SmartStream

Reference data: working smarter

SmartStream has recently joined forces with Goldman Sachs, JP Morgan Chase and Morgan Stanley to create Reference Data Services LLC, an industry-led service using the SmartStream Reference Data Utility. Philippe Chambadal, CEO, SmartStream, tells FX-MM why the initiative can transform reference data management and why the utility approach has the potential to boost efficiency and lower trading costs across the financial industry.

Philippe Chambadal
SmartStream

Why are banks looking to adopt utility models for their trade processing requirements?

The cost of running post-trade operations within banks is unsustainable. It is as simple as that. For 30 years during the bull market that preceded the financial crisis, they did nothing to improve their systems. If there was a problem, they just hired more people. As a result, 30 years later they found themselves with thousands of people in their back offices.

The reason why there are so many people in financial firms' back offices is because there is no straight-through-processing. You have broken everything within banks' back offices: broken payments, broken transactions, broken corporate actions and broken reference data. All of this needs repairing and a lot of those repairs are done by hand.

There needs to be not only a re-tooling of the back office, but also a rethinking of the processes. Banks need to understand what processes give them a competitive edge – and which are better managed in house – and which do not. Processes in which there is no competitive edge, and which cost a lot of money, are better managed as a shared service.

What makes reference data suitable for the utility approach?

Five years ago, many banks believed that good reference data management represented a competitive advantage and that they needed to control it themselves, and build the best systems.

We were arguing that the opposite was the case: banks were creating a problem for themselves and their counterparties. What you want is to have the same data as your counterparties. It is not about having the best data – having the best data is like having the best electricity; at the end of the day you just want the lights to turn on.

That is the essence of the problem: banks can spend any amount of money on the problem but if their counterparty has bad reference data then a trade is going to break anyway.

Put simply, banks want to clear their trades. They realised that reference data management costs were getting out of control and what they had been doing for the past 30 years was not working. They realised they had to mutualise the cost and move to an industry utility model.

What are the potential benefits of the utility approach?

Typically, the large sell-side banks spend between $50 million to $100 million a year on reference data management. We can take over that function that exists in-house and do it once for the entire industry. There is a direct cost saving in terms of banks not doing the work themselves, but the largest cost saving is downstream, because bad data breaks trades. For every $100,000 financial firms spend on reference data management, we estimate they spend between $300,000 and $500,000 on repairing trades that were broken by bad data.

Overall, the waste in the post-trade space caused by broken trades is thought to be between $50 billion to $65 billion per year. 30% to 40% of that, around at least $15 billion, is caused by bad reference data. The ripple effect of bad data in post trade is gigantic. If financial institutions use the same high quality data model, those trade breaks are going to disappear.

What makes SmartStream's Reference Data Utility up to the task, and why was it chosen as the framework for the new bank-led initiative?

Unlike other vendors, which have bought existing companies active in data management and tried to change them into utilities, our system from the start has been, by design, multi-tenanted, with the ability to scale to a huge level. From the get-go it has been designed as a utility.

We cross reference so that firms' internal systems can speak the same language, and then when they come to settle a trade with a counterparty, they have common keys and a common data model so trades don't break. We can reduce clients' marginal cost by 30% to 50%, and eliminate 80% to 90% of trade breaks due to reference data management mismatches. From the start, we can save clients tens of millions of dollars. We think we are at least three to four years ahead of our nearest competitor.

For further information: www.smartstream-stp.com