

Fund Processing Standardization

Tracking industry progress



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Preface

In its resolution of 13 December 2007 on Asset Management II , which was prepared by MEP Wolf Klinz, the European Parliament welcomed the establishment by EFAMA of the Fund Processing Standardization Group (FPSG) and other initiatives to improve fund processing.

Indeed, the industry has made good progress since the publication of FPSG's initial recommendations in 2005. Just to name a few landmarks - market participants are investing in ISO 20022 as the key messaging standard for fund processing. Support for the Fund Processing Passport has been strong with valuable lessons learnt from pilot implementation.

Having published the initial recommendations of the FPSG in 2005, covering order and settlement process, EFAMA has published a new report in September 2008 in order to update these earlier recommendations to reflect the current landscape and thinking and extend their scope. In the report EFAMA also indicated that it is determined to monitor a range of fund processing standardization indicators that will enable it to monitor the industry's progress towards greater harmonization and automation, from data gathered from the industry.

The inefficiencies of fund processing are most apparent in the cross border distribution of funds. This is a very important segment of the European fund industry, which is now offering UCITS as a global brand far beyond Europe, in particular to Asia, Latin America, and the wider EMEA region.

We very much welcome the initiative of SWIFT to help EFAMA monitor the progress of fund processing based on a survey of transfer agents (TA), initially those from Luxembourg, and soon to be expanded to transfer agents from Ireland. Given the huge importance of these two fund domiciliation hubs for the cross border distribution within and outside Europe, the report definitely has the focus right on the problems.

Surveys of other domestic European markets may complement the survey at a later stage. The report demonstrates that much has been achieved in the fund processing of cross border trades, but more can be done and the effort must continue. Only when the necessary changes are implemented by all industry players, political pressure on the industry will relent and regulatory action may be avoided.

More important, however, investors will benefit from better service, reduced risk and less cost!

Rudolf Siebel, FPSG chairman

1. Report highlights

1.1. Scope

Survey covers 75% of Luxembourg volumes

This report covers the period starting January 2007 to December 2008. It covers third-party fund distribution of Luxembourg domiciled funds and captures the standardization and automation rates evolution of orders received by Luxembourg-based transfer agents from external order givers (third-party distributors and fund hubs).

The report is based on the input from 19 Luxembourg based transfer agents to a joint EFAMA-SWIFT survey. The survey covers an estimated 75-80% of the total Luxembourg order volumes and captured automation data on a volume of more than 15 million orders in 2008.

1.2. Standardization rate evolution

Luxembourg reached 66% automation rate in Q4 2008

The level of ISO standardization has increased by 6.3% since Q1 2007 to reach 41% in Q4 2008. When we combine both the ISO standardization rate with the proprietary formats automation rate, Luxembourg transfer agents reach a total automation level on incoming orders of 66% in Q4 2008 (+ 7.6% vs Q1 2007).

ISO drives the growth of automation

Most of the growth in automation (83% of it) comes from ISO open-market standard adoption by fund players, in line with the recommendations developed by EFAMA's Fund Processing Standardization Group (FPSG).

Still >5 million manual orders in 2008 though

In 2008, 9.7 million orders were received in an automated way versus 5.3 million orders received manually.

This highlights the importance of pursuing the efforts to further improve the fund industry standardization rate, so as to reduce operational costs and risks, and improve scalability and service levels.

1.3. Variation in standardization rates based on order giver location

1.3.1. Regional split of order volumes¹

Europe stands for 65% of order volumes

About 65% of order volumes originate from order givers based in Europe, the Middle East and Africa (the EMEA region). The bulk of these orders is attributable to EU-based order givers: indeed Middle-East /African cross-border fund business translates rather into low volume – high value order flows. Another 30% of the volumes come from order givers based in the Asia-Pacific countries (APAC region) and the remaining 5% from Americas'-based order givers. These figures confirm the importance taken by UCITS as a global brand.

1.3.2. Standardization rates evolution

46% of EMEA orders are ISO standardized

ISO standardization rates are much higher with EMEA-based order givers: it stands at 46% of the 2008 total order volumes (against 8% in APAC²). When we look at the manual rate per region for 2008, it translates into the following pattern:

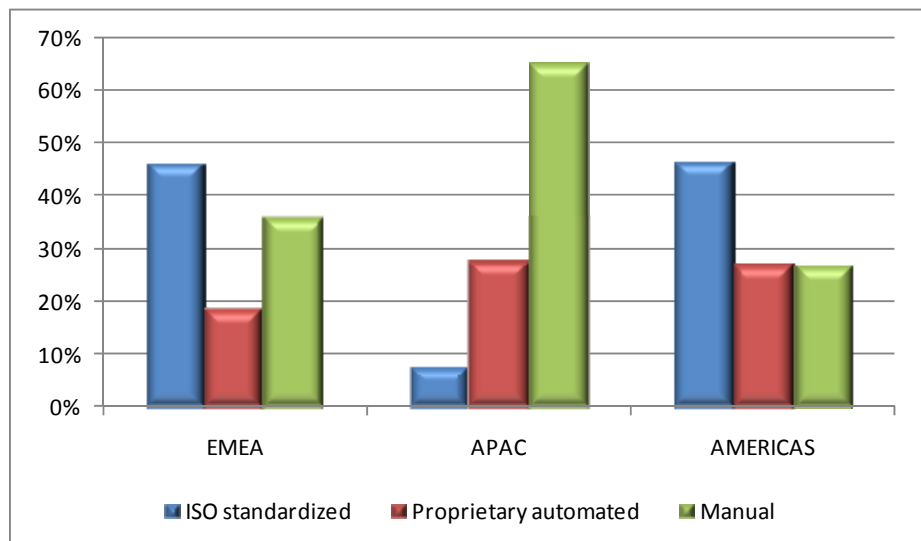


Figure 1: Automation rate evolution per region

¹ Please note that regional data is based on contributions of 12 out of the 19 transfer agents. This explains data variations compared to the full survey sample statistics.

² The 8% APAC standardization rate is probably under-estimated since EMEA-based large fund platforms do channel via ISO a growing number of Asian orders to Luxembourg transfer agents. The latter volumes are however classified by most survey contributors under the EMEA heading and not the APAC heading.

65% of APAC orders still manual

Automation and standardization campaigns have only more recently been launched in Asia-Pacific (e.g. by the Asia Fund Automation Consortium - AFAC). They need to be beefed up to align automation rates with EMEA and Americas' ones

2. Survey scope and methodology

The main steps carried out to publish this survey in accordance with the methodology jointly defined between EFAMA and SWIFT are outlined below:

Luxembourg cross-border third-party mutual funds

a) Survey scope:

- Instruments: cross-border third-party investment funds (mostly UCITS)
- Flows: orders received by the transfer agent from 'external' order givers (not in-house)
- Markets:
 - o Phase 1: Luxembourg investment funds (focus of this first 'progress report')
 - o Phase 2: Irish investment funds (see Next Steps)
 - o Contributors: in-house and third-party TAs

19 transfer agents >75% market coverage

b) Survey contributors:

- Survey contributors are solely transfer agents. This choice was made to avoid duplication of data with order givers.
- The target is to have a sufficient number of contributors to cover at least 70% of estimated total market volumes.
- 19 transfer agents have contributed to this first progress report
 - o 10 in-house transfer agents
 - o 9 are third-party transfer agents
- Contributors include a good mix of large/medium/low volume players
 - o 5 TAs received above 1 million orders in 2008
 - o 7 TAs received between 0.5MM and 1MM
 - o 7 TAs received less than 0.5MM orders
- We estimate that this progress report covers more than 75% of order volumes in Luxembourg³.

³ This estimation is based on volumes data reported in the September 2007 Deloitte-Clearstream study on cross-border fund distribution in Europe and the subsequent interviews on the volume growth in 2007.

***Joint EFAMA –SWIFT
survey supported by
the TA industry***

c) Survey management and reporting:

- SWIFT carried out the joint survey, and reported the outcome at market level to the EFAMA’s Fund Processing Standardization Group (FPSG), as well as relevant local fund industry associations.
- Contributors provided monthly automation data.
- The minimum core data to be provided is:
 - o Total number of fund orders received
 - o Split of the total number of orders between:
 - orders received by fax/telephone (‘manual’)
 - ISO standardized messages/files (ISO 15022 and 20022 carried on swift and/or another automated channel)
 - Use of multiple bilaterally agreed proprietary formats
- Recommended additional data (provided for this report by 12 out of the 19 contributors) is:
 - o Same data set as above-mentioned, split by region where the order giver is located. Three regions are identified : EMEA , APAC and Americas.

***Bi-yearly market
reports***

The goal is to issue a progress report once a year to cover end-year data. A mid-year status is also planned to report the evolution of standardization rates during the first six months of the year.

3. Progress report

3.1. Scope

Very good mix of contributors to the survey

Period covered	Jan 2007 – December 2008
Market covered	<ul style="list-style-type: none"> • Luxembourg investment funds (mostly UCITS) - third-party distribution focus • External orders received by transfer agents (TA system-generated orders are excluded – e.g. auto-generated savings plan orders are excluded)
Survey contributors	<p>For the <u>global data</u>:</p> <ul style="list-style-type: none"> • 19 Luxembourg transfer agents: • By type: 10 in-house and 9 third-party, of which • By volume: 5 with >1 MM orders/year, 7 with 0.5-1MM & 7 with <0.5MM <p>For the <u>regional data</u>:</p> <ul style="list-style-type: none"> • 12 out of the 19 contributors: • By type: 8 in-house and 4 third-party
Survey coverage	<p><u>For the global data</u>:</p> <ul style="list-style-type: none"> • 2007: 17.4 million orders • 2008: 15 million orders = Estimated >75% market coverage (by order volumes) <p><u>For the regional data</u>:</p> <ul style="list-style-type: none"> • 2007: 10.3 million orders • 2008; 8.2 million orders = 57% of the survey volumes (for 2008)

3.2. Order volumes evolution 2007-2008

3.2.1. Order volumes evolution

Order volumes decreased by 14% between 2007 and 2008. Volume volatility is high as depicted in the graph below: transfer agents have experienced 7 major variations (between 20% and 40% increase or decrease) of monthly order volumes over the period 2007-2008.

Order volumes are very volatile

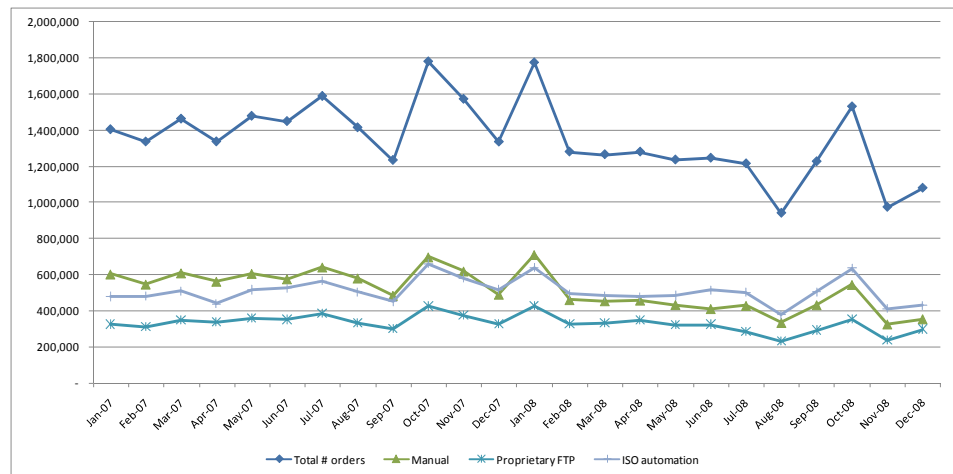


Figure 2: Order volume evolution

Volume volatility is comparable in EMEA and APAC:

Automation required to manage volume peaks smoothly

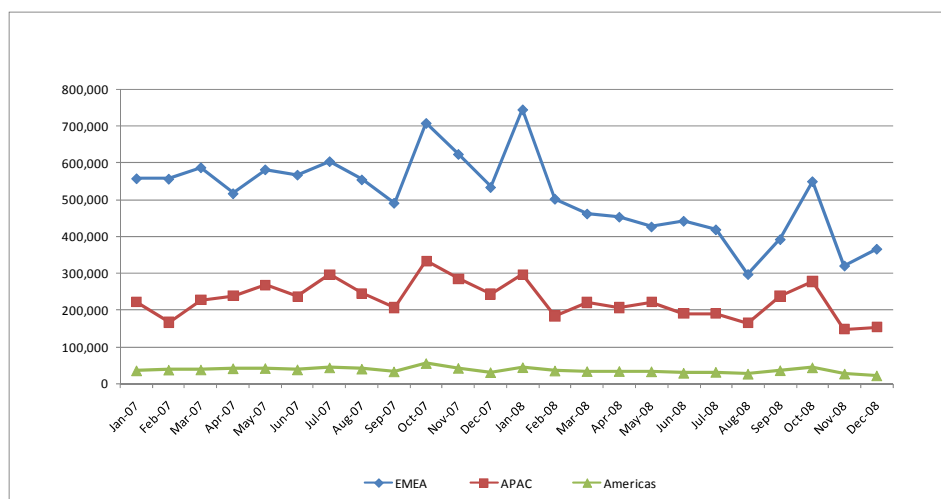


Figure 3: Order volume evolution per region

The high volatility rate is another important reason for achieving a high automation rate to manage smoothly unexpected peaks in volumes.

3.2.2. Regional split of order volumes

Europe stands for 65% of order volumes

About **65% of order volumes** originate from **EMEA-based order givers** (vs 67% in 2007). The bulk of these ‘EMEA volumes’ are attributable to EU-based order givers: indeed Middle-East/African cross-border fund business translates into low volume – high value order flows. 30% of orders come from APAC (+1%) and 5% from the Americas (+1%)

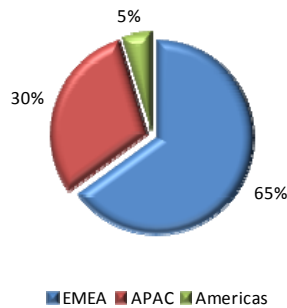


Figure 4: 2008 Luxembourg fund order volumes

The drop in volumes observed in 2008 was stronger for EMEA order givers than for APAC order givers⁴.

Volume drop is higher in Europe



Figure 5: 2007-2008 volume evolution per region

⁴ Please note that the sample for regional data is based on input from 12 TAs out of 19. This explains the lower total number of orders reported in Figure 5.

3.3. Standardization and automation levels

ISO standardization rate at 41 %

The level of ISO standardization has increased by 6.3% since Q1 2007 to reach 41% in Q4 2008.

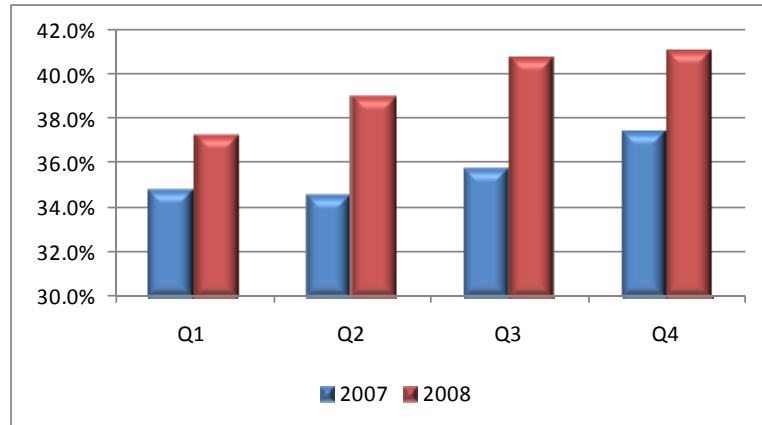


Figure 6: 2007-2008 ISO market share evolution

Total automation level at 66%

When we combine both the ISO standardization rate with the proprietary formats automation rate, Luxembourg transfer agents reached a total automation level on incoming orders of 66% in Q4 2008 (+ 7.6% vs Q1 2007). So most of the growth in automation comes from ISO open-market standard adoption by fund players - in line with the EFAMA's recommendations.

	Q1 2007	Q4 2008	Progress
ISO standardization rate	34.9%	41.1%	+6.3%
Total automation rate	58.3%	65.9%	+7.6%
Manual rate	41.7%	34.1%	-7.6%

Figure 7: 2007 – 2008 total automation rate evolution

The chart below depicts the monthly fund orders automation rate evolution over 2007 – 2008: ISO standardization adoption has gained momentum in 2008 and has consistently exceeded manual rate since February 2008.

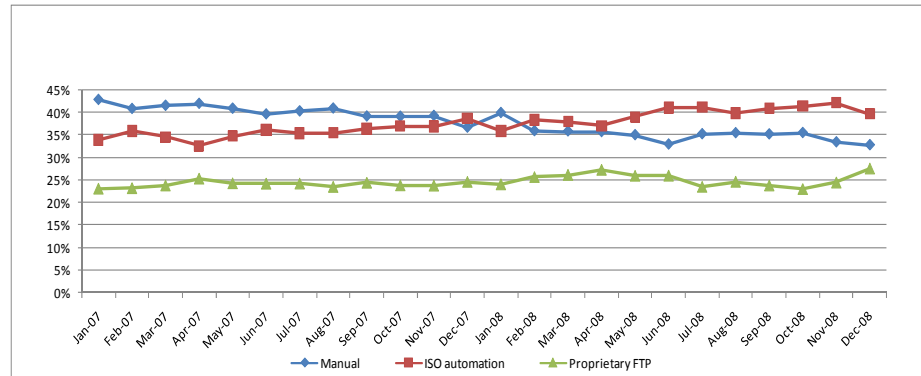


Figure 8: Automation rate evolution Luxembourg market

Still > 5 million manual orders in 2008

Manual orders still represented 36% of the total 2008 volumes (-4% vs 2007), down to 34% Q4 2008. This is a good evolution compared to Q1 2007 where the manual rate was about 42%. However this still translated over the whole year 2008 in 5.3 million manual orders (versus 7 million for the whole year 2007).

3.4. Variation in standardization and automation levels based on order giver location

Higher automation rate in EMEA

Much higher ISO standardization rates are achieved with EMEA-based order givers (47% in Q4 2008) than with APAC-based order givers (8%⁵ in Q4 2008). Americas-based order givers rate is the same as EMEA (47% in Q4 2008).

A similar pattern exists for the total automation rate (Q4 2008): 63.5% for EMEA, 36% for APAC and 73% for Americas.

	ISO Standardization rate			Full automation rate (ISO + proprietary formats)		
	EMEA	APAC	Americas	EMEA	APAC	Americas
Q1 2007	41.0%	5.7%	48.9%	58.8%	32.6%	79.1%
Q4 2007	46.8%	5.8%	45.3%	66.4%	31.0%	75.8%
Q4 2008	47.3%	7.7%	47.2%	63.5%	36.2%	72.9%

Figure 9 : Rate comparison per region

⁵ The 8% APAC standardization rate is probably under-estimated since EMEA-based large fund platforms do channel via ISO a growing number of Asian orders to Luxembourg transfer agents. The latter volumes are however classified by most survey contributors under the EMEA heading.

The below graph highlights the different regional standardization and automation rates in 2008:

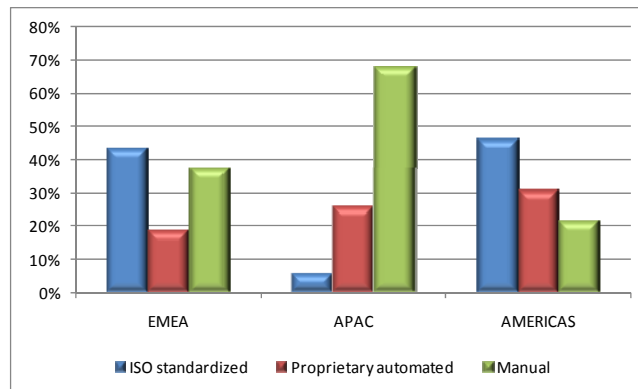


Figure 10: Automation rates evolution per region

ISO standardization progresses in APAC

In APAC ISO standardization has progressed by 2% and proprietary formats automation rate by 1% over 2008.

Manual rate in APAC still at 65% in 2008 however

Manual rate is still extremely high: 65%. This is partly due to the fact that automation and standardization campaigns have only more recently been launched in Asia-Pacific. The challenge for the automation/standardization business in Asia is the investment cost required and the low FTE cost. Operational risk reduction and enhanced service level will generally be stronger drivers of standardization for distributors in APAC than operational cost reduction.

4. Next steps

Luxembourg cross-border market: A mid-year progress status is planned for publication in September 2009.

Irish cross-border market: a first report for 2007 – June 2009 is planned for publication in September 2009.

The second annual report presenting the situation at end 2009 will be published in March 2010.

Glossary

AFAC	Asia Fund Automation Consortium: a informal group of major fund houses promoting ISO automation of fund operational flows
alfi TASC	Transfer agent working group at the 'Association Luxembourgeoise des Fonds d'Investissement' (Luxemburg fund association)
APAC	Asia-Pacific region
EFAMA	European Fund and Asset Management Association
FPSG	EFAMA Fund Processing Standardization Group
EMEA	Europe - Middle-East - Africa region
EU	European Union
FTE	Full Time Employee
ftp	File transfer protocol
total automation rate	Total number of ISO + proprietary formats orders received by the transfer agent via an automated channel divided by the total number of orders received by the transfer agent
ISO standards	ISO stands for International Standards Organisation. ISO issues open-market global standards
proprietary format automation rate	Total number of orders received by the transfer agent that are formatted in bilaterally agreed proprietary formats divided by the total number of orders received by the transfer agent
ISO standardization rate	Total number of <u>ISO</u> (ISO 15022 and/or 20022) formatted orders received by the transfer agent via an automated channel (swift and/or another communication channel) divided by the total number of orders received by the transfer agent
STP	Straight Through Processing
transfer agent	The operational agent in charge of processing fund orders and managing the register of shareholders when applicable. It can be a third-party service provider or an in-house department at the fund manager