la SOCIÉTÉ FRANÇAISE des ANALYSTES FINANCIERS

Le Délégué général

Paris, August first, 2014

ESMA Consultation (MIF II) – answer to question n°79

Q79. Do you agree with the proposed exhaustive list of minor non-monetary benefits that are acceptable? Should any other benefits be included on the list? If so, please explain.

No, SFAF does not agree with ESMA's approach.

1. The role of research

Investment research and more precisely financial analysis is an auxiliary investment service (Code monétaire et financier art. L. 544-1). Its role is to provide decisive insights on the investment process to enable asset managers to make decisions in the customer's best interest. As such, it is an integral part of the investment process.

Financial analysis is a specific intellectual service which rests on knowledge of the sector, of the governance structure of the issuing company, of the risks inherent to the activity, of the quality of the issuing company's information tools, on account analysis. It requires an ongoing study of the equity in question. As such it is a unique service based on the analyst's inner convictions and in due consideration of the market information issued to investors.
The value and pertinence of the analysis for asset management firms stems from the diversity and confrontation of opinions.

Financial analysis is present on all levels, from asset allocation based on financial instruments, through choice of sectors and down to the ultimate choice of the issuing company.

The financial analyst provides a clear added value to the asset manager for maximizing the efficiency of their investment strategy IN THE BEST INTEREST OF THEIR CLIENT.

2. Remuneration of financial analysis

Producing quality financial analysis has a significant monetary cost. It represents almost 2/3rds of all invoiced commissions.

Although SFAF fully agrees with the principle of improving the transparency of Research costs, the change proposed by ESMA does not appear to us to be in line with the ultimate goal of improving customer service

In substance, we consider that Research is a value added service and as such cannot be classed as non-monetary advantage. It also cannot be considered an inducement. Ultimately, the asset manager makes the choice of the financial analyst to remunerate. It is a false assumption to believe that the asset manager is benefitting from an advantage at the expense of the end customer.

On the form, and this is the focus of question 79, the way in which Research is financed does not affect its inherent nature. Whichever way Financial Analysis is remunerated, it remains an essential necessity for asset managers. It allows managers to provide the best possible return on investment.

3. Existing measures and other solutions

In order to guarantee proper functioning of the invoicing process with full due concern for transparency and fairness for the end customers, there are already existing measures provided for by MIF I such as:

- Order execution policies, better selection of intermediaries,
- The existence of a register and a system for detecting and managing conflicts of interest,
- Implementation of commission sharing arrangements (CSA).

Before calling into question the method for financing Research, it is necessary to review the existing policies and devices in order to improve them as well as to step up the use of CSAs.

It is possible to ask asset managers for increased transparency by, for instance, providing a half yearly summary of costs incurred. In this way, end customers will be able to ensure that the services provided are adequate to their needs.

4. Negative impacts and risks

SFAF considers that ESMA's proposal will have the following effects:

- A violent unbalancing of the Research ecosystem which will negatively impact the depth and breadth of supply and therefore impoverish the available help in making investment decisions,
- A drastic reduction of small and mid-cap coverage, favouring the use of non-independent research, paid for by issuing companies,
- Harder access to all type of Research for small asset-management firms,
- A competitive disadvantage for European based asset-managers compared to those in the United States and Asia,
- A concentration of Research suppliers with the emergence of monopolistic situations.

5. Conclusion

SFAF considers the measures proposed by ESMA to be damaging for Research, for financial analysis and therefore, ultimately, to ESMA's stated goal of protecting the interests of investor interests.

ESMA wishes to implement important changes in the industry without previously evaluating the negative impacts and the risk of endangering the current business model and causing the disappearance of certain brokers, independent suppliers and asset management firms.

SFAF argues for the importance of increasing and diversifying the number of participants to achieve comprehensive financial analysis in order to give asset managers as full and clear a view as possible of the issuing companies.

SFAF also puts forward that analysts are one of the main balancing forces in favour of shareholders and others stakeholders as opposed to the communication provided by listed companies and its possible abuses. In addition to its essential role in helping asset managers in their decision making process.

For all these reasons, SFAF is strongly opposed to the implementation of these measures.