

*BEYOND MiFID II...*

Frost Research  
Systems



An Emerging Global Standard for Research Transparency?



360 Degree View of Input CSA Eligibility:  
Are You Seeing the Whole Picture?

MIFID II



## BACKDROP

### **360 Degree View of Research Inputs (and their CSA-eligibility).**

- UK/EU regulators concluded that research via P&L left their asset managers at a global disadvantage and have changed regulation to make it easier for managers to charge clients for research.
- Many P&L managers are analyzing the possibility of returning to a client funded research model. This includes both client and ROI considerations.
- A narrow focus on fundamental research in isolation ignores the fact that a series of newer inputs that qualify as “research” have transformed both the manager investment process and the ROI of reverting to a client-funded model.
- This short deck outlines the wider “perimeter” of CSA-eligibility.
- In the UK/EU fund or strategy-level attribution of all “research” inputs will be required to make them CSA-eligible.
- Access to research inputs, free from the market risks inherent in the P&L funding model, has important implications for the medium-term competitiveness of asset management franchises - particularly as AI plays a greater role in the investment process.

## ACHIEVING A SUCCESSFUL RESEARCH FUNDING TRANSITION

### Establishing Priorities:

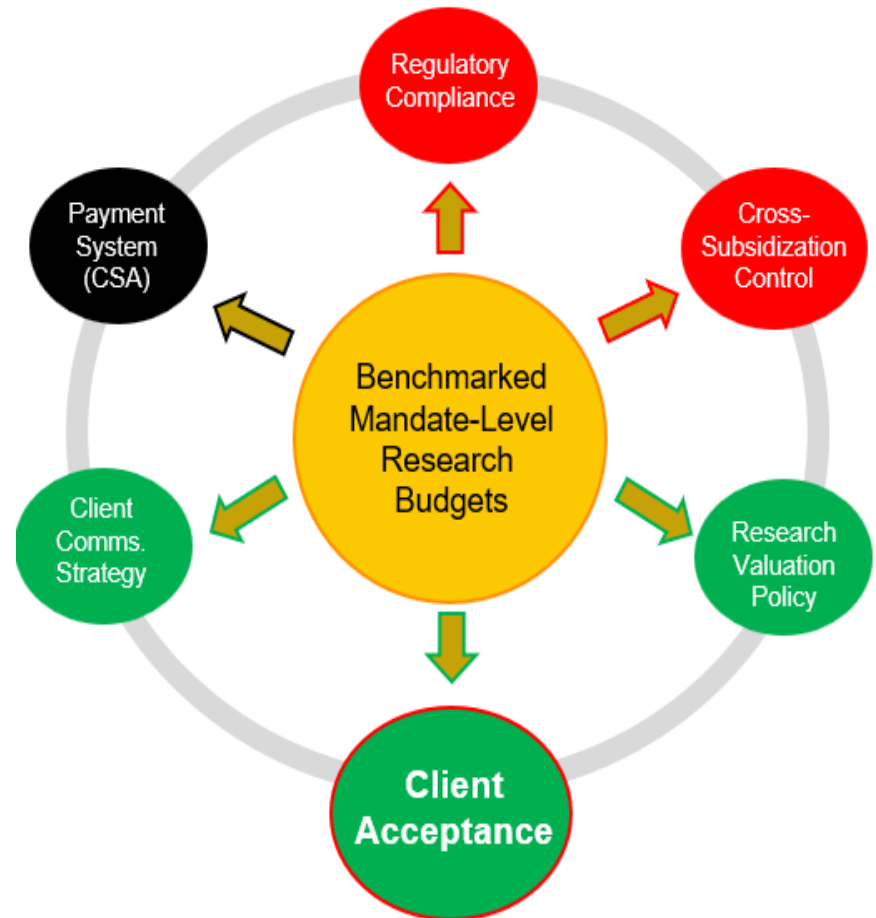
The success of manager research funding transition programs is defined by asset owner acceptance of manager research charges.

### What do asset owners care about?

- Mandate-Level Budgets
- Cross-Subsidization Control
- Strategy Benchmarking
- Fair allocation of research costs.

### Prioritizing Key Process Components:

- Benchmarked, Mandate-Level Research Budgets are the fulcrum around which the entire process revolves.
- Asset owners don't care which CSA payment system managers use.
- **But they do care that research payments are fair and transparent.**



## INVESTMENT DECISION INPUT AUDIT

CSA Eligibility:

Is your firm capturing the full value chain?

### Research

- Written Research
- Analyst Access
- Corporate Access/ Conferences (ex-UK)
- Independent Research
- Bespoke Research

### ESG Inputs

- ESG Research
- ESG Ratings
- ESG/Climate Data
- Portfolio ESG Analytics
- Proxy Advisors

### Research Services

- AI Tools
- Expert Networks
- Aggregation Tools (i.e. AlphaSense, Visible Alpha)
- Alternative Data (i.e. Yipit)

INVESTMENT DECISION INPUTS: 5-YEAR SPENDING TRENDS\*



\* Estimates: Frost Research Systems and Neudata

# STRATEGY/FUND-LEVEL ATTRIBUTION: ALL RESEARCH CATEGORIES

Regulation

MiFID II P&L

Post-MiFID II

Research Aggregation

Manager Level

Strategy Level

FrostRB Process

Research/ESG Payments

DOCUMENTS



ANALYST ACCESS



EXPERT NETWORKS



ESG



ALT. DATA



Research Inputs

Admin. Level

Reporting

Compliance

Strategy Budgets

Fund-Level Budgets

Cross-Sub. Solution

Strategy 1



Strategy 2



Strategy 3



Firm Level

Complete Cross-Subsidization Solution

## RESEARCH INPUT ALLOCATION MATRIX

New UK/EU client money research rules require a Research Valuation Policy that explains the manager's approach to fairly allocating research costs between clients and products.

### Research

- Written Research
- Analyst Access
- Corporate Access/ Conferences (ex-UK)
- Independent Research
- Bespoke Research

### ESG Inputs

- ESG Research
- ESG Ratings
- ESG/Climate Data
- Portfolio ESG Analytics
- Proxy Advisors

### Research Services

- AI Tools
- Expert Networks
- Aggregation Tools (i.e. AlphaSense, Visible Alpha)
- Alternative Data (i.e. Yipit)

### Asset Class

Equities

Fixed Income

Multi-Asset

Private Assets

Active Funds

Passive Funds

Active ETFs

Separate Accounts

Traditional MiFID II research valuation processes are designed for fundamental research applied to active equity strategies – *only*. Rapidly evolving investment processes require new approaches.

New CSA structures now enable all products/asset classes to pay for their fair share of research inputs.

# FROST RESEARCH INPUT ALLOCATION MODELS: ACADEMIC FOUNDATIONS

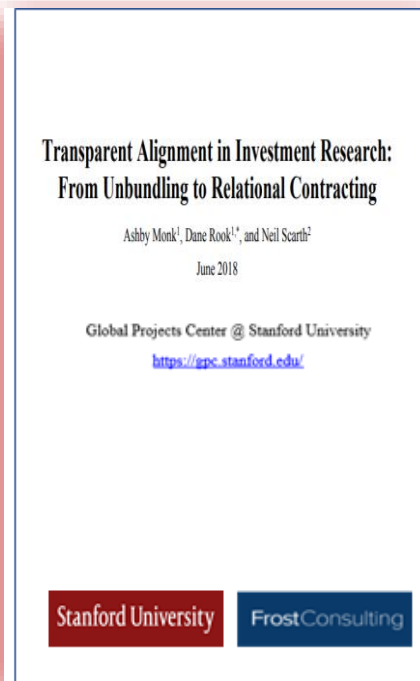
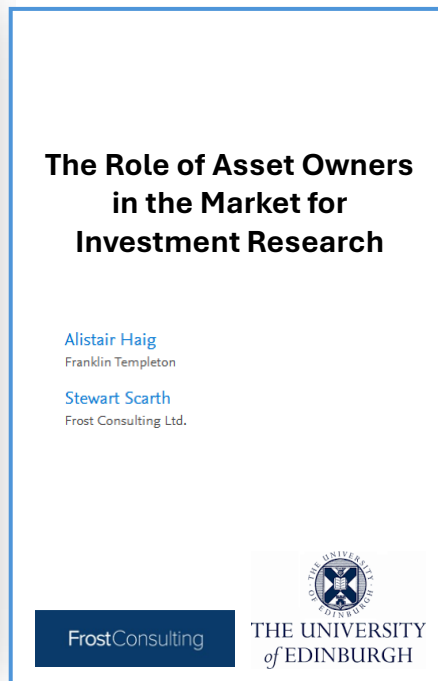
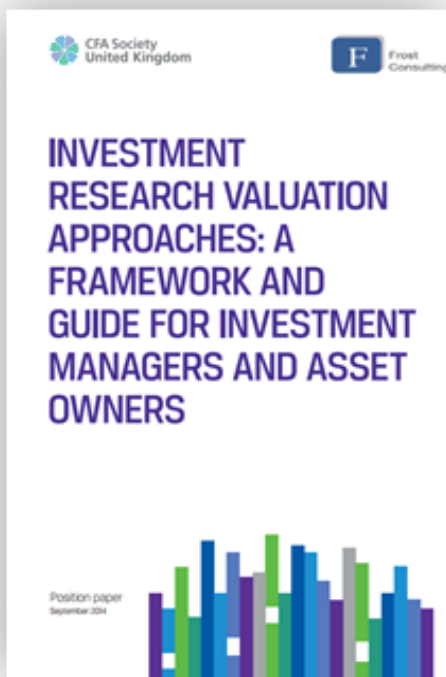
Frost can engage with asset owner clients to explain the foundations of the Quant Models & Benchmarks.

Seminal work on  
Research Valuation  
for CFA Institute - 2014

Asset Owner/Asset  
Manager Research  
Dynamic – April 2016

Analysis of MiFID II  
Impact on Asset Owners –  
with Stanford - June 2018

Other  
Collaborators



**Institutional Investor**

**Bloomberg**

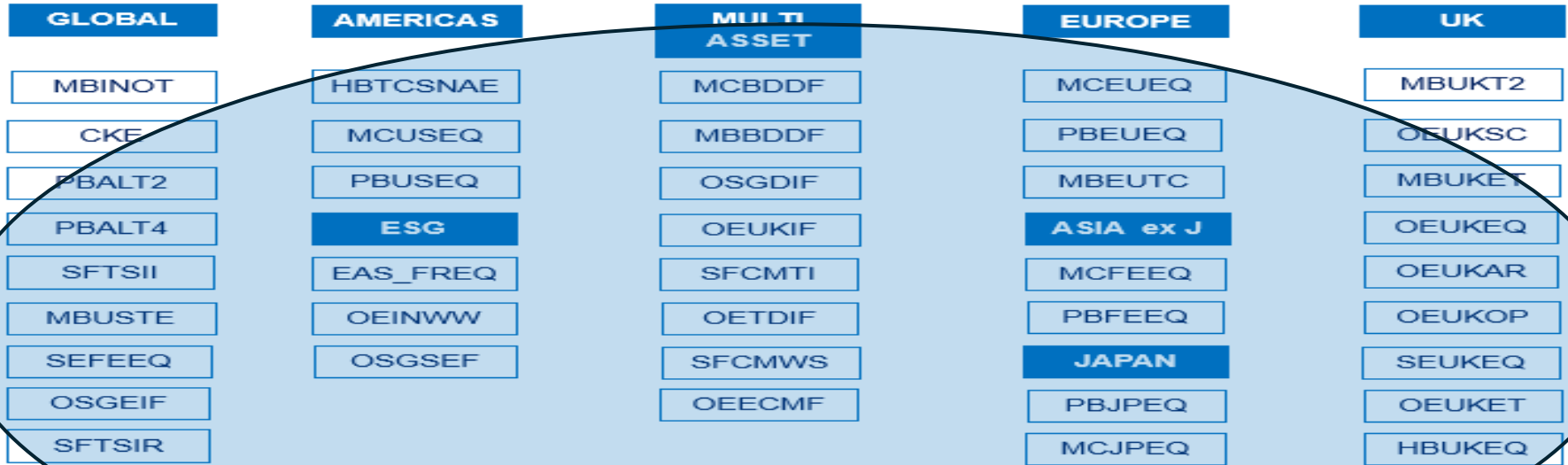
**Council of Institutional Investors®**

**EVERCORE ISI**

**UK Capital Markets Industry Taskforce**

Quant-driven research input allocation based on client/fund investment process and targeted outcomes.

# TARGET OPERATING MODEL: UNCONSTRAINED INFORMATION



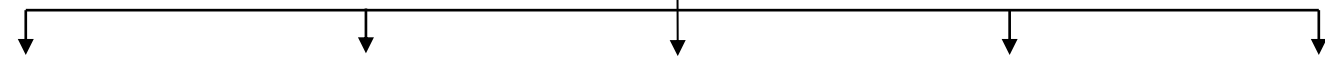
**ACME**

Asset Management

How can ACME AM share research between products....

...and fairly allocate research/ESG/Data costs between products....

FrostRB



UK

Multi-Asset

ESG

USA

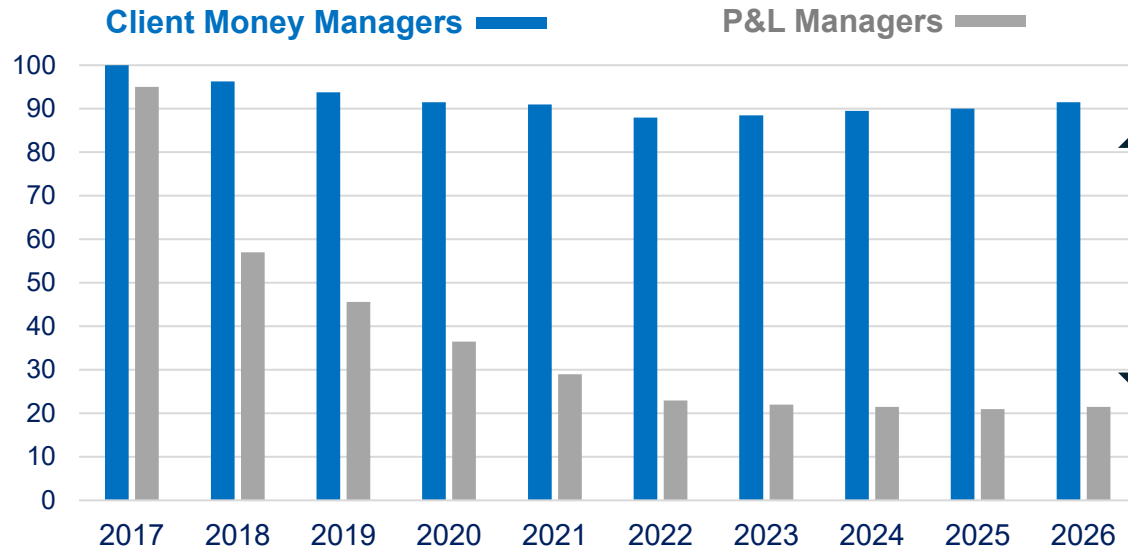
Global

# TRANS-ATLANTIC INFORMATION/DATA GAP: AI IMPACT

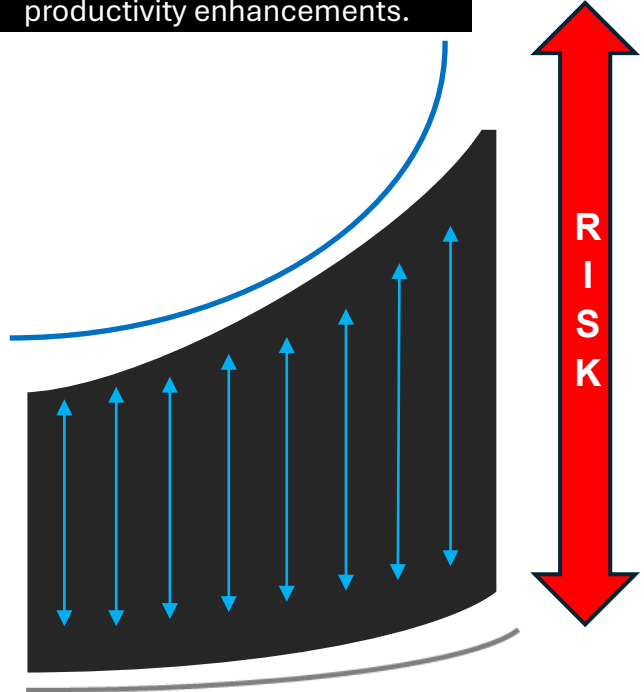


Existing AI applications for manager investment processes are already yielding startling productivity enhancements.

Research Spending: Indexed at 100 in 2017 (Pre-MiFID II)\*



RISK



AI Era

MiFID II Era

\* Frost Consulting Estimates

## APPENDIX: RESEARCH DEFINITIONS

SECURITIES AND EXCHANGE COMMISSION 17 CFR

Part 241

[Release No. 34-54165; File No. S7-13-06]

### Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934

A. Framework for Analyzing the Scope of the “Brokerage and Research Services” under Section 28(e)

For purposes of the safe harbor, a person provides . . . research services insofar as he –

(A) furnishes advice, either directly or through publications or writings, as to the value of securities, the advisability of investing in, purchasing, or selling securities, and the availability of securities or purchasers or sellers of securities;

(B) furnishes analyses and reports concerning issuers, industries, securities, economic factors and trends, portfolio strategy, and the performance of accounts;<sup>89</sup>

Corporate governance research (including corporate governance

analytics) and corporate governance rating services could be eligible if they reflect the expression of reasoning or

knowledge relating to the subject matter of the statute (for example, if they provide reports and analyses about

issuers, which can have a bearing on the companies’ performance outlook).<sup>94</sup>

## APPENDIX: RESEARCH DEFINITIONS



(1) concerning one or several *financial instruments* or other assets; or

(2) concerning the issuers or potential issuers of *financial instruments*; or

(3) closely related to a specific industry or market such that it informs views on *financial instruments*, assets or issuers within that sector,

and which explicitly or implicitly recommends or suggests an investment strategy and provides a substantiated opinion as to the present or future value or price of such instruments or assets, or otherwise contains analysis and original insights and reaches conclusions based on new or existing information that could be used to inform an investment strategy or be capable of adding value to a *firm's* decisions on behalf of *clients*.



### Core Definition

Research constitutes material or services concerning:

- One or several financial instruments or other assets, or issuers/potential issuers; **and**
- New or existing information that explicitly or implicitly suggests an investment strategy, adding value to client investment decisions. icmagroup

**Legal Disclaimer Notice**

This document has been produced by Frost Research Systems LLC. Everything in this document is provided "AS IS: and without warranty of any kind. We have made every effort to offer current, correct and clearly expressed information as possible. Inadvertent errors can occur and changes will be made when any error is brought to our attention. By providing this document, Frost Research Systems LLC shall not be held liable, or undertake any responsibility whatsoever, for the content of third-party information. All content and material on this site is exclusivity property Frost Research Systems LLC and may not be republished without expressed written permission.