Citi Enters Managed Account Outsourcing Business

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Citigroup is shouldering its way into the crowded managed account outsourcing space. By most accounts, the big bank's offering is backed by impressive in-house technology. But with no external customers to boast of, it still has to prove it can convert that technology into a scalable offering to outside managers, say industry participants.

New York-based Citigroup says it will start marketing a suite of "asset manager solutions designed to meet the middle- and back-office outsourcing requirements" of money managers early in 2005. "By providing a modular solution that automates services ranging from portfolio manufacturing process to sponsor connectivity, asset managers can choose from an array of services depending upon their operational needs," the company says in a press release. "Using this technology platform, Citigroup enables asset managers to deliver customization, tax efficient management and investment restrictions monitoring, while enabling asset growth, improving compliance, and lowering costs."

Citigroup's position as the leading manager and sponsor distributor of retail managed accounts will likely be perceived as an asset by prospects evaluating Citigroup's back-office outsourcing services, says Dan Seivert of Los Angeles-based merger-and-acquisition advisory and consulting firm 3C Financial Partners. But he adds that Citigroup is entering a hotly contested, three-year-old battle to capture the outsourced accounts of managed account managers and gain crucial market share in a space that is likely to see no more than four main players — from today's field of eight — emerge dominant. That, he says, has been the case with "almost all other financial service processing businesses."

Andrew Clipper, a director with Citigroup's Global Transaction Services group, says his unit - which runs a total of 660,000 accounts for in-house clients Smith Barney, Citigroup Private Bank and Private Client Investment Services - can process accounts at a rate of 25,000 per operations employee. Seivert says the paradigm that now prevails has investment managers processing their own managed account operations at a productivity rate of 500 to 1,500 accounts per operations professional. Though he cautions against making an apples to oranges comparison, Seivert adds that the new paradigm of managed account processing will likely afford a 10-fold improvement and allow operational professionals to oversee 5,000 to 15,000 accounts per operations employee.

But Stella Vanguestaine, head of marketing for the Bank of New York's SmartSource outsourcing unit, figures any new entrant is going to face tough competition from entrenched players. "Not everyone who jumps in will be there down the road," she says. "At the end of the day you're going to have fewer [vendors]." And those, she adds, are likely to be "those that came up with the idea for a product and a focused strategy to deliver it as well as 'referenceable' clients."

In addition to the Bank of New York, Citigroup will be butting heads with Mellon, PFPC and SEI - firms that recently announced contracts with managers Old Mutual, Neuberger Berman and Transamerica, respectively - as well as State Street, BISYS and JPMorgan Chase. Citigroup's Clipper says he isn't daunted at the prospect of competition, however. "We feel [the managed account industry] is growing at a very attractive rate," he says. Indeed, the Money Management Institute, a Washington, D.C.-based industry association, projects that that managed account assets under management - which passed the half-trillion-dollar mark late in 2003 - will surpass $2 trillion before the decade is out. As a result, says Clipper, "more sponsors and more managers are getting into the business." By Clipper's count there are about 200 managers in the retail managed account space, and, as only a handful of those have outsourced their back offices, he sees plenty of scope for his group's offering.

Vanguestaine sees some merit in that view. As more managers - established practitioners and neophytes alike - opt for outsourcing, so will there be room for more vendors. And that's a process she says is already underway, as managers look to lower per-account costs against a backdrop of declining fees and the possibility of more stringent performance reporting standards.

In any case, says Sandy Schwartz, a managing member of the McNamara Group, a New York-based asset management consultancy, Citigroup isn't likely to have set its sights on managed account outsourcing without a solid strategy to back its efforts. "People should take note of this," he says. "[Citigroup] is going into this because they see opportunities."

But to become an established, money-making player in the outsourcing game, Citigroup has to demonstrate that it can take its internally focused managed account processing prowess and tailor it to the back offices of external customers, according to a source who asked not to be named. The source adds that high productivity is only one of about 20 standards of excellence on the road to becoming a leading provider of outsourcing services.

And in terms of marketing, Citigroup will have to walk softly or risk alienating potential clients, says Schwartz. "When a money manager or a sponsor gets into the outsourcing business, the question is always whether prospective clients will view them as competition."

That's a hurdle Rorer Asset Management is said to have faced when it considered taking its own in-house operations system to the marketplace, according to another source. In the end, it decided to sell its outsourcing business to SEI - which quickly saw fit to ditch a tagline that ran something like "built by managers for managers."

But the sheer weight of any managed account offering from Citigroup makes its outsourcing business a formidable offering. "It's a steamroller," says a source. "But it's like you're on Fifth Avenue and its on Fifty-fifth Street; you can't see it yet, but you can feel the road rumbling and you can see some of the buildings start to shake."

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