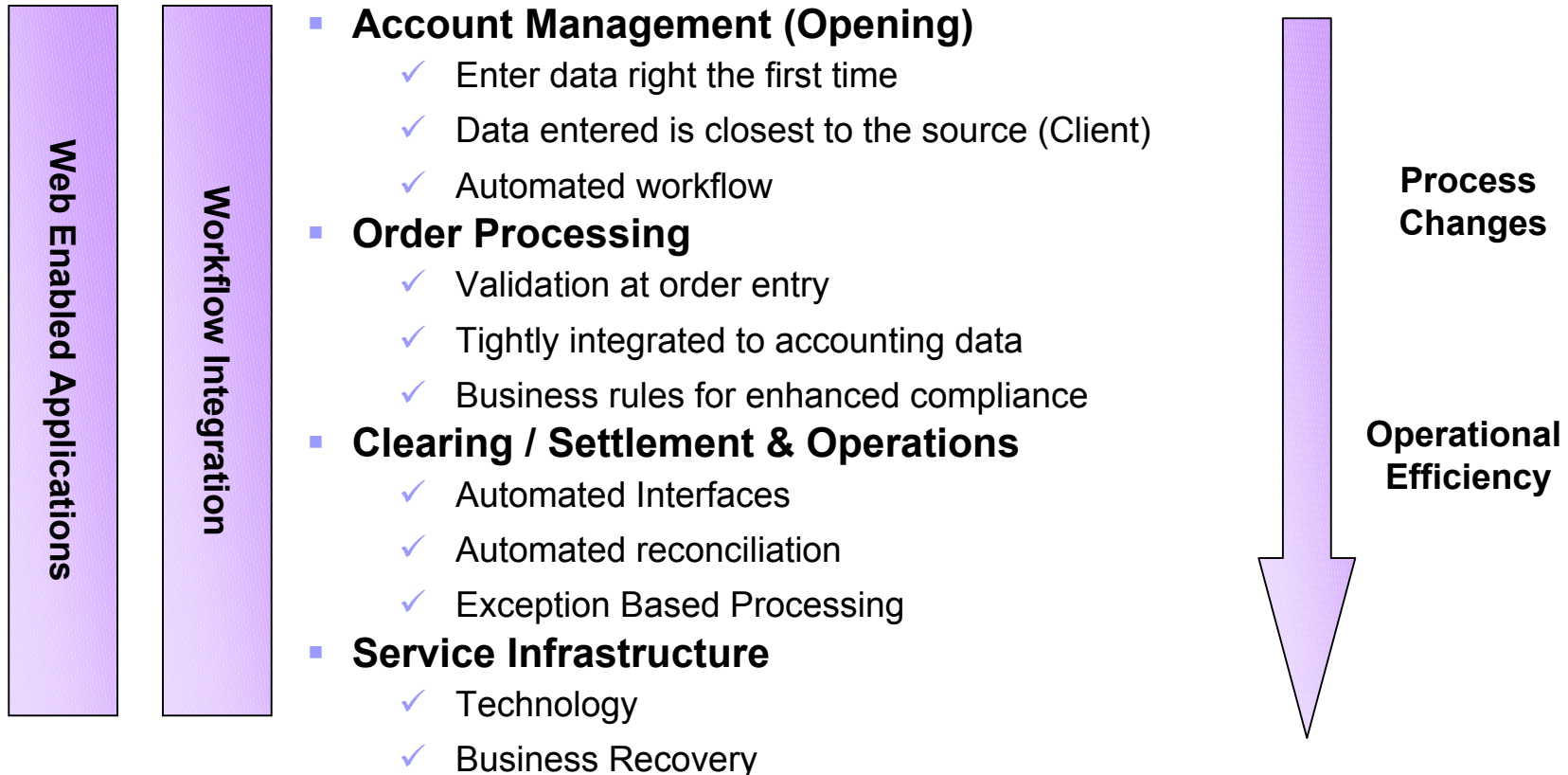
## Deficiencies in the Process

- Information not communicated electronically
- Re-keying of information into different systems (no data enrichment)
- Process flow is inefficient – back and forth
- Verification and matching in several points of the process flow
- Human intervention on the ‘routine processes’ and not just ‘managing exceptions’
- Batch over-night process
- Potential for having incomplete data

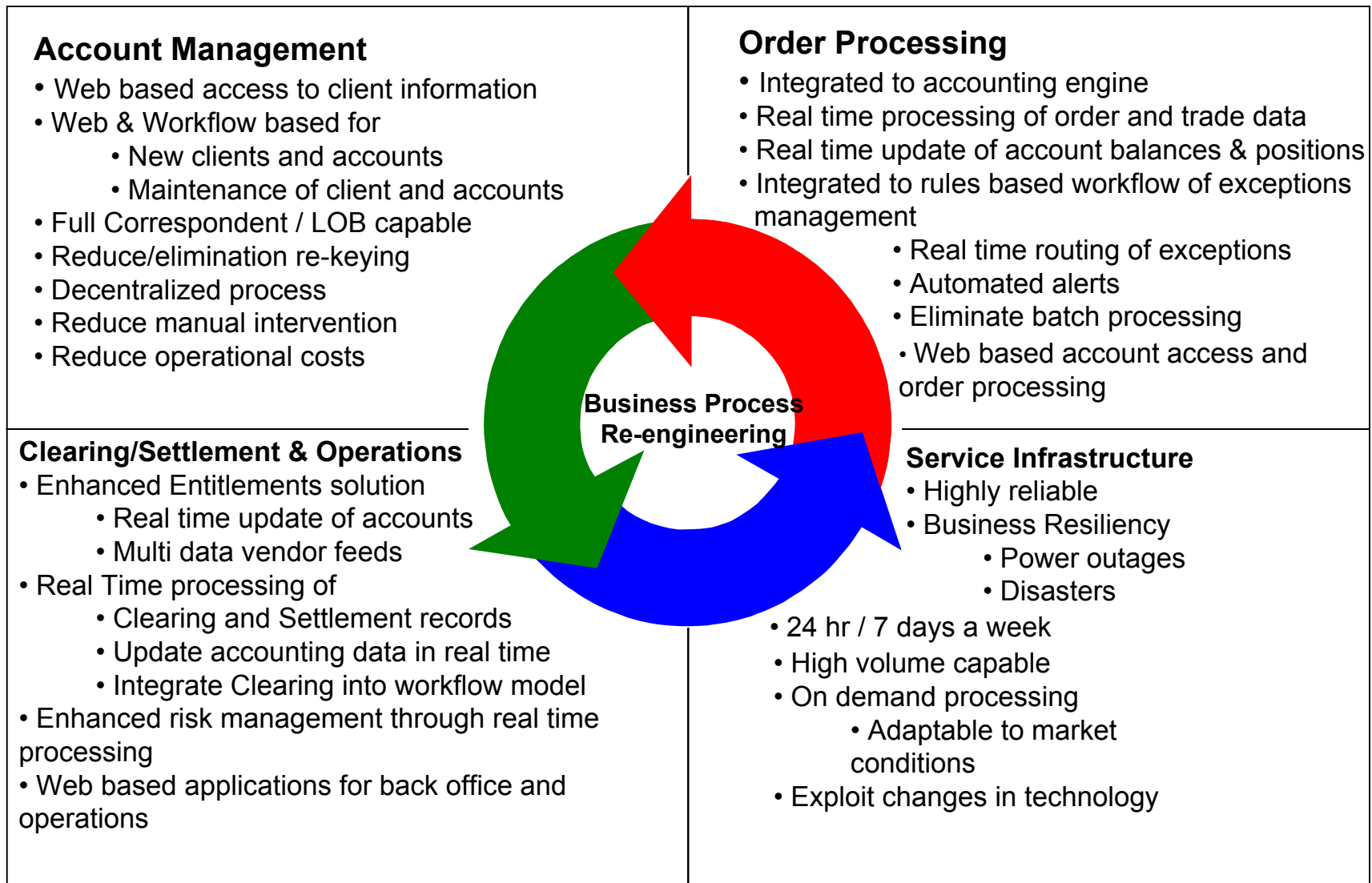
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# Focus on specific functional areas



# Optimize STP technology & process strategies throughout your business



## How can you get started?

- Develop an STP vision
  - ✓ Goals (real time, reduced cost, reduce risk, eliminate manual process, errors)
  - ✓ Ability to integrate with the Canadian solution(s)
  - ✓ Ability to integrate with global clearing & settlement initiatives
  - ✓ Assess your current trading environment
  - ✓ Data structures, messaging, internal/external interfaces, applications
  - ✓ Understand your business partner's/vendor's strategy for STP
- Develop a strategic roadmap to move from the current environment to the vision
  - ✓ Taking a holistic approach will maximize the effectiveness of chosen solutions and minimize costly overlaps in functionality
- Participate in industry conferences/ industry surveys / monitor developments at the key industry organizations: IDA, CCMA, SIA, CDS, CSA, SEC
- Work with your business partners and vendors

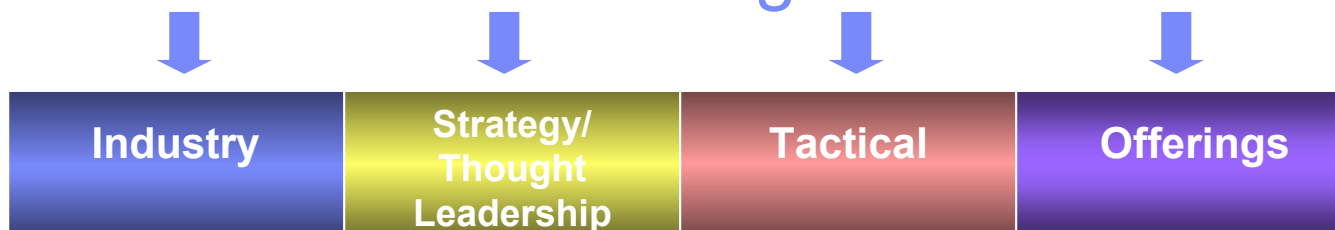
## It's up to you...but you are not alone

- Start early ....
- Understand and work towards the benefits that STP enables
  - ✓ Fewer trade failures
  - ✓ Reduced operating costs
  - ✓ Timely information
  - ✓ Risk reduction
- Get ahead of the next big run - Bull market
  - ✓ Prepare for increasing volumes
  - ✓ Take advantage of the slow times
- Tomorrow's leaders will use this time to invest in making their business processes more efficient
  - ✓ Automation in workflow
  - ✓ Real time implementation
  - ✓ Web Access
- Consider a comprehensive strategy in tackling STP
  - ✓ Discuss with your service provider
  - ✓ Develop an STP strategy and roadmap
  - ✓ Validate the firm's ability to integrate with Canadian and global clearing & settlement processes
  - ✓ Begin to develop your target architecture to realize STP

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# What are some of the things that IBM is doing?



- ✓ IBM SIS has launched the timely delivery of STP related solutions for their clients
- ✓ Work with CSA/OSC to develop and analyze the 2003 STP e-survey in Canada
- ✓ Co-authored the Canadian Capital Markets Association (CCMA) Institutional Trade Processing T+1 White Paper
- ✓ Work with our securities and financial markets customers to advise and assist them in their technical and business STP needs
- ✓ Securities Architectures (Business and Technical) – industry leading intellectual capital developed as a basis for offerings
- ✓ Sponsorship of key security industry conferences (SIA, CCMA)
- ✓ Publish articles, speaking at conferences on T+1 and STP
- ✓ Recognized IBM strengths in on demand hardware, messaging infrastructure, data management and related products and services to deliver the secure, scalable environment required by our clients for achieving STP

- **END of SLIDES**