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Re-establishing the fund management industry: some observations

Emerging from the Ashes: Prospects for European Wholesale Banking in the Wake of the Crisis

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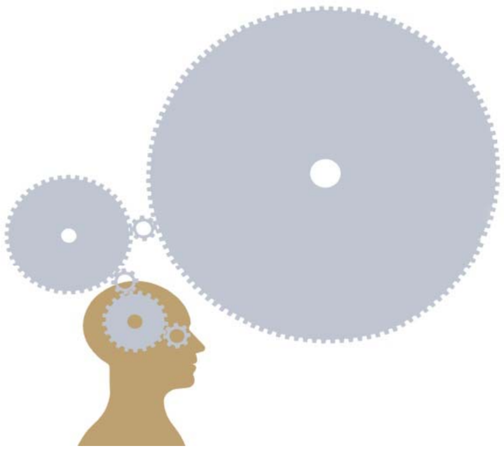

March 31st 2009

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Overview

- impact of the financial crisis on investment managers (IMs)
- role of IMs in
    - facilitating private savings and investment
    - establishing efficient capital markets
- regulatory change and challenges

Impact of crisis on IMs

- significant fall in assets under management
- net outflows from investment funds
- downward pressure on margins
- shifts in desired asset allocation and product preferences
- regulatory reform programme

⇒ short-term adjustments are required, but what are the long-term challenges and opportunities?

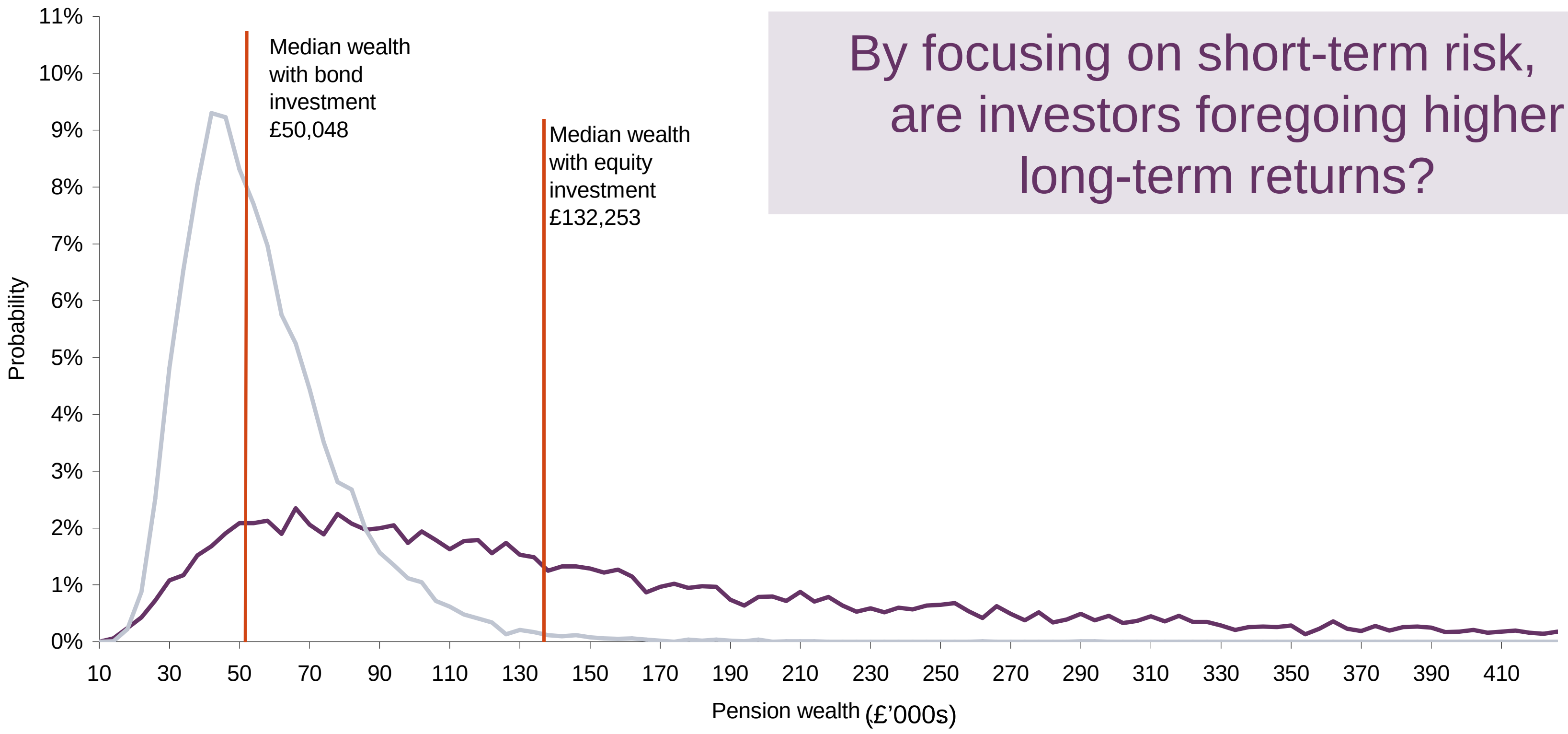
Facilitating long-term private savings and investment

- losses of confidence in capital markets and intermediaries
  - increased risk aversion
- a concern for public policy given shift to private pension provision (and defined-contribution pensions)
  - exacerbates problem of undersaving and insufficient retirement provision
- more need than ever to focus on key IM functions
  - manage investment risk and return
  - develop product solutions to meet individual needs and preferences
  - promote advice and financial education

⇒ contributes to restoring confidence and developing a growing market for private savings and investment

Impact of investment choices
An illustration

Simulations of impact on retirement wealth (30 years)



By focusing on short-term risk, are investors foregoing higher long-term returns?

Notes: Simulations of retirement wealth accumulation for 10,000 individual accounts, based on historic risk-return parameters for real government gilts (bonds) and equity returns for the UK since 1950 (obtained from Barclays Equity Gilt Study 2008). The individual contributes £1,000 in the first year, and contributions then grow at a rate of 2% (real) over 30 years. No tax and management fee.

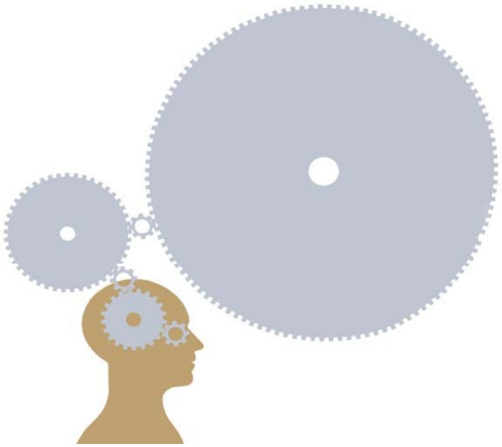
Source: Oxera modelling.

Establishing more efficient capital markets

- IMs can, and now more than ever should, play an active role, by
  - exerting pressure to reduce all-in transaction costs
  - improving corporate governance and exercising due diligence
  - facilitating product innovation
  - valuing assets (and challenging methodologies used by others)

Regulatory change should facilitate not hinder

- La Rosiere and Turner reports are explicit that IMs were not main source of problem, but specific proposals are directly relevant
  - rules for certain investment vehicles
  - definition of economic activities
- policy debate focuses on increasing capital requirements for banks, but higher capital cannot be the answer in IM
  - risks in IM are different to those in banks and insurance
    - no own positions, segregation of client assets
  - other risk mitigation mechanisms are more effective
    - strengthen custody arrangements and role of depositary/trustee



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