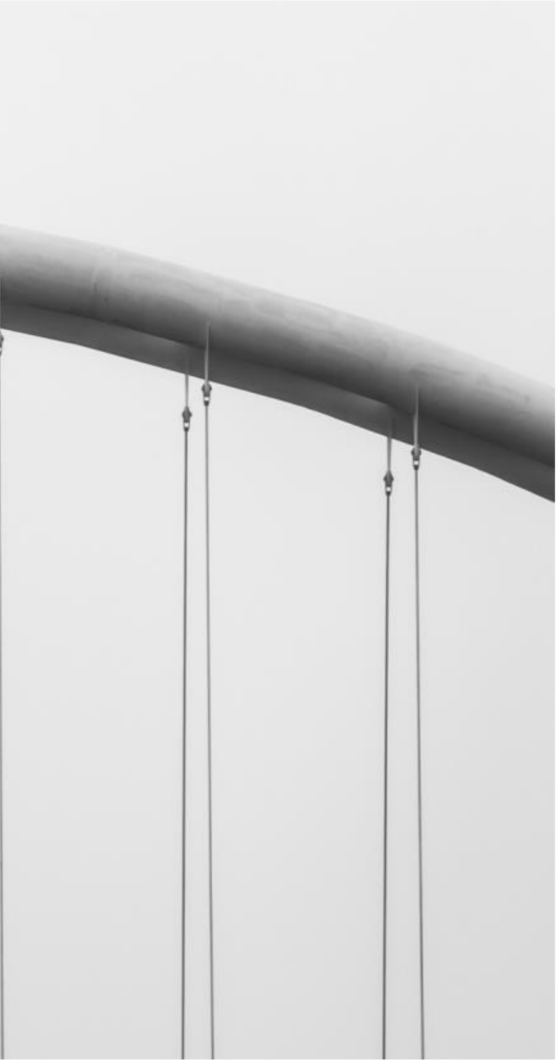
CAPCO & Finextra

WHAT MAKES UTILITIES USEFUL?



WHAT MAKES UTILITIES USEFUL?

THE FINANCIAL INDUSTRY'S APPETITE FOR POOLED UTILITY MODELS[1] CLEARLY EXISTS. WHAT ARE THE DRIVERS FOR GROWING THEIR UPTAKE? WHERE ARE THE OBSTACLES? WHAT, TODAY, DO FINANCIAL INSTITUTIONS SEE AS MOST USEFUL FROM UTILITIES? AND WHAT SHOULD THEY LOOK TO ACHIEVE WITH THE UTILITY MODEL TOMORROW? THE RESULTS OF THE LATEST GLOBAL SURVEY BY CAPCO AND FINEXTRA OFFER FRESH INSIGHT.

CONTENTS

Introduction – Exploring why Utilities are useful

In 2015, Capco, in association with Finextra, carried out a global survey of a wide range of financial institutions. The objective was to explore attitudes toward the Utility models that already succeed in other industries. We wanted to know why and where Utility models have been useful. We wanted to discover where the application of a Utilities model is still perceived as off-limits. And we wanted to estimate how the Utilities approach must evolve in order to drive increased uptake among banks. In short, our objective was to answer two fundamental questions about Utilities in the financial industry: where do they fit, and how far can they go?

Utilities overview – Beyond sourcing

Outsourcing in commoditised areas of banking IT, now commonplace, offers a range of approaches from captive through to near and offshore. We have seen shared service centre models (SSCs), too. While effective in many regards, outsourcing has not totally satisfied the industry, which has experienced a degree of sourcing fatigue. Specifically, in the area of labour arbitrage, compound salary increases in previously low-cost delivery locations have substantially increased costs.

An institution's profile significantly impacts sourcing uptake in its various forms. Tier 1 banks are usually big enough to undertake even the most commoditised processes themselves, although debate has grown around whether this approach is ideal. But this has not prevented large banks from extensive and long-term utilisation of a wide range of sourcing options. Many tier 2 and 3 banks have continued to own and operate commoditised processes, even in high-cost locations. Now, they too must examine alternatives to in-house services. The process rationalisation story remains far from over with many areas still demanding cost optimisation. Banks, especially tier 1 banks, have exhausted many of the existing cost reduction levers. These limitations drive the urgent need for a measurably and radically more effective approach.

What differentiates Utilities from sourcing? The Utilities approach goes beyond sourcing. It directly addresses areas of complexity where banks have systemically limited capabilities. It reduces risk, deals highly cost-effectively with large transaction volumes and drives up Capability Maturity Model Integration (CMMI) levels, among many other benefits.

As the industry learns to progress beyond today's fragmented and costly ways of operating nondifferentiating processes, the Utilities model offers a highly structured approach to providing reliable and cost-efficient solutions. At high level we have identified three key Utility model stages: mutualisation, standardisation and utilisation.

UTILITY MODEL STAGES

1 Mutualisation	2 Standardisation	3 Utilisation
• A driver for organisations that run identical programmes and comply with the same regulations • First isolates and then examines an organisational task, typically noncore and nondifferentiating	• Examines core operational elements: applications, data, infrastruc-ture and people • Uses as many common technologies and approaches as possible, thus establishing a 'shared normal'	• Detailed development and implementation of a Utility-based concept, shared by several banks or industry-wide • Replaces a fragmented landscape with a set of common approaches and radically reduces the number of variables, enabling cost reduction and freeing up resources

Mutualisation is a driver for organisations that run identical programmes and comply with the same regulations. In practice, mutualisation first isolates and then examines an operational task in detail. Typically, the task is noncore and nondifferentiating, bringing no specific competitive advantage to any industry player. It is nonelective, complex and carries a high business risk if quality, timeliness or precision fail. It imposes the same (or very similar) burdens on all players in a particular market or group of markets – such as the impact of Payments Services

Directive 2 (PSD2) and TARGET-2 Securities (T2S) on the eurozone. Examples include Know Your Customer (KYC), regulatory reporting, payment transaction processing, collateral management and post-trade activities. There is a clear mutual interest in approaching such tasks as efficiently as possible.

Standardisation of processes examines core operational elements: the application landscape, the data set, the current infrastructure and the people involved – profiles, roles and responsibilities. Standardisation uses as many common technologies and approaches as possible, thus establishing a "shared normal." Examples include the FIS™ derivatives post-trade utility platform. Developed in partnership with Credit Agricole Corporate and Investment Bank (CA CIB)[2], this utility provides a standardised platform for global banks to share their IT services for cross-asset derivatives. For users, the benefits include predictable and significantly reduced unit cost of execution and increased efficiency.

Utilisation is the detailed development and implementation of a Utility-based concept. This may be shared by several banks or even be industry-wide. It replaces a fragmented landscape with a set of common approaches and radically reduces the number of variables, enabling fixed or predictable price process operation. Usage charging rates are appreciably lower (savings as high as 30 per cent are commonly predicted and achievable, especially in the case of institutions that have not previously implemented process rationalisation). As a result, valuable resources, including human talent, are freed for differentiating activities (i.e. to grow the bank).

Examples include FIS's utility for post-trade futures and cleared over-the-counter (OTC) derivatives operations. Implementation of this utility concept enables derivatives brokers to achieve greater efficiency, reduce operational risk and cut total cost of ownership (TCO) by leveraging economies of scale in middle and back office processing and technology. Barclays, an industry leader in the global cleared derivatives industry, became the utility's anchor customer in 2015[3]. Barclays will also apply utilisation to specific futures and OTC derivative clearing operations and technology processes.

For our survey, we defined a "pooled Utility model" as the use of an external party that serves multiple customers to provide a pay-for-usage service in technology, data or process management.

Our hypothesis ahead of the survey

Our experience suggested some "pre-conclusions" about Utilities uptake:

- Key barriers include cultural and organisational issues within banks
- Lack of standardisation and fragmented/complex processes block uptake
- Banks have ongoing concerns around data security and related issues

> With every investment dollar under scrutiny, financial institutions must seek ways to share or mutualise costs where there is minimal differentiation. Then they need to reallocate budget to important areas of positive differentiation.

Survey specifics

POSITIONING

We wanted a snapshot of how the financial industry currently identifies operational elements suitable for a Utilities model, of what value they may already derive from the model and the nature of any obstacles preventing Utilities adoption.

SURVEY RESPONDENTS

We gathered a statistically significant response from 69 financial institutions distributed across 26 countries and representing a spread of global, international and regional financial institutions. The respondents ranged from C-suite to specific operational areas, including CTOs, COOs and specialist Operational Heads, among them treasury, IT, payments and digital.

SURVEY QUESTIONS

We asked 12 questions to gauge the current situation and key attitudes toward further Utilities uptake. The full question and results set is available on request from enquiries@capco.com.

What did we discover?

This summary focuses on the following areas of questioning:

1. How complex is your business today?
2. What savings do you expect from the Utilities model?
3. What are the operational key drivers toward Utilities adoption?
4. How far have you gone toward applying the Utilities approach, in named key areas?
5. What are the strategic drivers for Utility model uptake across the industry?
6. What is preventing you from moving closer to a Utilities approach?

The responses contribute to a deeper understanding of where institutions are today – in relation to the key issues surrounding Utilities uptake – and of the factors that will shape their future decisions.

1.

How complex is your business today?

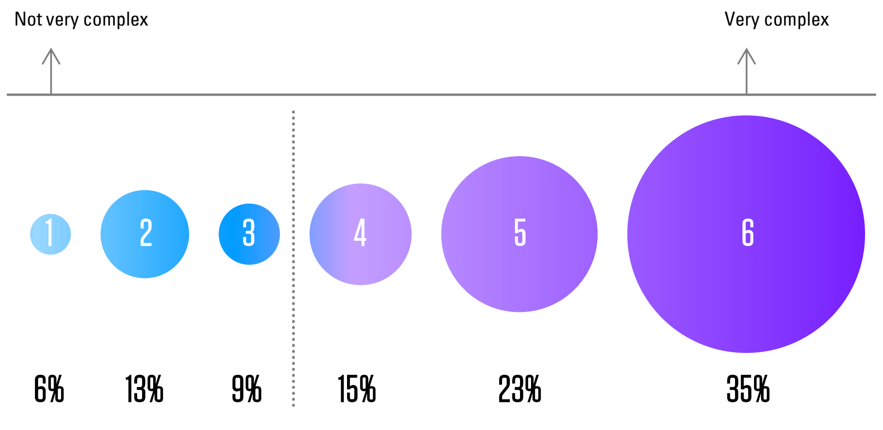
The Utilities model aims to provide a positive contrast with operational, technological and structural complexity, through a simplified pay-for-usage service. So, how do respondents rate the complexity of their business, currently?

Remarks

Nearly three-quarters of the surveyed market consider its business significantly to highly complex. For the remaining responses, we see a strong likelihood that they represent institutions with a simpler business model and/or limited multiple jurisdiction exposure. Complexity remains a significant macro trend impacting banks. Legacy technology is driving up costs and reducing overall agility.

This in turn creates migration obstacles to new technologies. Increased regulatory burden – the "regulatory tsunami", – and its required responses in terms of change management for technology, operations and organisational areas (MiFID2[4], Too-Big-to-Fail, Dodd Frank, EMIR[5], etc.) have left no capacity to deal with "unplugging" complexity. In fact, it has pushed institutions to build ad hoc solutions to comply with regulatory requirements. Manual, nonstandardised, over-engineered and differing across locations, these solutions increase complexity even further.

HOW WOULD YOU RATE THE COMPLEXITY OF YOUR OVERALL BUSINESS (ACCOUNTING FOR FACTORS SUCH AS GEOGRAPHIC REACH, NUMBER OF BUSINESS LINES AND CUSTOMER SEGMENTS, ETC.)



2.

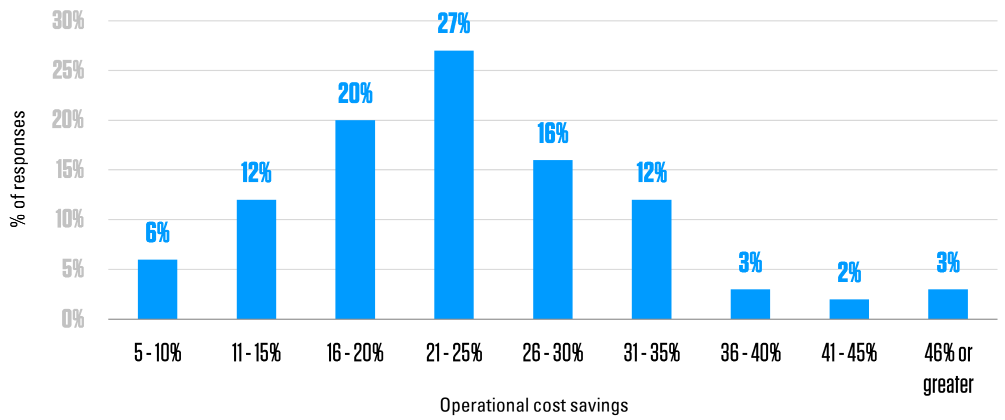
The bottom line – What do you expect to get out of the Utilities model in terms of measurable savings?

One of the promises of the Utilities model is a significantly more cost-effective approach to nondifferentiating processes. What, in operational cost savings terms, do respondents expect to get out of choosing Utility?

Remarks

Those respondents expecting cost savings of above 30 per cent are in the minority. Some 15 per cent would be happy with more modest (but still significant) impacts of up to 15 per cent. Most respondents desired 16 per cent to 30 per cent savings. The institutional profile is important here. Even those financial institutions that have a long established track record of sourcing in various forms can anticipate savings of around 20 per cent. For tier 2 banks in particular, which may to date have maintained a medium to high footprint in more expensive process implementation geographies, savings of 30 per cent (or higher) are achievable.

TO MAKE THE EFFORT OF MIGRATING TO A UTILITY MODEL WORTHWHILE FOR A PARTICULAR AREA OF BUSINESS OR OPERATIONS, WHAT OPERATIONAL COST SAVINGS WOULD YOU EXPECT TO ACHIEVE AS A MINIMUM?



3.

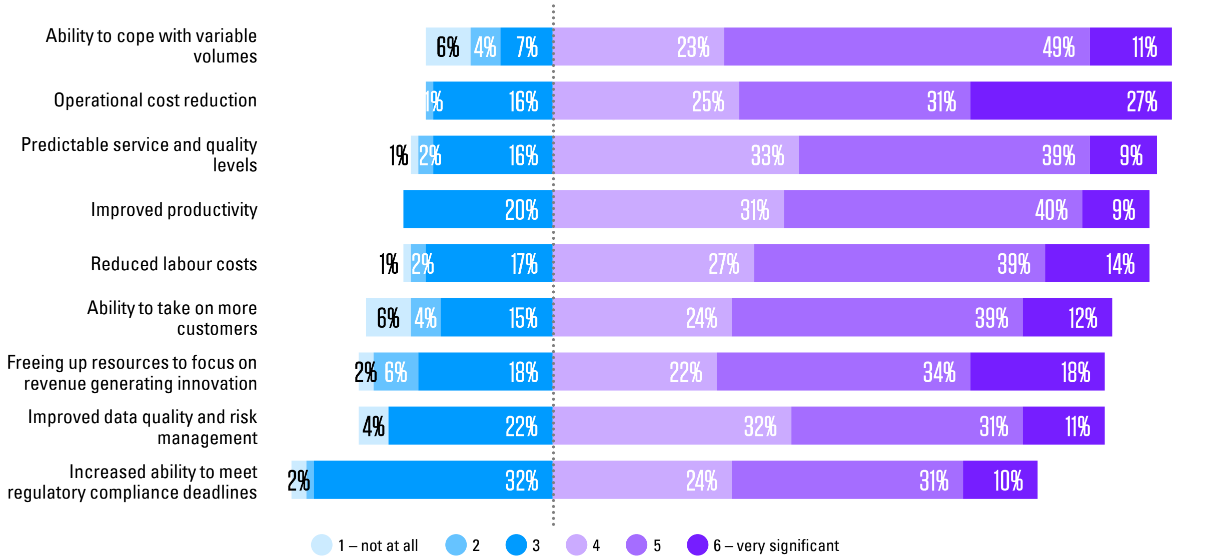
What are the operational drivers for Utilities adoption?

Cost reduction is not the only driver for Utilities uptake. We identified nine key areas of positive potential impact. Then we asked our respondents to rank their significance.

Remarks

There is a quintet of top drivers here that clearly underscores the reasons for Utilities adoption. The operational flexibility that comes from the ability to cope with variable volumes is paired with the ever more important issue of cost reduction. The second pairing is between predictable service and quality levels and improved productivity. Reduced labour costs occupy a position as fifth top driver. We can reasonably infer that the majority of financial institutions see Utilities as a route to lower-cost, high-volume and flexible processing, delivering predictable quality at a substantially lower price. These fundamental advantages are closely followed by some wider improvement and growth benefits, with new customer attraction, innovation focus and enhanced data and risk management issues all closely clustered. Interestingly, regulatory compliance is (slightly more than marginally) perceived as the least significant driver in this set, although it remains prominent.

PLEASE RATE HOW SIGNIFICANT THESE POTENTIAL BENEFITS ARE IF YOUR ORGANISATION MOVES TOWARDS A UTILITY MODEL



4.

How far have you gone toward applying the Utilities approach across your operation?

We asked respondents to confirm - for 11 key technology and operational areas - the extent to which they have engaged with the Utility approach, on a spectrum from "would not consider" to "have embraced as part of major restructure."

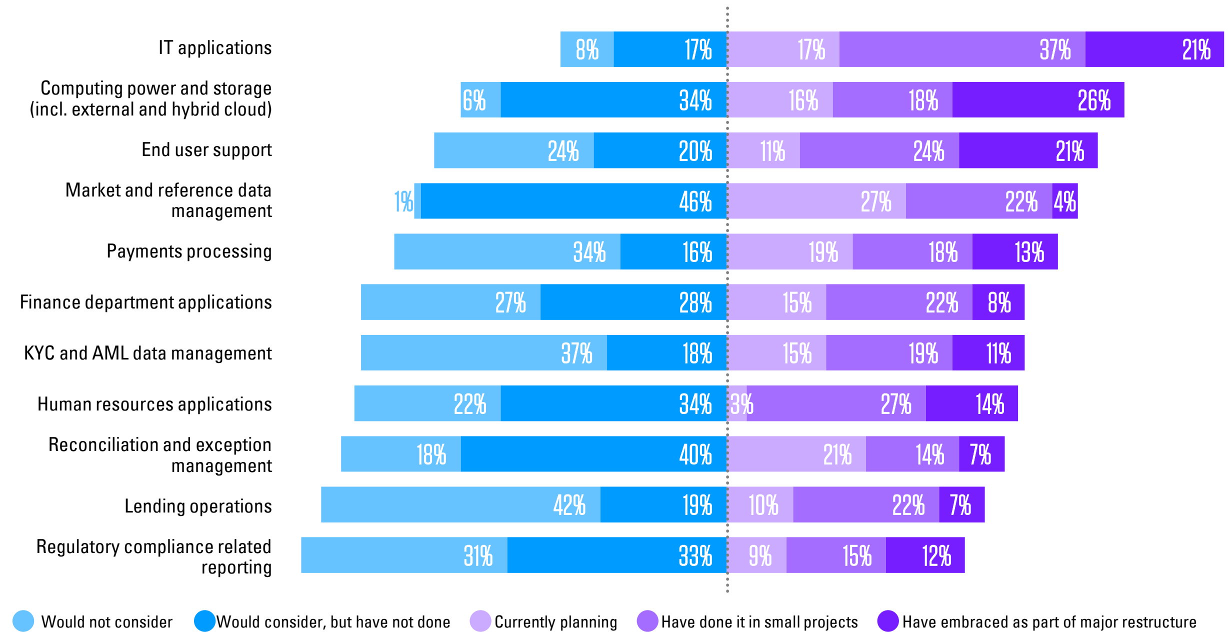
Remarks

The apparent and approximately even split between adopters and laggards can be credibly attributed to institutional profile differences among respondents. Here, we see IT Applications as the most mature Utility model offering, followed in descending but fairly close order by computing power, storage and cloud and end user support. Note that across these three key areas significant percentages of respondents are institutions that have embraced a Utility model as part of a major restructure. This suggests that, increasingly, Utilities are both a symptom of and are playing a central role in significant organisational and operational change.

Further evidence of this growing importance is provided by the percentages of respondents who have incorporated Utilities as part of a major restructure in payments processing (13 per cent), human resources applications (14 per cent) and regulatory compliance related reporting (12 per cent). While relatively low (7 per cent), the existence of Utilities-based approaches to the lending function as part of a major restructure is interesting. It signals a growing realisation that this historically high manual content activity can respond positively to automation and that Utilities can add value there.

As a rule of thumb, success with Utilities will lie in reviewing a function and determining which components are repeatable, low risk and sourceable. Institutions will likely continue to execute operational elements that carry significant decision process and risks. This analytical split will enable organisations to comfortably and securely address the cost base in most post-trade technology, operations and finance functions.

WITH REGARD TO EMBRACING A UTILITY MODEL, WHAT IS YOUR ORGANISATION'S STATUS IN THE FOLLOWING AREAS:



5.

What are the strategic drivers for Utility model uptake across the industry?

Sitting above the day-to-day operational issues is a set of more strategic drivers for Utility uptake. We identified three of those drivers and asked respondents to rank their significance.

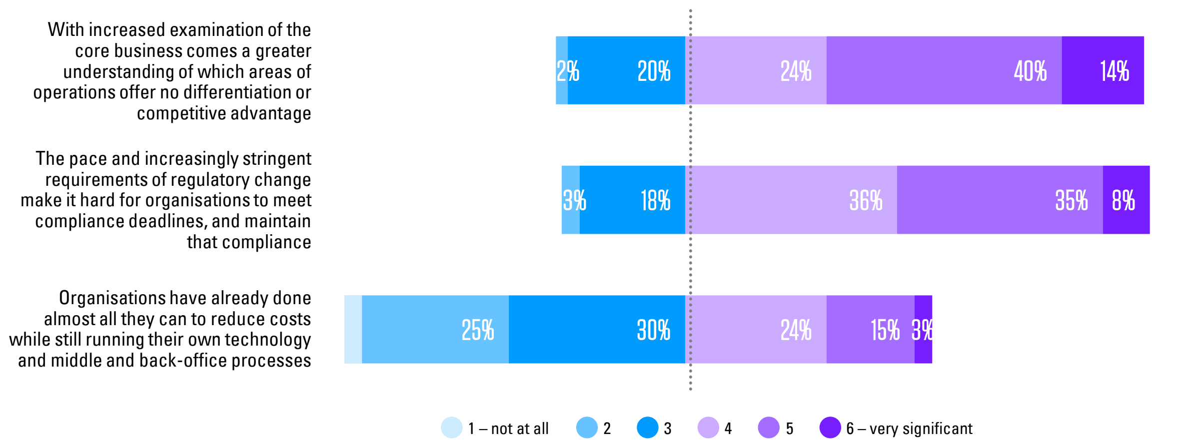
Remarks

A convincing majority of the surveyed market said strongly, or very strongly, that a close look at their business shows where the areas of value-add lie. This enhanced knowledge is surely a driver for Utilities adoption, to address clearly identified areas of nondifferentiating process. Three-quarters of the respondents see compliance as a driver. But this prominence contrasts with the 12 per cent, in the previous responses set, that have actually embraced Utilities as part of their active regulatory responses strategy. This discrepancy may be because many financial institutions are still in 'heads down' mode when it comes to operational responses to regulation. A Utilities model makes sense in principle. In practice, the reality of dealing with new regulatory demands remains a series of tactical fixes.

The final response around scope and scale of internal rationalisation/process efficiencies reflects the spread of respondent institutions. Roughly half the respondents – likely the tier 2 and tier 3 organisations – have still to fully examine and enact internal process cost savings. The other half – typically tier 1 banks – is experiencing a degree of fatigue with current and well-tried cost saving options in the sourcing arena. They are now looking to Utilities both for a radical approach and for greater cost reductions than their current options yield.

With every investment dollar under scrutiny, financial institutions must seek ways to share or mutualise costs where there is minimal differentiation. Then they need to reallocate budget to important areas of positive differentiation. Regulatory compliance continues to absorb a large percentage of investment, yet the underlying requirements are common across all participants in a given market, strongly suggesting that effective solutions in this space will become highly sought after.

ACROSS THE FINANCIAL SERVICES INDUSTRY, RANK THE SIGNIFICANCE OF THESE DRIVERS FOR THE ADOPTION OF POOLED UTILITY SERVICES



6.

What is preventing you from moving toward a Utilities approach?

We identified six potential obstacles to uptake of a Utility model and asked respondents to rate their importance within their operation.

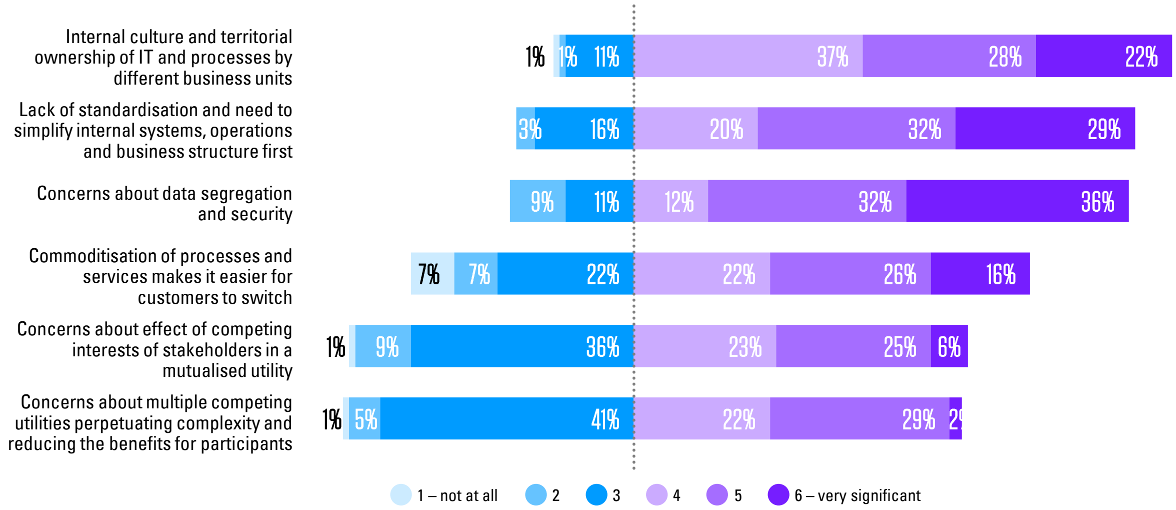
Remarks

The internal culture responses strongly suggest that "not invented here" remains alive and well at the centre of bank thinking. Often this goes beyond parochialism, carrying nothing short of an emotional charge. In organisational terms, a siloed structure adversely impacts capacity to adopt new and consistent cross-bank approaches. This is reflected consistently in the lack of standardisation responses. These suggest that significant numbers of financial institutions are still too internally complex, in terms of systems and structures, to easily adopt a standard cross-operational Utilities model. With core processing activities impacting multiple areas (front office, risk, compliance, finance, operations, etc.), driving Utilities uptake requires deep and sustained internal conviction. This must come from the top down and will demand leadership from the front.

Respondents reported, revealingly, anxieties around disappearance of complexity through simplification and commoditisation of process. The perceived downside is that simplification would make it easier for customers to switch from their current bank. From the institutional perspective, the entrapping effect of process complexity is positive for the stability of the bank business model. The big "but" here is that this positive-for-the-bank may in fact erode customer satisfaction and loyalty.

The roughly even split of responses to the final two questions suggests a broad mix of market perceptions. Some institutions worry about receiving a fair deal from a shared Utility. Others imagine a land of unintended consequences, where the Utilities that ought to simplify life and streamline process instead lock users into a different form of complexity. These reservations may well be attributable to tiers 2 and 3 respondents, who are as yet unfamiliar with the service level agreement frameworks that should come with the territory as part of a well-structured Utility service.

RATE HOW SIGNIFICANT THESE POTENTIAL OBSTACLES ARE FOR YOUR ORGANISATION MOVING TOWARDS A UTILITY MODEL




REGULATORY COMPLIANCE CONTINUES TO ABSORB A LARGE PERCENTAGE OF INVESTMENT, YET THE UNDERLYING REQUIREMENTS ARE COMMON ACROSS ALL PARTICIPANTS IN A GIVEN MARKET, STRONGLY SUGGESTING THAT EFFECTIVE SOLUTIONS IN THIS SPACE WILL BECOME HIGHLY SOUGHT AFTER.

Do the survey results validate our prior assumptions?

At the outset, we shared our set of pre-survey assumptions around the key obstacles to Utilities uptake:

- Cultural and organisational issues within banks
- Lack of standardisation and fragmented and complex processes
- Anxieties around data security and related issues

Does the survey data evidence support these assumptions?

Cultural and organisational issues – The overwhelming majority report internal culture splits and 'territorial' ownership of IT and process as a barrier to Utility model uptake. Assumption justified.

Fragmentation and technology complexity – As a likely corollary of the first issue, the vast majority of respondents cite internal lack of consistent standards as a barrier to employing an external, cross-operational Utility platform. Assumption justified.

Data security and related issues – Some 80 per cent of respondents rate these concerns from significant to very significant. There can be no doubt that the security and effective segregation of data in a pooled Utility model remains a live issue. Yet, more than three-quarters of the surveyed market, paradoxically, see improved data quality and risk management as a driver toward Utilities uptake. Assumption justified, but clearly financial institutions have an appetite for greater efficiencies.

Emerging issues

Are there other key trends that should receive focus going forward? Certain Utility approach issues were not on our radar to as great an extent before the survey. We discuss three of the key issues below.

Banks are concerned that more consistent cross-industry process will reduce customer "lock-in". Some 80 per cent of respondents expressed, to some extent, concerns that commoditisation of processes and service will make it easier for their customers to switch banks. This view appears to confuse consistency, a good thing, with the idea that predictable processes will somehow reduce the distinctive appeal of the offer. Or, perhaps, the reasoning is that current complexities "lock in" customers. They "helpfully" contribute to consumer inertia when it comes to moving banks.

The brand and reputational issues involved here join more concrete factors: in some jurisdictions, government stimulus of banking competition already translates into regulation. The UK, for example, requires banks to facilitate a current account switch in just seven days. This will inevitably be an important factor in overcoming consumer inertia. It will also drive further demand for process standardisation and simplification. As banks find they have no option but to provide real choice for account holders, this area of resistance to the Utilities approach seems likely to decline.

Banks are concerned about maintaining their fair share of access to a shared Utilities-style service, when co-utilising it with other institutions. Well over half of those surveyed appear to have a range of concerns around getting a fair deal from a mutualised Utility. This reflects concerns expressed, for example, in Germany by certain categories of bank. When financial institutions partner with each other to create a shared utility, inevitably concerns will arise around the relative service entitlements of senior and junior partners. Industry experience to date strongly suggests, however, that adequate upfront focus on accurate and tailored key performance indicators, reinforced by careful service level agreement drafting, can prevent or substantially mitigate any such unequal treatment.

Banks are concerned about replacing current processing complexities with a set of different but equally challenging issues, if they choose the Utilities route. Again, well over half the respondents had concerns that Utilities could result in unintended consequences. In effect, a new model might replace the complexity they know with unfamiliar and perhaps tougher challenges. This reaction seems attributable, reasonably, to unfamiliarity. Tier 2 and 3 banks, for example, are still learning about the particulars of the Utilities approach. Also, many of the reservations around doing something different and more radical may have less to do with the new platform than with the challenges of change itself. Many financial institutions, as confirmed by our respondents, still face substantial challenges around organisational and technology complexity and fragmentation. It may well be that the prospect of overcoming such issues, as opposed to any direct reservations around Utilities, is the real concern.

Significant proportions of our survey respondents said they had embraced the Utility model as part of a major restructure.

Where do we go now with the pooled Utility model?

Despite three decades of progressive growth in sourcing and the emergence of the Utility model, many banks still hold on to internally executed processes, incurring significant and addressable expense. This happens in areas that contribute little or nothing to positively differentiating the customer experience or growing the business.

Regulatory maturity – One of the most important and costly areas is operational response to **regulatory change**. Here, banks spend billions without achieving true regulatory maturity, defined as the predictable ability to satisfy regulatory standards and timetables. Along the way, failures in compliance continue to attract enormous fines and cause substantial reputational damage.

It is striking that just under 80 per cent of the surveyed market sees regulatory change as a major driver of Utilities adoption, and yet 64 per cent of the same sample have not considered or taken any action to pursue the application of Utilities to their own regulatory change capabilities. Only 12 per cent have fully embraced the Utility model in this context.

One potential explanation of the disparity is that financial institutions are too busy just doing the work of compliance. It is challenging to make the time available to examine regulatory response approaches strategically. However, with the unrelenting volume of regulatory changes and burdens, more institutions will realise that reactive and tactical regulatory response initiatives alone are inadequate and too expensive. Over time, the desire to take more effective action will translate into more radical approaches.

Fully independent Utility platform – The next focus area banks should reconsider is the operation of mutualised utilities where several users are involved. As we have seen, more than half the market surveyed has concerns about potential conflicting interests. It is easy to predict scenarios of peak demand when everybody involved will want everything at once, and some institutions' interests must come second – bad news for them. How can these limitations be overcome?

One answer lies in a move to a fully independent Utility platform. This platform will rely on specialist external fintech expertise to assure the most appropriate technology choices and operating approaches. Crucially, it will also provide industrial-strength capacity for all users, removing internal competition. Instead of limited, isolated capability, a process supply grid will scale and flex to support all users fully at all times. Thus, all users have the assurance of key performance indicators and a service agreement framework that accurately reflects their specific operational needs.

Regulatory Utilities – Applied in the context of **regulatory response**, this could revolutionise the current situation. We can even envision a series of regulatory Utilities that match the regulators' drive toward standardisation and consistency. These Utilities will provide cost-effective processing capabilities on an agnostic basis to all users. They will reduce the risk of fines for noncompliance. Potentially, they can even provide an automated, instant and credible platform for regulators to validate compliance, on a machine-checks-machine basis. Contrast this with the awkward and hugely expensive inspection regimes at work today. Without radical changes in approach, both the regulators and the banks will need to continue to pump resources into compliance for the foreseeable future.

Next steps

Our suggested next step, for any institution that has not already done so, is to apply the three-stage approach referenced at the beginning of this paper.

Mutualisation – Examine a task in detail. Identify and quantify the mutual interests and advantages (across a bank group or among a group of separate banks) in approaching this task much more efficiently.

Front-load the development schedule with a heavy focus on asking the right questions.

- Why is the mutual approach potentially better than an in-house solution or a conventional piece of BPO?
- What are the timescales for significant cost savings delivery? (Expect 24 months as a realistic benchmark.)
- What are the most relevant key performance indicators for the institution’s specific situation and needs?
- What are the appropriate service level agreements to protect the institution’s interests at all times and assure adherence to predictable quality and cost parameters?

Standardisation – Examine the core operational elements related to the task identified above. Find a route to standardisation that makes use of as many common technologies and approaches as possible. If there is little or no commonality at the outset, this may involve significant change. (Remember, significant proportions of our survey respondents said they had embraced the Utility model as part of a major restructure.)

Utilisation – Develop and implement a Utility-based concept. This may be shared by a few or several banks, or even be industry-wide. It may even be provided agnostically, through a fintech-developed platform. In any context, the key to successful utilisation is the **right balance** between highest quality and lowest cost, pay-for-usage, shared service in technology, data or process management, and individual institutional control.

Here, control means protection through effective oversight rather than total domination through de facto infrastructure ownership or constant micromanagement. Oversight mechanisms must be in place to ensure that service level agreements translate into continuously satisfactory achievement of key performance indicators. However, it must be emphasised that the objective here is smart control: consistent high-quality delivery, protection from any regulatory noncompliance vulnerabilities and measurable cost reductions – not continuing to bear majority responsibility for the infrastructure or expending as much (or more) management time than in the pre-Utility state.

End benefit – The end benefit of this three-stage approach is that the institution can replace a fragmented landscape with a set of common approaches. It can radically reduce the number of variables. It can enable fixed or predictable price process operation at significantly lower cost. And it can liberate more resources for differentiating and growth activities. Banks can achieve all this in a context of far more predictable compliance and without relinquishing the mission-critical oversight required to meet regulatory responsibilities.

Many of the reservations around doing something different and more radical may have less to do with the new Utilities platform than with the challenges of change itself.

Conclusion and outlook for 2016

Financial institutions, having experienced several consecutive years of stringent cost management, have reached the limits of conventional cost reduction opportunities. Infrastructure renewal and partnerships to radically simplify the existing technology estate would seem likely focus areas because they will return the highest reward. Given the burden of cost and the challenging effort required for change, we anticipate an increase in shared initiatives among participants, with solution design and software delivered by third parties.

There are, as we have seen, areas of strong support for Utilities already. So, what currently impedes the adoption of Utilities? There are at least four major factors at work: fragmentation, lack of standardisation, expectation of strict control and lack of trust.

First, banks remain concerned about silos – cultural and operational fragmentation – as serious barriers to Utilities uptake.

Second, ad hoc responses to regulatory requirements obstruct technology standardisation, preventing the emergence of a consistent cross-bank and cross-industry response. This counterproductive cycle delays the necessary conditions for the Utility model to realise its full potential.

Third, banks cannot outsource responsibility in the regulatory response arena. Irrespective of the processing approach and the underlying technology platforms, banks are almost always the liable party if noncompliance is established (there is limited accreditation of some third-party service providers). This leads them very often to limit the full potential and scope of a Utility-based solution, because they insist on a large element of control.

Finally, the culture of trust – either of other (rival) players or third-party fintechs – is still emerging. Many institutions do not want to be first (or even second or third) in a multi-tenanted Utility. The approach has been one of wait and see, mixed with the idea that "nobody else could possibly be trusted with our data."

Faced with these obstacles, why should financial institutions continue to adopt and implement Utilities? The ultimate answer lies in the benefits of joining the dots between areas still seen as separate: organisational and operational best practice, cost savings, technology best value, predictable regulatory response, improved customer experience, competitive advantage and growth.

How will 2016 impact Utilities uptake?

PRESSURE ON COSTS WILL CONTINUE, deriving from a range of drivers, from cost of capital and the need to address the fixed cost base to the effects of continuing regulatory rollout. This will have two direct impacts. First, institutions that have done all they can with various forms of BPO will have to consider new cost reduction levers, including Utilities. Second, banks that have until now retained all their own infrastructure, or very substantial elements thereof, will have to look at cost reduction. Many will bypass the more established routes and engage with a Utilities model.

UTILITIES UPTAKE WILL BE DRIVEN BY GROWING REALISATION OF THE FAVOURABLE DEALS AVAILABLE TO EARLY ADOPTERS. Utilities providers are typically in for the long game. Even where their business models are predicated on profitability derived from multi-tenanted solutions, they will offer very attractive savings to those banks that are first, second and third in. This means early adopters have a considerable commercial advantage and a strong business case incentive to overcome any reservations.

THE PROFILE OF UTILITIES WILL GROW THROUGH INCREASED UPTAKE. And, as a corollary, so will industry trust levels. We are at the tipping point with Utilities adoption. In just one recent example, a major tier 1 player joined a pooled utility service for its US securities operation, bringing a processing volume that dwarfed all the existing service users' requirements combined. Within a short time period, three comparable global institutions took the same decision, providing an example to their peers and a gravitational pull for the wider industry. This scenario looks likely to replicate through 2016, as examples of Utilities uptake become less hidden.

BANK PERCEPTIONS OF CONTROL WILL EVOLVE. It is clear, not least from the volume and value of fines for noncompliance, that exclusively in-house responses to regulation are not working. Yes, many financial institutions are preoccupied with the raft of regulator-imposed initiatives they must develop, fund and implement. But as Utilities providers' expertise grows around building oversight mechanisms and control functions, banks will

In any context, the key to successful utilisation is the right balance between highest quality and lowest cost, pay-for-usage, shared service in technology, data or process management, and individual institutional control.

increasingly realise that cost reduction does not imply greater regulatory vulnerability – quite the opposite in fact.

MORE BANKS WILL CLEAR UTILITIES FOR TAKEOFF. Of one, final, prediction there can be little doubt: Utilities will certainly not disappear in 2016. Over time, even the most organisationally complex and culturally sceptical institutions will realise that appropriate shared services are the way forward, even in a heavily regulated industry. After all, multiple competing airlines safely share mission-critical service provision, from baggage handling to refuelling to air traffic control. Equally, multiple competing banks can share a raft of nondifferentiating services (even those with high-level criticality), freeing up increased resources to focus on the core of their business: their customers.

1. For our survey, we defined a "pooled Utility model" as the use of an external party that serves multiple customers to provide a pay-for-usage service in technology, data or process management.
2. http://www.fisglobal.com/C031922.
3. https://www.sungard.com/company/newsroom/press-releases/2015/utilitypr2015.
4. Markets in Financial Instruments Directive II.
5. European Market Infrastructure Regulation.

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