

Nextra's back office automation delivers on promise

Mauro Pernigo, Head of Operations, Nextra Investment Management sgr

Shaping STPSM



THE PROMISE OF STRAIGHT THROUGH PROCESSING



Nextra automated its back office in 1999 by implementing Omgeo OASYS GlobalSM, Omgeo AutoMatchSM and Omgeo ALERTSM. The key, measurable benefits Nextra has seen post-automation are at least a ten-fold decrease in failed trades, whilst retaining the same number of back office staff to manage trading volumes. Nextra has seen a clear ROI¹ through increased performance levels and new business opportunities.

Why did we decide to implement Omgeo's solutions? Well, it's a complex series of events, something I'm sure we're all familiar with! We at Nextra had various challenges within our back office which created risk and cost for both us and our clients. Most importantly, our business is to deal with our clients' assets, therefore, we have a moral obligation to our clients to give the best possible service and to keep our risk and cost to minimal levels.

As a business, we had to remove the inefficiencies that result from manual processes. Our challenges included: dealing with a high number of failed trades and their follow up; the need to conduct cross-border trading efficiently and the need for standards to evaluate our and our counterparties' performance as well as reliable SSIs². Ultimately, we wanted to see the transformation of our back office from a manual processing function to a consultative department, enabling us to deal with changing market environments. Let me take you through the different components related to automation for Nextra.

“Non-automated firms represent a risk to us, therefore, we cannot do business with them”

Without proper levels of automation you can't go far without failing especially when, like us, you have an average of 30,000 trades per month. The majority of our trading volumes are with cross-border counterparties and those most regularly traded with are: UK, France, Italy and Germany. We use 50 brokers, 10 of whom deal with 90% of our total trading volumes and the rest deals with 10%. The high levels of automation of these countries (especially the UK) compelled us to increase our levels of automation accordingly, so that we could trade with the most desirable cross-border counterparties. The challenge we now face is that only very few counterparties in Italy are able to follow our standards and we have an increased awareness that automated processes result in reduced operational risk.

“Before automation we lost a great deal of time on following up failed trades. Now we can use our resources more efficiently”

Our back office has reaped many benefits since the implementation of Omgeo's services, including a positive impact on back office staffing. Automation has led to a change in the function of the department from a manual processing shop to a consultative unit. Before automation, 40% of our staff concentrated on reconciling the cash account. Post automation, because we have reduced the number of failed trades, we redeployed staff to handle counterparty relationships, since we also have reliable information to benchmark trade counterparties.

In addition, we have seen a reduction in what we call “pending” trades. Pending trades are those not affirmed on the same day of the trade, and these were a big problem for us. The reason for this is that Nextra's goal is to match everything by 7pm each day – with the exception of a few UK brokers (who send their data at the end of the UK trading day) and some US brokers (who send their data very early the next day). In order to increase SDA³ rates, therefore levels of efficiency, we had to send everything to custodians by noon the next day (1pm at the latest). Pre-automation these pending trades could number up to 800 (4% of the total number of trades that day), which had to be managed by several people each morning.

1. Return on Investment
2. Standard Settlement Instructions

3. Same Day Affirmation rates – when a trade is fully agreed – matched or affirmed – on the same day it is executed. This means the ability for trading parties to agree the trade (including all trade settlement details) and instruct the settling parties on trade date.

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“To us, our reputation and our competitive position in the market were key – therefore we didn’t consider just the economical return. Going forward – we are investigating the ROI before implementing other smaller projects, e.g. Omgeo Central Trade ManagerSM”.

Mauro Pernigo,
Head of Operations,
Nextra Investment
Management sgr

Post automation, we have only 300 pending trades that are managed by 2 people the next day. If we consider the figure before automation, we managed to reduce pending trades by nearly 4 times. These are “pending” but not failed. Therefore, there are 2 hours when we follow up with the counterpart and detect discrepancies, which means we can also reduce the number of pending trades that convert into failed trades. You can see how we’ve now achieved a dramatic reduction in the number of failed trades overall.

In addition, the cost of following up failed trades also had to be considered. In the past we had so many failed trades that it was impossible for us to follow them up. Now, being automated, we can quantify the reduction in the number of failed trades we have to follow up in terms of the redeployment of 2 members of staff. This is a very important factor when considering the benefits of automation to our organisation.

The redeployed staff members now measure the performance of our counterparts to ensure we are working as efficiently as possible. This measurement takes into account two factors: credit control (based on the credit rating of our counterparts) and operational quality.

This is a huge improvement. We now have complete statistics about the performance of our counterparts: instructions arriving late, instructions arriving incorrect, instructions forgotten... We now choose the counterparts we want to work with and, more importantly, how to work better with our counterparts.

“We reduced the number of failed trades by 10 times”

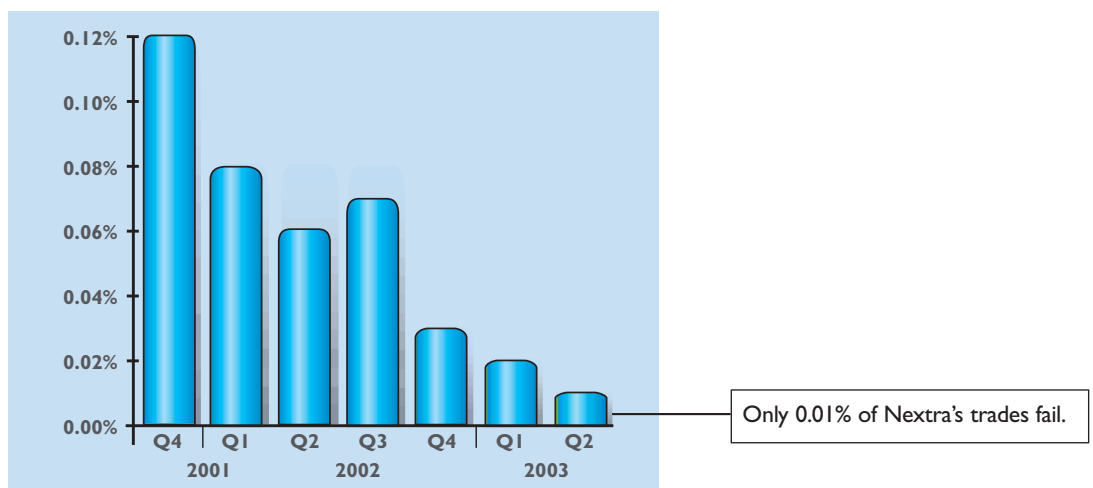
The way we prepare failed trade reports post automation is by relevant groups which we find very accurate. We differentiate failed trades caused by us and by our counterparts. Therefore, we are able to track the performance of all groups separately to trouble-shoot more easily.

Our reports showed that only 15% of failed trades are on the part of Nextra (wrong data or time delays); 24% of failed trades are due to custodian banks’ issues (time delays with the clearing houses) and 61% of failed trades are due to counterparts. *Today, and thanks to Omgeo’s systems, failed trades make up only 0.01% of the total number of trades processed. This represents a reduction in the number of failed trades by 10 times.*

I am pleased with the level of SDA rates post automation. This is important because we all know how much more productive you are when you get into work to find, for example, that the US sent confirmations overnight so you have time to deal with exceptions. This is down to an increase in SDA rates – I can now dedicate my mornings to US trades and exceptions. Our original goal was to achieve 70-80% SDA rates and I am happy to say we have achieved this and more.

Nextra’s reduction of failed trades (%)

Figures represent the monthly average per quarter starting from 2001 Q4 ending to 2003 Q2. The key, measurable benefits Nextra has seen post-automation are at least a ten-fold decrease in failed trades whilst retaining the same number of back office staff to manage trading volumes.



“I don’t believe automation is simply about dealing with increased volumes, but about coping with volume peaks and troughs”

Trading volumes, obviously, affect the economies of scale in our business. When manual processes are in place, you need more people in the back office to deal with high volumes. If you are automated, you can process more trades with less people and increase efficiencies when dealing with your counterparts. Without automation, not only are there no standards, but you need more people; the whole thing is a mess... it gets very complicated even with low volumes!

Therefore, I don’t believe it’s simply about increased volumes, but about coping with different volumes, especially peak volumes. Automation allows you to adapt and react quickly to changing environments in the market – scalability is key in our ever-evolving industry in order to ensure we remain competitive.

“The way we work now, post-automation, is to agree with our counterparts how we want to work together”

Our vision for implementing standards was first to align in-house processes, then to have a clear configuration with the custodian banks. The big change was when we fully automated the settlement instructions we received from our counterparts. This allowed us to reduce the number of custodians we used from three to one and the automation of our processes meant we could then make a decision on standards, i.e. SWIFT messages. Therefore, *Omgeo ALERT* and the integration of custodian banks are very important drivers for STP.

The final step after trading is to reconcile the cash account. Since we had reduced the number of failed trades we were also able to reduce the work required in this area (reconciliation of settlement instructions, client instructions, dividend etc.) by 40%. There is a knock-on effect – to settle a trade you have to cash the settlement on time. In the past the high level of failed trades were causing a chain of problems including the lack of availability of timely cash dividends. This created huge costs for Nextra!

We use 1 custodian for 90% of our total trading volumes, and 6 custodians for the rest (10%). When it comes to custodian banks, the more problems you cause, the worse your profile and reputation in the industry. Our reputation is very important to us as it ensures our clients’ needs are of the utmost importance and helps the industry as a whole to progress.

Our CEO and the Director of Investment Department wanted an integrated system to link front office to back and all the way to settlement, which I call “internal STP”. The CEO was interested in getting an online view of the process, failures and integration with accounting systems. Some of the activities that had formerly been delegated to custodian banks – essential to avoid failed trades – were then taken in house, e.g. performance measurement of counterparts. We can now manage our own information on our capital which had been delegated to custodians before.

The way we now work is to agree with our counterparts how we want to work together – we create a matrix or parameter of objective measurable results so we’re all working to the same standards. In the past it would have been impossible to get comparable figures, whereas now everything is under our control and our decisions are based on reliable information. Therefore, another key benefit for Nextra is the change of role of the back office – we have become a decision-making department in the company. Post-automation, our approach and role is much more strategic. The CEO also now works closely with the back office to understand the operational profile of the counterparts before we select them for business.



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“We can see a clear ROI in excellence in performance and new business opportunities”

Our reputation in the marketplace has changed dramatically. Custodian banks that we don't use now invite us to meetings to testify about the quality of our operational efficiency. We are now considered a more trustworthy investment management institution. The transparency of our operations is the leading factor for this change in perception – in the past we could not publish operational results, but now we can be confident of their accuracy. Our excellent performance results give us a competitive advantage for a number of niche products – such as, pension funds, risk sensitive institutional clients, any fund with "capital protections" allowing us to specialise as a business. The point is not just to invest but to understand more about the investment and to be able to make decisions about the kind of investments we are making at any given time.

Nextra is looking forward to increasing its levels of automation further by migrating to central trade management through *Omgeo Central Trade ManagerSM*, once we have formalised our plans to become an outsourcer for this service. Now that we have the time to research into new business ventures, we hope to be able to expand our remit further than we have already with *OASYS Global*. We look forward to enjoying the benefits central trade management will offer.

Company Snapshot

Nextra has 110 billion Euros in mutual fund assets under management, 90 billion Euros of which are automated using Omgeo's services, and 20 billion Euros of private banking assets under management. The key instrument types Nextra trades in are: Equity (56%), Fixed Income (10%) and other securities (33%) including Forex, Derivatives and Repos. Nextra trades over 2000 fixed income trades a month and between 13000 and 15000 equity trades (90% cross-border) a month. Of the total number of trades, more than 80% are cross-border and 20% domestic of the total number of trades. All domestic trades are automated via Omgeo's services.

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