

The Future of Custody

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The investment industry, and its associated supply chain, are at an inflection point where the future begins to look progressively different from the past. While there are many factors that underpin this change, two stand out: the quest for alpha and the growing demand for new products and strategies, including the search for absolute returns, from rapidly retiring baby boomers.

In the aftermath of the dot-com bubble and the market timing issues in the U.S., regulators across the world will continue to aggressively look to harmonize markets and protect the retail investor.

The effects of these trends resonate across the entire value chain from issuers requiring support for CDOs or execution of LDI strategies, to investments in an ever expanding set of markets with increasingly sophisticated instruments (e.g. complex derivatives). Thus, as the front office becomes more complex so will the mid- and back-office. The winners in this game will be those who can find creative remedies to these needs and are able to turn the traditional axiom on its head by doing more for less.

Several tightly interconnected, highly interrelated factors are driving and shaping the future of custody, and more broadly, the investment servicing industry:

Globalization

Globalization has traditionally been understood to be the opening of new emerging markets in the search for incremental returns. No doubt that



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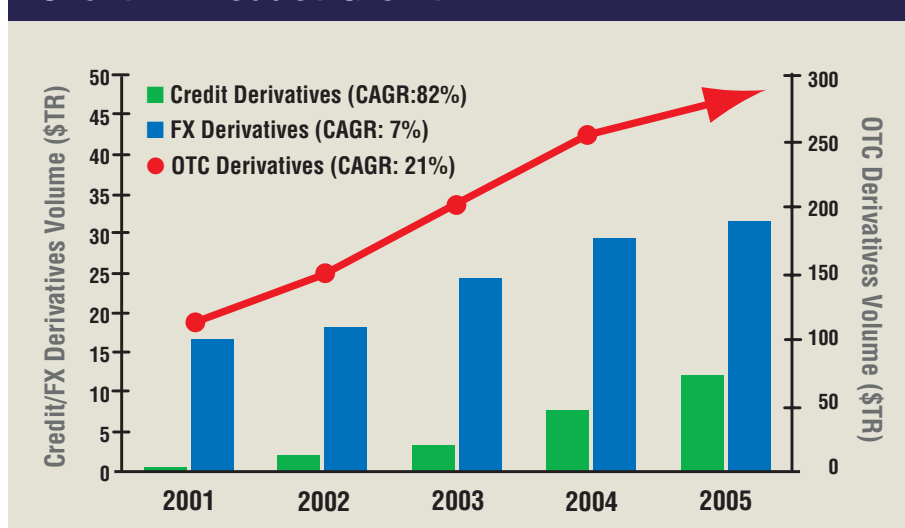
trend will continue - but interestingly, emerging market countries such as India and China will become sources for investment capital as their insurance companies and pension funds mature. New investment vehicles, products and distribution capabilities will be required for locally domiciled global products. Custodians will not only have to provide

clearance, settlement and safekeeping capabilities in many more markets than ever before, but will also have to supplement these services with on-the-ground support so that their clients can quickly and efficiently tap into these local and intra-regional flows.

Regulation

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Chart 1: Product Growth



Source: Bank for International Settlements, International Swaps and Derivatives Market Survey, 1987 - present

