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Navigating Regulatory Developments and Meeting Investors' Needs in a Global Industry

By Jeanne Arnold

There is a great opportunity for capital markets to develop all over the world, presenting a huge opportunity for the mutual fund industry, according to David Wright, secretary general of the International Organization of Securities Commissions (IOSCO). The question, he said, is, "Can we seize the moment?"

Wright posed this important question during his remarks at ICI's General Membership Meeting (GMM), held May 6–8 in Washington, DC. He gave an opening speech at the final day's morning session, "Regulatory Developments and the Demands of Operating a Global Asset Management Firm," setting the stage for a lively and insightful conversation among a group of panelists whom he joined to discuss capital market initiatives worldwide, the debate surrounding asset management and financial stability, and the challenges and innovations in the Asia-Pacific region.

Capital Market Development: A Global Trend

During his opening remarks, Wright examined efforts around the world to develop and strengthen capital markets, citing several reasons behind these efforts:

- an increasing recognition of the role that deep, liquid capital markets can play in fostering economic growth;
- a growing need for alternative sources of financing outside of the banking sector; and
- challenges facing governments worldwide in funding pension obligations.

"The world is moving in the direction of the U.S. financing model, and I think this is an extraordinary and timely opportunity for U.S. political and regulatory leadership," he asserted. "Yet it won't be here forever. I would argue that the United States is in its strongest position right now, because, every day that passes, the share of U.S. capital markets in global capital markets will decrease as others rise up, including China, India, and Brazil."

Wright also noted that even as policymakers are pursuing capital market initiatives—notably in the European Union through the Capital Markets Union (CMU) initiative—global regulators are becoming more concerned about certain aspects of market-based financing, including the role that asset managers and their funds play in financial stability.

Support Reducing Systemic Risk—Not Market Risk

Offering an update on the work of the Financial Stability Board (FSB) and IOSCO, Wright stated that the FSB could have a final methodology for designating funds or their managers as global systemically important financial institutions (G-SIFIs) by the end of the year. He also mentioned a new FSB/IOSCO workstream focusing on analyzing asset managers' activities, which he said the organizations should be ready to begin to discuss by August.

What happens in the United States with the work of the Financial Stability Oversight Council, however, "will have a crucial bearing on the overall global outcome," said Wright, adding that everyone also should bear in mind what Securities and Exchange Commission (SEC) Chair Mary Jo White said in a speech last December. "I very much agree with her words that 'our objective is not to eliminate all risk. Far from it. Investment risk is inherent in capital markets—it is the engine that gives life to new companies and provides opportunities for investors.'" He further agreed with White that as regulatory programs evolve, so must regulators' understanding of the balance between "reducing undue risk and preserving the principle of 'reward for risk' that is at the center of our capital markets."

Once the panel got started, panelist Barbara Novick, vice chairman of BlackRock, agreed with both Wright's and White's shared sentiments, explaining that BlackRock "very much supports reducing systemic risk in the markets—but we don't believe in reducing market risk. We think that's what markets are all about. That's how capital is allocated, and that's a very important part of our system."

Novick also refuted some "misinformed theories" she said regulators have about asset management and financial stability, concluding that "the only way to reduce systemic risk—if there are risks to be addressed—is to take a product and activities approach, one that deals with the entire market ecosystem."

Pressing on the Accelerator While Pulling on the Brake

Bringing two of the panel's main topics together—the trend toward developing capital markets, and the debate surrounding financial stability and asset management—Christian Dargnat, CEO of BNP Paribas Asset Management, discussed how regulators' efforts could affect capital market initiatives in Europe, specifically the CMU.

The goal of the CMU is to diversify and deepen funding sources for the EU economy by developing and integrating the region's capital markets. However, he said, the FSB's work on asset management and financial stability is at odds with the CMU's goal, because it would hinder market-based financing—a key element of strengthening the European Union's capital markets.

"It is as if you were driving a car," said Dargnat, "and you were pressing the accelerator while pulling on the brake."

Speaking about the regulatory challenges facing the industry and the FSB's work, Dargnat added that "the FSB has a tendency to look at everything as a bank. Asset managers are not banks. Our business model is completely different. It is based on an agent model, not a principal model."

Challenges and Innovations in the Asia-Pacific Region

The panelists also discussed how to meet evolving investor needs in a global marketplace. David Semaya, executive chairman of Nikko Asset Management, highlighted the challenges that the Asia-Pacific marketplace presents. The Asia-Pacific region is a very diverse place, he explained. For example, as the Japanese population ages, Japanese clients are focusing less on accumulation and more on decumulation. Meanwhile, the industry faces a rising middle class in other markets, and young people who don't want to put money in a savings account, as their parents did. "They're looking to us for guidance on how to invest—but 'investment' in Asia often means 'trading,' so delivering the right plan and advice to that cohort is critical for us," said Semaya.

Finally, there is China, where investors are technologically savvy and want to know about their portfolio securities in real time. "They want to know what decisions are being made in [regulated funds] and why this stock was sold and this one was bought," stated Semaya. "This is a challenge because everyone is connected, people are on Twitter, and this will affect our business."

Speaking about innovation in the Asia-Pacific region, Wright discussed his curiosity about Chinese e-commerce company Alibaba, which—among other services—allows customers to invest in Yu'e Bao, a money market fund that already has collected $87 billion in assets, according to the *Wall Street Journal*.

"Alibaba is a fascinating development," he said. "It seems to me that this convergence of e-commerce trading with payment systems in financial markets is immensely powerful. I've suggested Europe needs [its own] Alibaba, which would connect businesses through Europe and facilitate development of capital markets."

Remarking on the range of topics covered during the panel, moderator Campbell Fleming, CEO of Columbia Threadneedle Investments, said that the asset management industry is putting "a lot of effort and intellectual firepower" into the issues discussed, particularly those surrounding capital market development and financial stability.

"It behooves us to get these right," he concluded. "We only exist because people give us their hard-earned savings to manage, and we must never forget that."

Jeanne Arnold is a senior writer and editor for ICI.