GROWTH AND COST TAKEOUT FOR CAPITAL MARKETS SERIES

Article 2 – A Leaner Operating Model to Fuel Growth

Speed Read

- Following the growth strategy, firm operating models should be assessed for opportunities to support growth initiatives while addressing efficiency needs
- An operating model of the future can deliver optimal resource allocation for top and bottom-line efficiencies at the same time

IN THE PURSUIT OF A LEANER OPERATING MODEL OF THE FUTURE

In the **first installment** of Capco's series, we detailed the imperative for growth and cost takeout to work in tandem. A growth strategy acts as the first aspirational portion of this approach. In this article, we will describe how businesses can reorganize and instill discipline to become leaner, more customer-centric, and competitive at the same time. We will consider why and how cost takeout and leaner operating models can fuel growth.

The Leaner Operating Model has been a long-desired industry goal. Structural industry costs (at least $700 billion each year) offset more than eighty percent of the total industry revenue[1]. Broker-dealers are face-to-face with a unique transformation opportunity.

The Leaner Operating Model of the future must deliver growth and optimum efficiency at the same time. There is no one simple answer, but a clearly defined growth strategy provides the guideposts for how an operating model can be designed and the key drivers that determine the direction changes (e.g., cost competitiveness, customer value creation, regulation). Pursuing such changes can reveal capabilities that are not essential and should be reduced or eliminated completely. Derived savings can be repurposed for investment into the core capabilities for growth.

> *"The industry is rapidly accommodating external players, including fintechs, into internal ecosystems, making a stronger case for commoditized parts of future operating models to be executed outside of the core organization."*
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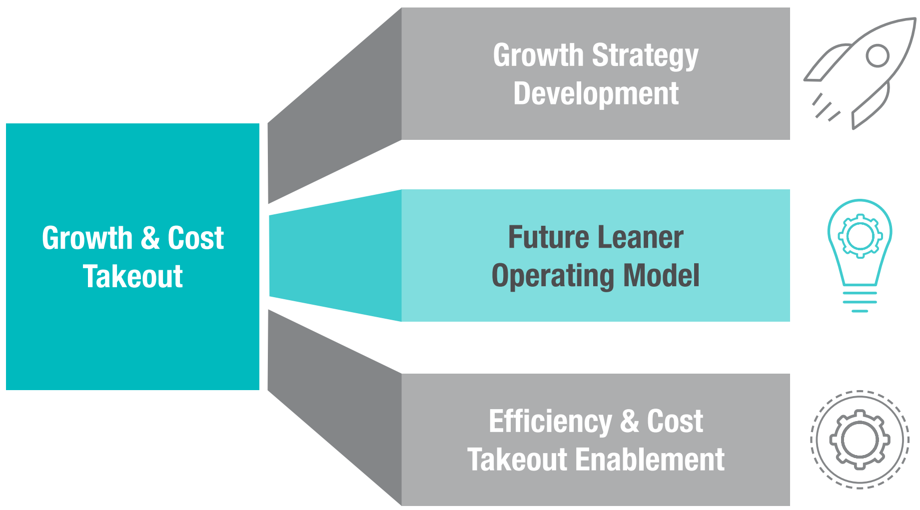
> – George Black, US Capital Markets Practice Lead

1. https://www.sifma.org/resources/research/fact-book/

EXHIBIT 1



BREAKING DOWN INDUSTRY OPERATING MODELS

Industry executives should consider the following set of key questions to challenge and optimize existing operating models:

What does the Leaner Operating Model of the future look like?

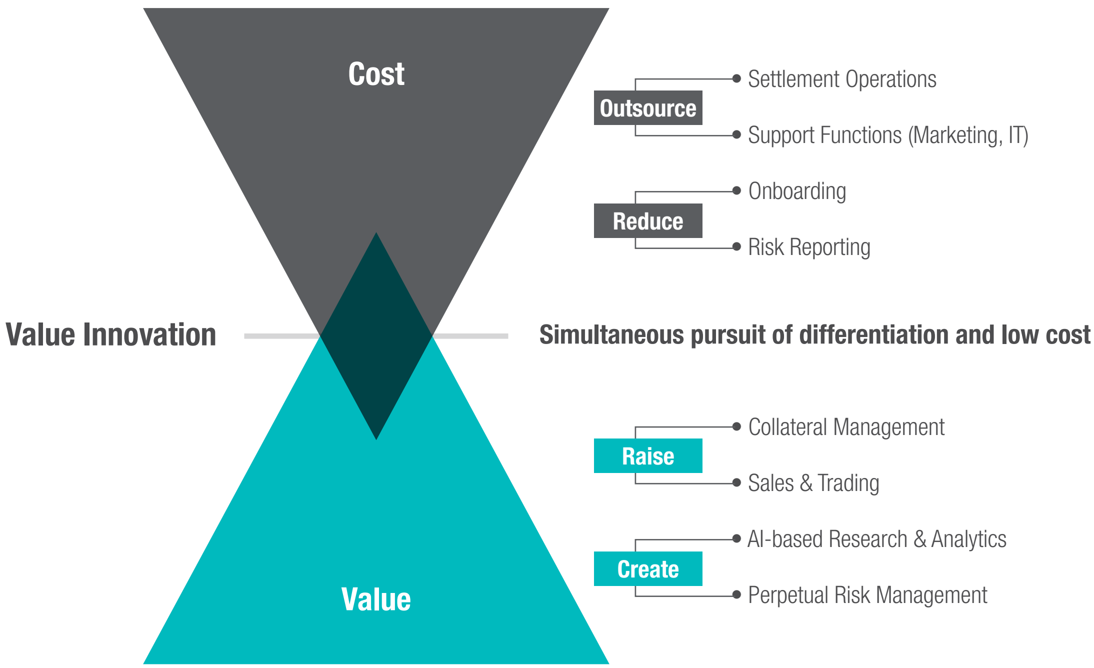
- All resources should be rationalized for growth and cost-efficiency
- Broker-dealers should prioritize value innovation – continuous low cost and customer value creation (see Exhibit 2) where non-core functions are stripped down, outsourced as shared services, or eliminated completely to allow for investment elsewhere
- High-value and differentiated capabilities are optimized to improve client experience
- Depending on the nature of the business, broker-dealers may pursue different transformation tactics (e.g., outsourcing, post-merger integration, divestiture) to rationalize resources for change

How should functions, teams, locations, and the business be organized to fuel growth?

- Broker-dealers can apply a blue ocean framework for the analysis of all capabilities and functions based on key customer needs and organize its businesses to ensure the most optimal structure
- Key findings from the analysis can reveal opportunities where the firm is allocating too little or too many resources, revealing inefficiencies in organizational structure and cost reduction opportunities
- A centralized design authority can govern operating model change opportunities, to ensure consistent, enterprise-wide alignment to growth and cost efficiency goals and coordinated operating model design and realization

EXHIBIT 2:

Sample Capital Markets Functional Cost vs. Value Analysis



What are the latest industry trends to achieve the Leaner Operating Model?

- Many broker-dealers have outsourced trade settlement activities to third-party vendors as the capability is not differentiated across firms and can allow for resources to be reinvested elsewhere
- Depending on the size of the broker-dealer, larger players have built combined in-house and vendor-based trading platforms, while others rely entirely on third-party vendors, prioritizing cost efficiency over value creation to achieve growth
- The industry is actively implementing automation/robotics, data and cloud computing solutions for risk management – aimed at realizing cost efficiencies and real-time risk management simultaneously
- The industry is yet to consistently realize new cost takeout opportunities for enterprise-wide workforce management in a distributed workforce environment. Nevertheless, this trend is definitely one to watch (for Capco workforce strategy intelligence, please read here).

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Automation is helping capital markets firms process trade data more efficiently, streamlining not only the trade lifecycle but also placing better information in the hands of the business units to enable revenue uplift. It is changing the way people think about their processes and evolving the skillset requirement up the technical curve across the industry.”

– Jon Herna, Managing Principal, US Digital Practice

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LEANER OPERATING MODEL ENHANCEMENTS CAN FUEL GROWTH AND UNLOCK COST TAKEOUT OPPORTUNITIES

Capital markets firms can differentiate themselves and their operating models now to become leaner and grow at the same time. In the third part of this series, we will discuss how businesses can embed and govern a continuous cost takeout approach to achieve strategic goals for the future.

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