HEIDRICK & STRUGGLES

GLOBAL MARKETS PRACTICE

What global markets clients want: A view from US buy-side institutions

To remain competitive and capture buy-side investments, sell-side brokers need to provide tailored offerings and a differentiated experience.

When it comes to services provided by the sell-side brokerage community, buy-side investors have departed from the old "one-stop-shop" mentality and now crave a differentiated and unique experience, according to interviews with more than 30 buy-side executives conducted by Heidrick & Struggles. In this cost-conscious environment in which the sell side finds it increasingly difficult to provide a broad range of top-notch services to all customers, buy-side clients advise that brokers should focus on high-grading their service offerings.

Through our interviews, we identified four areas that seem to move the needle for these investors: tailored expertise, flawless execution, a new relationship model, and inventive technological tools. How can sell-side firms differentiate themselves in these areas and move their organizations ahead of competitors, both newly emerging and well established, in a systematic and sustainable way? In our experience, there are four levers that are most crucial for firms to build momentum and meet client requirements more quickly than competitors: mobilizing, executing, and transforming with agility, or what we call META (see figure).[1]

These four levers will help brokers accelerate improvement in all four key areas identified through our interviews.

Tailored expertise

Buy-side investors today believe that the equity research they receive has been substantially diluted, with analysts reiterating the same high-level facts and data points without providing differentiated insights or deep dives. According to our interviewees, this is due, in part, to increased burdens placed on analysts to cover more companies, as well as the dilution of overall analyst talent as firms have generally failed to replace departed research analysts with individuals of comparable experience or capabilities.

This dynamic has created a good opportunity for a variety of specialized boutique firms to gain market share, especially when it comes to providing insightful research on sectors that are underrepresented at larger firms. Boutiques such as Cleveland Research, Consumer Edge, Evercore ISI, and Wolfe Research, among others, have flourished in this environment. Certain investors

Figure

M + E + T + A = Acceleration

Mobilize	inspiring aligned action based on a compelling ambition and purpose and a simple set of strategic priorities
Execute	fully harnessing and streamlining resources to consistently deliver excellence in the core business
Transform	experimenting and innovating to create growth engines and reinvent existing businesses ahead of the market
Agility	spotting opportunities and threats, adapting and pivoting faster than competitors to create competitive advantage

[1] These ideas are explained most fully in *Accelerating Performance: How Organizations Can Mobilize, Execute, and Transform with Agility*, by Colin Price and Sharon Toye (Wiley and Sons, January 2017). For more information on the META framework and the research behind it, see "Putting META into action," on heidrick.com.

we spoke with commended these firms for having a unique, significant, and sustainable edge defined solely by the quality and insight of their research product. Based on their satisfaction with the work of such firms, these investors commented that it may be more impactful and profitable for the sell side to focus on a more limited number of products or sectors rather than trying to cover everything.

According to the buy side, focus alone isn't enough, however. Most investment managers have identified a shift in equity research quality over the past decade, saying that "while equity research was approached very scholastically by the sell side before the financial crisis, since the crisis, research has been cut to smithereens, and it's because of expenses." Other buy-side managers we talked with remarked: "I've seen a significant trend of senior value-adding, battle-tested analysts being replaced by younger ones, probably a former associate." In many cases, the less experienced talent is tasked with a wider mandate, significantly affecting the quality of the research they are able to produce.

So where are those battle-tested analysts going? They are going either to the buy side itself or to boutique firms that want to leverage their expertise to provide more in-depth perspectives over a smaller coverage universe.

These overall trends have made commission budgeting increasingly difficult. Buy-side clients need to ensure that they allocate sufficient capital to boutiques to get the research and sales quality they want. This focused strategy also better allows these specialty brokers to reinvest commissions from clients directly into the specific businesses that generated the commissions in the first place. On the other hand, the buy side continues to see the substantial value proposition of larger banks with respect to trade execution and capital market allocations (rather than research). As one manager explained: "I don't need the Street for market color. I need it to give me new issue allocations and move large blocks of paper when I need liquidity. On the other hand, with respect to the smaller guys, I need color, I need insight, I need ideas."

In summary, in a world with limited resources, buy-side institutions are suggesting that brokers, boutiques, and bulge bracket firms mobilize their operations by 1) shaping their strategy to prioritize areas that, based on their platform and vision of the market, create distinctive value for their clients by delivering tailored expertise and 2) engaging and energizing the firm by investing heavily in and retaining top talent that makes a difference.

Flawless execution

In addition to tailored expertise, buy-side institutions view trade execution capabilities as an additional form of differentiation among sell-side firms. Trading spreads have narrowed drastically as a result of the increase in electronic- and algorithm-driven trading, and best price has become a given when determining who gets the trade. As a result, pricing has, in many cases, supplanted traditional relationships as both the buy side and sell side have become more cost sensitive and regulated. A portfolio manager commented that, today, "Better dealers are separated by tighter markets, trading and showing axes."

It is clear in this competitive environment that sell-side firms can stand out from the pack by continually monitoring and improving their execution. In our interviews, buy-side executives regularly stated that they value transparency, speed, and accuracy, with little room for error.

Although pricing and expertise trump the old-school relationship model, relationships still matter—especially for moments when mistakes are made. As more sell-side analysts move to the buy side, the executives we spoke with generally agreed that the analysts understand the position of the other side, how they think, how to deal with them, and whether they are being honest. Having a transparent, trust-based relationship helps guide both parties to a reasonable solution in an otherwise tense situation. And, as with expertise, hiring people with experience is a key to success in execution and relationship building.

A new relationship model

In that context, successful sell-side companies are transforming their relationship-building model to one based on offering distinctive, tailored, and holistic advice to clients. In the past, relationship building centered around dinners or sporting events. Today, it is becoming increasingly difficult for clients facing commission allocation constraints to identify a specific return on investment for every interaction they have with the sell-side. As a result, they are accepting fewer meetings and outside entertainment to avoid being held accountable for such so-called investments. "It has become more difficult for buy-side clients to justify using anything but a top-notch research sales business because they are more conscious of consuming the marginal resource," one executive noted.

According to investors, meaningful relationships are now built on foundations of creating opportunities that allow for sharing knowledge. When sell-side firms offer events today, for example, clients weigh whether to attend based on learning potential. They place higher value on a meeting of minds among senior investors, executives, and industry leaders that expand or poke holes in their investment theses or offer perspectives on emerging trends. As one product manager explained: "When you decide to buy something, understanding why someone else is selling it is just as important as knowing why you want to buy it." This consideration extends to conference attendance as well, where the buy side prioritizes events that generate useful dialogue and help draw reason out of the noise. Goldman Sachs, J.P. Morgan, and Morgan Stanley, in particular, were praised by investors we spoke with for having the types of events that allow investors the opportunity to share perspectives with CEOs and fellow investors alike and add to their overall knowledge base.

Many sell-side executives we talked with mentioned that this new successful relationship model is also based on a culture of internal collaboration. Most praise firms that have a strong culture of information sharing because it positions the account managers to best serve them by delivering a cohesive strategy. On the contrary, investors expressed frustration when it comes to firms that are very siloed. One said, for example, that "while I understand that at some firms there is not a culture of collaboration, because of competing incentives, I would pay more money for a cohesive tailored strategy."

Culture transformation starts at the top. Leaders at sell-side companies are better able to foster business success when they promote a culture of collaboration. This may entail breaking down traditional silos or ending the industry habit of supporting small, closed teams that go from company to company as a unit. It may also mean changing financial incentives to promote collaboration. And it will certainly include acting as role models and champions of change.

Inventive technology tools

Another element of the new relationship model is technology, which amplifies and simplifies how the buy side can find and use research and helps sustain relationships over time. Buy-side clients want products with sleek websites and mobile apps that are easily accessible. Each investment manager has the opportunity to choose from a handful of good analysts in every sector. If one offers faster, more digestible information, then the lion's share of clients will gravitate to that company. A portfolio manager explained: "If somebody has a broad enough menu of products that manages to get their website bookmarked on my computer, then that's one

> *Successful sell-side companies are transforming their model for building relationships—offering distinctive, tailored, and holistic advice.*

The consensus from the buy side is clear: if you can't be everything to everybody, then don't try.

more way to get me to consume [their] research over somebody that is just as good at research but hasn't earned a place in my shortcut path. It's smart, but not everybody has done it."

Technology can bolster perceived expertise as well as relationships. The research team at UBS was cited by one executive we spoke with for creating a culture of value-added research through its use of technology. UBS publishes insightful reports on big topics in the marketplace by leveraging its Evidence Lab, which conducts data-intensive projects to validate or disprove investment theses. For example, the team has used technology to analyze large data sets and evaluate the distance of various companies' assets from one another in order to come to a point of view on antitrust-law overlap analysis. In this case, there were thousands of assets to evaluate, so the question lent itself to a systematic data-intensive project—and publishing the findings to its clients helped UBS differentiate itself. Another example of how sell-side firms can use technology to differentiate their expertise and foster relationships is Morgan Stanley's AlphaWise, which employs surveys in addition to quantitative or analytical processes.

Adopting new technologies and continuously learning keep brokers agile to meet client needs in this changing market environment.

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The consensus from the buy side is clear: if you can't afford to be everything to everybody, then don't try. Satisfying these current demands extends beyond finding the right people, whether those people are experienced analysts, strong execution executives, or digital-product designers. In addition, talent must be managed and led in new ways to ensure the robust, holistic, simple connectivity that buy-side companies want today.

That said, the executives we interviewed agree that some large firms are doing well. But even they, as well as the boutiques mentioned, are shifting to a strategy driven by META: *mobilizing* more tailored expertise, *executing* flawlessly, *transforming* the relationship model, and improving *agility* through more inventive use of technological tools—all in the context of more collaborative cultures that require evolving talent management. ■

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Global Markets Practice

Heidrick & Struggles' Global Markets Practice provides buy- and sell-side clients with unsurpassed leadership and counsel related to talent acquisition and organizational design.

Our differentiated approach to the market leverages our asset management, hedge fund, fintech, and corporate practices to gain access to the senior-most individuals at buy-side and corporate companies, providing unparalleled market insight and intelligence on the best talent and organizational structures for global markets clients.

This team-based, collaborative approach has been particularly valuable during the past several years as top talent has crossed back and forth as a result of market disruption. Our unique international team and culture give us a competitive advantage that translates into unparalleled market insight and intelligence that produce results for our clients.

We create talent strategies that not only mitigate risk but also make an impact on an organization's long-term competitiveness by leveraging buy-side perspectives with our sell-side expertise. We determine who holds the real relationships and possesses the desired expertise by tapping into our network of institutional investors, sponsors, and corporate partners to create a tailored list of talent to meet our clients' needs.

Leaders of Heidrick & Struggles' Global Markets Practice

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