Persistent PODCAST

Persistent Podcast | Episode 05

Regulatory Compliance and Risk Management within the BFSI Sector | Andreas Blatt and Steve Hook

Barath Narayanan: Hello and welcome to another episode of the Persistent Podcast series. This series explores various topics around transformation and innovation in the future. I'm here today, taking over from my friend Gurvinder Sahni as the host. I have two industry veterans from the financial services industry with me for today's episode.

Before that, let me briefly talk about my role at Persistent. I'm Barath Narayanan, responsible for the banking, financial services, and insurance business unit and the Europe region at Persistent. As part of my discussions with customers over the last six months, I am seeing an enhanced focus on regulatory compliance and risk management.

Most customers are focused on improving revenue streams, operational efficiency, customer experience, and consistent use of new technology advancements. But one consistent factor that came across for almost 100-plus clients that I've met in the last six months is the focus on regulatory compliance and risk management.

With that, we have two industry veterans joining us today, and I'm very proud to have them in this series to share their points of view. Let me start by introducing my first guest, Andreas Blatt, whom I have known for more than ten years. He's been a CIO board member and has played various leadership roles across investment banking, wealth management, front-office sales, front-office trading and sales, and technology. Of course, a significant part of his leadership has been managing risk and compliance in the financial management space. With his background, he can add tremendous value to this conversation today.

I'm so proud to have him as part of this podcast series. Welcome, Andreas.

Andreas Blatt: Thank you very much. It's a pleasure being here. I'm very much looking forward to our conversation today.

Barath Narayanan: Thank you, Andreas. That takes me to my next guest, and you will understand why I am so excited to host the series. Let me introduce Steve Hook, whom I also know from my past work in the industry and from managing some of my customers.

Steve has 25+ years of experience in the global market. He has been a CIO and responsible for managing a large portfolio of applications in the front office, driving strategic vision for technology organizations. He has a unique blend of driving technology innovation and solving business problems, managing and delivering complex problems for business counterparts.

And he’s going to be adding tremendous value to this episode. Steve, welcome.

Steve Hook: Thank you, Barath. I am excited to be here.

Barath Narayanan: Thank you so much, Steve and Andreas. Coming back to the topic, We have seen Andreas and Steve, which are not new, right?

The regulatory compliance and risk space are not new. We have seen this continuously evolve over the last 15 years, and most banks have spent billions of funds addressing this. What is something new that has happened in the last three to five years that we are seeing?

Again, enhanced emphasis on regulatory requirements. Compliance and risk management space. I request both of you to chime in, starting with Andreas, with you first.

Andreas Blatt: Sure. It’s a very good question, Barath. And as you say, right, particularly after 2008, we have seen a significant change in the regulatory response after everything that happened in 2008.

In those days, the regulations primarily addressed financial stability, capital and liquidity, and risk management in general. Financial institutions globally had a lot to work on. As you said, billions have been invested in streamlining processes, improving data quality, implementing controls, and so on.

Transparency was key. A lot has been done over the last 10 years — from 2010 to 2020 — but this doesn’t stop there, right? So, if somebody is thinking that this is it, and now everything is clear, and it won’t evolve further, that’s definitely not the case. Over the last five years, we have seen that the regulatory focus has expanded to encompass broader issues, such as technological innovation.

And we’ll talk about those, especially around data, privacy, operational, resilience, and sustainability. This requires the bank to continuously adapt to new regulations, invest in new technologies, and maintain a proactive approach to new regulations, risks, and regulatory changes. And to give you a few examples of things that have evolved over the last three to five years. we have all seen the increased frequency and sophistication of cyberattacks, not just in the financial industry but across industries. They might be politically or criminally motivated from a financial perspective, but they exist and are becoming ever more sophisticated.

That makes regulators concerned about how banks protect themselves against it (cyberattacks) also from a client’s perspective. And operational resilience is now a key topic for many regulators, and the Bank of England published a new supervisory statement just a few years ago on this.

Operational resilience was also driven by what we all have experienced out of COVID, right? Crisis management: how can we be better prepared for disruptions and ensure continuous operations of the banking processes? And I was talking about new technologies, right? Over the last few years, crypto assets have evolved significantly across the world, and while it’s great to have new technical innovation, at the same time, it also comes with a threat. (We need to understand) Is there transparency around? What’s the risk for the end client, right? Is there some market abuse that needs to be prevented?

So also here, new regulations surfaced one and a half years ago under MECA that now will get into action set up by the individual banks.

Credit risk is an old topic, but it also evolves further. There is more sophistication in how credits are given, driven by rising interest, rising inflation, and sociopolitical uncertainty that is out there to ensure that loan takers are treated fairly, but at the same time are truly able to also pay those loans right? Loan underwritings and stress testing frameworks will evolve even further. These are just a few that I wanted to mention, but I'm sure my dear colleague Steve has a few more on his mind.

Steve Hook: Yeah, I agree with Andreas. I mean, it's a continuous process. It's not just about the banks. It's about the external environment that the banks are operating in, which continues to change with innovations and with new events like the pandemic, as Andreas mentioned. With some recent issues that have occurred with a few banks, liquidity management is a big topic of focus, and how the treasury functions in banks operate the challenges they may have, particularly in the data management space, is a theme that we're seeing. There are still issues out there in the AML space as well due to some recent events where banks have been fined for challenges in their AML compliance processes, et cetera.

Climate risk is a newer topic that has received considerable attention from both a regulatory perspective and how firms report and manage their climate-related risks. Of course, there's also an investor angle to it in terms of providing ESG investment vehicles and managing them.

Of course, the topic du jour is AI and machine learning. Everybody in the industry is experimenting with and talking about it, so regulators, of course, are also trying to understand the inherent risks of AI and the models that fuel it, which brings us to the data that the AI models consume.

This also introduces other risks because quite a few of these models really can't be executed, and the learning process can't occur on-prem or within a firm's own data centers. So, that introduces the risks of moving data out to third-party cloud providers as well. A lot of banks are paying attention to model risk management around AI at the moment. I'm quite sure there will be some challenges in this space over the next few years as well.

Barath Narayanan: Thank you, Steve.

Andreas Blatt: If I may add a few more, based on my general observation over the last years, I have perceived that the expectations of the regulators are significantly increasing.

Steve Hook: Yeah.

Andreas Blatt: It's different from what it was in the past. Earlier we only needed to do what was written in the letter. Today, it's more about the spirit of the letter, with an ever-increasing need to surpass the ever-rising bar that goes to the next level. This also comes with less patience on the regulatory side. We see more enforcements, more fines for misbehaviors, and more failures of compliance. So, it's no longer a 'nice to have'; it's absolutely a focus item for all banks— if they want to be in the game for the future, (they need) to understand compliance, take it very seriously, embrace it, and continuously improve their processes.

We'll probably talk about data in a second as well, especially the data management practices. This will not end; it will become more challenging as we progress.

Barath Narayanan: Wonderful, Andreas. I absolutely concur with both Steve and you on what you just said. I was going to come into the technology discussion, but before that, Andreas, what you brought out is very important: seeing this function. Both of you played this role, right? This function is vital in balancing 'doing the business' and 'protecting the business'. For leaders responsible for regulatory risk compliance, the critical factor is protecting the bank from exposure and not allowing something wrong to happen.

But how do you balance this is a question, number one. Number two, what are the common themes you see? Adopting and implementing changes to make the function very nimble and agile and respond while protecting the bank. Right, Steve, you have been the CIO on the investment banking side. How do you see this?

Steve Hook: Yeah, just to add one thing to your point about protecting the bank. There's also an element of protecting all your stakeholders, including clients and the market. For example, as a market maker, you are responsible for protecting even your shareholders and employees. So it's about more than just protecting the bank. One of the common themes to your question, in my opinion, is around data because in banks, data underlies pretty much every process. One of the challenges many financial services firms have is just the inherent complexity (of data) having grown over decades, even hundreds of years, et cetera. They have global, very complicated ecosystems. Data is a fundamental asset for each financial institution, and it underlies all regulatory reporting, monitoring, processes, and controls.

If we look at cyber security, for example, effectively, you're trying to protect the crown jewels, which are the data assets. So, effective data management is critical to preventing and protecting against breaches, whether customer or bank data, securing sensitive information, classifying data properly, with real-time threat detection, etc.

Operational resilience is also critical regarding backing up data, recovering it, dealing with disruptions, etc. These processes and controls rely on the underlying data for some functions like credit risk management, consumer protection, and AML. Again, its accuracy is one of the challenges many firms have. Due to the diversity of businesses, the data then makes its way into the corporate credit risk management functions, for example. Organizations have many challenges in maintaining the lineage and quality of that data, front to back.

Most financial institutions' risk frameworks rely on data quality at its fundamental level. This is also true for newer areas, such as climate risk. As I've already mentioned, in the AI and ML space, data is the fuel for algorithms. So, the quality of the data and the biases therein are critical topics that financial institutions need to pay attention to and be aware of.

Barath Narayanan: Got it. Thank you, Steve, for bringing in an important element about data. Now, Andreas, Steve has called out the whole importance of data as a common theme. How do you see the evolution of artificial intelligence impacting or bringing in an element of change in the way regulatory requirements can be addressed via AI against the common theme of data? How do you see this evolution?

Andreas Blatt: First of all, you know me, but I've always been speaking about data this way, and I'm very pleased to hear that Steve shares this view as well. I think data is probably the biggest asset that financial institutions have, and I am not blaming anyone; it has historically grown through mergers and acquisitions.

It was tough to get data aligned in a front-to-back data model. What we see across most financial institutions is that data gets sourced, and multiple amendments, overrides, and adjustments happen in silos. No wonder it isn't easy to get that data together again in corporate systems.

It's perceived as an overhead of how data can be treated rather than a business goal. You call it (data) the fuel; it's our water—the thing that lets us live. To generate benefits from it, we have to set things straight, right? And once we establish a data management (mechanism), we can have clear water to run through the pipes. This is where AI plays a very important role.

To answer your question, AI absolutely can help. But again, one of the preconditions is that the data needs to be clean, complete, unbiased, and ethically correct. So, there are attributes that need to come with it, but one should not assume that one needs first to clean the entire bank or that the entire (data) framework needs to be in place.

Does data need to be clean across the entire bank before you can start AI? No. You can use individual areas or use cases where you get the front, the groundwork, and the framework established, and then you can use AI.

How can bank AI be used in a space like risk, regulation, and compliance? Well, banks can enhance, for example, their efficiency, reduce costs, improve the accuracy of their work, and ensure faster compliance with the ever-evolving regulatory requirements that we were talking about earlier. I'll give you a complete, concrete example: The compliance process could be automated using AI. You can streamline document management or screen how new policies evolve worldwide. Then, understand the differences in that policy versus your existing policy implementation, understand the delta and assess it, and then spin off change programs. So, the entire regulatory change management can significantly benefit from AI and NLP.

Anti-money laundering is a typical case where AI can help. The same is true for counterterrorism financing. You're dealing with huge amounts of data: millions and millions of transactions flowing through the pipes. By using that data to analyze complex patterns and anomalies that might exist in financial transactions, you can better indicate money laundering activities.

I already talked about operational efficiency. Repetitive tasks that can be automated, but (AI can also help with) monitoring of conduct risk internally. You can scan the various communication channels within a firm, be it chats, calls, or emails, and see whether there is any potential ethical misconduct, right? AI can also help manage the organization that way.

Another typical use case that is very easy to do is cross-border compliance. For example, you have (operations in) multiple regions, (across) multiple jurisdictions, and different policies apply. At times, relationship managers (may) need help understanding the latest rule. AI can provide a relationship manager, an agent with the (right) information related to his particular client and, on the spot, increase client satisfaction because the client doesn't have to wait. It's almost instant. Secondly, (AI) ensures that you proactively adhere to the latest compliance rules in that region for that use case.

So, in short, there are many opportunities for AI to help improve compliance adherence, efficiency, and cost reductions.

Barath Narayanan: Thanks, Andreas. That's very useful. Given that context, Steve, you are responsible for technology and digital services offerings as a senior partner at the reference point. You have also been exposed to Persistent Systems over the last two or three months. Andreas, you, as an advisor, have spent significant time understanding Persistent over the last six months. How do you see reference point and Persistent coming together to solve some of these challenges for the customers?

Steve Hook: One thing that is important in this world today is being able to bring multiple disciplines and skills together in effective and highly productive teams. I don't believe in a world where you can offer a capability in a single skill and domain. That's not particularly effective for financial institutions, so a combination of skills is critical. On the reference point side, we have risk and compliance domain experts — folks who have operated in the first and second lines of defense of financial institutions and regulators as well. Persistent has a robust technical engineering team with data engineering skills. Both of these are required to solve many of the problems that we've talked about in financial services firms, particularly understanding the regulations or how financial institutions operate, engineering the right solutions, and delivering them effectively at the right cost.

It's also about building highly effective teams. In terms of types of activity that we get involved in, we've worked with a broad range of financial service institutions across both financial and non-financial risk, helping them conduct assessments, for example, in the enterprise and operational risk spaces, risk governance and the cyber security space, AML, KYC - we've talked a lot about that. We have also done much work in risk analytics and)reporting. As a joint team, we can help firms understand what's required and engineer the right solutions, particularly when huge amounts of data are needed to provide effective risk reporting and analytics.

We also offer an independent point of view, which brings value through practitioners who've seen what happens at other firms to bear on a particular firm's challenge. We can often get a third-party point of view experience from different organizations, which can be valuable, mainly when dealing with MRAs or consent orders.

To be a little bit closer to the IT space, both Andreas and I have done a lot of work facing off against regulators and helping firms' IT functions consolidate U.S. Operations, particularly foreign banks that have those unconsolidated.

Barath Narayanan: Thank you, Steve, for your thoughts.

Andreas Blatt: I totally agree with Steve. I think the time when one came to the party and was good enough to manage this complex environment is definitely over. It's about pairing the best-in-class teams together to create a winning team. From what I've seen at the reference point, as an advisor to Persistent, I have had the opportunity to see what Persistent is doing for their clients. I think it is well-known that their strengths are product engineering and everything related to data - data) platforms, analytics, AI, and cloud migration. A very strong focus on these gives them much depth. And as Steve said, that combination of reference point and Persistent is a winning combination.

What I've seen Persistent do for various clients in the data space requires a lot of in-depth knowledge to understand the complexity around data governance, ownership, and accountability, right? Persistent can help firms operationalize their data management practices into true front-to-back quality management with clear ownership. Many companies forget about ownership and accountability, how data quality is managed, and the very important data lineage.

(The key is) to understand front-to-back how data flows from a loan capture system down to the balance sheet. Understanding the individual data attributes and how they flow through (different systems), where they get amended, whether right or wrong, requires deep insights into the business function and the technologies being used. As you can imagine, in a 50-year-old financial institution, gleaning deep insights will require data)integration, API technologies, and analytics.

Banks also need help uncovering data gaps. For example, they might exist and impact your decision-making or reporting. Employee training and awareness around using data and making data-driven decisions are also necessary, right? I've seen Persistent, in various instances with their clients, having that deep insight to educate their clients on the front-to-back data-related processes.

As said before, most issues that need to be remediated in regulatory compliance are data-related. A strong partner is highly recommended, and there is no time to fiddle around.

Barath Narayanan: Thank you, Andreas. That's wonderful to hear from both you and Steve. Thank you so much for joining this podcast. I enjoyed this conversation and, as always, connecting with you both. Before we wrap up, I would love to hear from both of you about the key takeaways from the discussion. Steve, could you start off with Andreas closing it?

Steve Hook: Yeah, I mean, for me, the first takeaway is that things continually change, and it's not a static environment. The external world is changing. Events happen, both fortunately and unfortunately. The financial markets are complex, and it's a huge opportunity for financial service firms. However, they must also bear in mind all their stakeholders as they continually evolve and continue to focus on regulatory compliance, the underlying controls, and the underlying data assets that effectively enable banks to run. So, those are fundamental aspects we've discussed today. But I'm optimistic, too, because plenty of exciting challenges are out there. With changes in the AI / ML space, there's a huge opportunity for financial service firms, customers, shareholders, regulators, and ourselves.

Andreas Blatt: As Steve said, it's an ever-changing environment. And I hope that financial institutions will realize that while it requires a lot of focus and investment and sometimes gets perceived as a burden, it's time to change our perspective. Is there a positive spin to all of it? There is! We're cleaning up our house, making it more efficient front to back. We have better insights and better transparency to run processes faster. So, if we already invest the money, the people, and our focus on it, we will begin to reap the benefits. It could be intraday processes - imagine a world where you can do pre-deal checks that allow you to see the impact of a new client or a new trade, not only to the front-office positions but down to the risk calculations, the RWA, your balance sheet, liquidity. All because your processes are streamlined, the data is clean and you can rely on it. You can do monthly closes every day; you don't have to clean up data at the end of every month. Wouldn't that be fantastic? And it's achievable if we turn this around from a burden to an opportunity and partner with the right people who show us how to get there.

Barath Narayanan: Awesome. Thank you, Andreas. I sincerely thank you both for joining this podcast to share your insights and thoughts. You know how much I respect you both for the value and insights you bring. And thanks to everyone for being part of this podcast.

Stay tuned for more on innovation and continuous changes in the business and technology landscape. Thanks!

Re(AI)magining™ the World

About Persistent

Persistent Systems (BSE & NSE: PERSISTENT) is a global services and solutions company delivering Digital Engineering and Enterprise Modernization to businesses across industries. With over 23,200 employees located in 19 countries, the Company is committed to innovation and client success. Persistent offers a comprehensive suite of services, including AI-enabled software engineering, product development, data and analytics, CX transformation, cloud computing, and intelligent automation. The Company has been recognized as the "Most Promising Company" of the Year by CNBC-TV18 at the 2023 India Business Leader Awards. Persistent has achieved carbon neutrality, reinforcing its commitment to sustainability and responsible business practices. As a participant of the United Nations Global Compact, the Company is committed to aligning strategies and operations with universal principles on human rights, labor, environment, and anti-corruption, as well as take actions that advance societal goals. With 327% growth in brand value since 2020, Persistent is the fastest-growing IT services brand in the 2024 Brand Finance India 100 Report.

USA
Persistent Systems, Inc.
2055 Laurelwood Road, Suite 210
Santa Clara, CA 95054
Tel: +1 (408) 216 7010
Fax: +1 (408) 451 9177
Email: info@persistent.com

India
Persistent Systems Limited
Bhageerath, 402
Senapati Bapat Road
Pune 411016
Tel: +91 (20) 6703 0000
Fax: +91 (20) 6703 0008

Persistent

www.persistent.com