FINANCIAL TIMES
MONDAY 10 DECEMBER 2018
FTfm

Investment research

Mifid II leads to global demand for transparency

Asset managers 'unbundle' research payments across worldwide operations, survey reveals

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European rules on the funding of investment research are changing behaviour globally in a shift that has consequences for fund houses, banks, brokers and investors.

Mifid II, introduced in January, requires European asset managers to separate the cost of research from trading commissions and transaction charges paid to banks and brokers, a process known as unbundling.

The reform was designed to improve investor protection by ensuring that asset managers' decisions could not be influenced by receiving research free.

More asset managers are implementing the European rules on research procurement across their worldwide operations in response to demands from investors for transparency.

A survey of 55 asset managers by Liquidnet, a trading venue, found that 53 per cent had already implemented European research unbundling standards as a global policy. A further 20 per cent planned to do so within five years.

"Research unbundling is going global. It is being led by investor demand as well as the practicalities of implementing [European] regulatory policy across different jurisdictions," said Rebecca Healey, head of Emea market structure and strategy at Liquidnet.

AllianceBernstein, MFS and Baillie Gifford have all implemented research unbundling globally.

Others have tried to limit research unbundling to European operations, waiting to see any changes made by regulators outside Europe and by competitors in the US and Asia.

Even within Europe, however, the rules have not been implemented uniformly. Ms Healey said she expected the European Securities and Markets Authority, the regional regulator, to push for consistent application.

France's financial regulator, the Autorité des Marchés Financiers, called for a review in November due to concern that research coverage of smaller and mid-sized companies would suffer. Almost half of the managers surveyed by Liquidnet said research coverage of small and mid-sized companies had been affected.

Some observers fear that smaller companies could struggle to attract investment if research coverage shrinks.

Some brokers and independent research houses, especially in London, are struggling to adapt to the drop in revenue caused by the new regime. This has forced some to consider a merger or sale to larger rivals.

Concerns about inconsistency in the interpretation and application of Mifid II led the UK's Financial Conduct Authority, the City regulator, to review the rules on research procurement during the summer.

Price quotes from some big banks for the entirety of their published research output have fallen to between $10,000 and $30,000 a year, from six-figure costs that were mooted in 2017.

The FCA has warned that investment banks cannot offer "unduly favourable terms" for research in an effort to entice asset managers to direct trading orders to them.

Ms Healey said the business models of investment banks had to evolve as asset managers were increasingly looking for new sources of investment ideas from social media and big data to complement traditional fundamental financial analysis.

"Both the production and consumption of investment ideas is set for wholesale change," she said.

**This article has been amended since publication to reflect the fact that Franklin Templeton's policy of unbundling research payments is limited to Europe following a clarification from the company.*