Amid Global Market Complexity, A Simple Focus on Investors

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As prepared for delivery

Good morning, ladies and gentlemen. I am Dan Waters, Managing Director of ICI Global, and let me extend a warm welcome to all as we begin our inaugural Trading and Market Structure Conference.

We have a robust programme, and I commend my colleague Ari Burstein, who leads for ICI Global on our markets brief, for his efforts in assembling it.

Our panel discussions today will cover several major topics: the role of the exchanges; technology; order routing; derivatives regulatory reform; and regional developments in securities markets. Each of those major topics has myriad subtopics, within which there is room for multiple points of view.

I am happy to say that we have some of the sharpest and best-informed minds in business and government with us today to help us master this complexity. I am especially looking forward to our keynote speakers: Verena Ross, the Executive Director of ESMA; Kay Swinburne, Member of the European Parliament; and Emil Paulis, Director, Financial Markets in DG Markt at the European Commission.

In addition to sharp and well-informed minds, we have another guide to help us through the sometimes daunting complexity of the issues on our agenda today: that is, a simple focus on investors.

This event will examine trading and market structure issues from the perspective of the buy side; and in particular, the long-term investor. It makes perfect sense that this should be our approach today, because an investor focus is a defining feature of ICI Global's mission.

We represent the interests of global funds, their managers and investors. These funds may be based anywhere in the world; but they must be regulated and authorized for sale to the general investing public, including institutional investors. ICI Global has grown to represent a diverse group of members in North America, Europe, and Asia who manage more than $1 trillion in registered fund assets.

Our members, major market participants serving millions of individual and institutional investors, have a strong interest in ensuring that global financial markets are highly competitive, transparent, and efficient. Accordingly, the regulatory structure that governs these markets must encourage, rather than impede, capital formation, liquidity, transparency, and price discovery.

Consistent with these goals, ICI Global has strongly supported efforts to address issues that may affect the fair and orderly operation of the financial markets—and investor confidence in their integrity. It is maintaining this confidence that must be our paramount concern.

So, just to warm us up, let me briefly outline one area where many of these efforts are taking place and on which we will hear plenty more today: technology and associated market risks.

Technology and its impact on financial markets, of course, is a deeply complex subject. But I think we usefully simplify the matter by asking ourselves a fundamental question, one that returns to the investor focus I have just described: Are capital markets working well for today's investors?

In many respects, the answer is yes. More than ever, investors around the world can choose from a wider range of investment products, in a wider range of markets and at lower cost.

Technology has unquestionably been a driver of that progress. New technological tools and capabilities have given retail and institutional investors much greater control over how their trades get done.

They have also contributed to lower overall trading costs and improved efficiency. Witness how heavily funds rely on technology for the efficient execution of their trades. That is why ICI Global devotes so much effort to tracking the evolution of technologies for generating, routing, and executing orders—as well as the changes in the speed, capacity, and sophistication of trading functions.

But technological advances, while bringing undoubted benefits, have also brought with them new challenges. These challenges signal to us that in some respects, capital markets are not working as well as they could for investors.

At the broadest level, it is clear that technology still poses risks to the marketplace.

In recent years, we have seen a troubling number of disruptions to market infrastructure, starting with the flash crash in the United States and continuing with a spate of recent technological problems experienced by exchanges, banks, and other trading venues.

Technological advances in trading may also enable those who would manipulate markets to do so more easily and cheaply.

Another challenge is regulatory: Simply put, changes in trading practices have outpaced regulations governing the financial markets. The potential for market abuse and disorderly trading related to computer generated orders remains troubling.

As someone who spent three decades as a financial regulator, I know how hard government agencies and regulators are working on these issues. I commend Verena and her team at ESMA, who have been working night and day for many months on the hugely demanding market structure reform agenda in Europe, itself mirroring the work going on around the globe.

That work is reflected in the regulatory engagement of ICI Global. Just in the past few months, we have filed comments on a consultation by the Hong Kong Securities and Futures Commission regarding proposals to enhance the regulatory framework for electronic trading; we have commented on an IOSCO consultation examining the challenges posed by technological developments to effective market surveillance; we have continued to engage with the reform in Europe of the Markets in Financial Instruments Directive, which would create a new regulatory structure for automated trading, high frequency trading firms, and electronic trading venues; and we also are monitoring efforts in Asia, Australia, and Canada that would address technology and related risks.

In our engagement with regulators, we have called attention to several factors, closely tied to technology, that have the potential to contribute to disorderly markets. One of those factors is the proliferation and complexity of order types. In the race for increased market share, trading venues continue to create order types to cater to market participants who are looking for a vehicle through which they can implement automated trading strategies.

Many of these order types allow strategies that may benefit those particular market participants—but that may also come at the expense of others in the market. Equally troubling, some of these order types also enable potentially abusive or manipulative practices. That is another big negative from the standpoint of the long-term investor.

Another issue we and other commentators have called attention to, is the large number of order cancellations in many securities markets, particularly orders that are cancelled almost immediately after submission.

These kinds of cancellations can strain the markets' technological infrastructure, and they have the potential to interrupt the ability to process trades. If we want to foster investor confidence in our markets, this is an issue that must be addressed.

Identifying challenges is often the easy part, of course. The real question is: what to do about them?

I will not run through the particulars of our recommendations to regulators. Many of these will be discussed today. At a high level, however, there are a number of important messages to regulators that we hope are getting through—three in particular, which I mention now.

First and foremost, we urge regulators to do what I hope we will all do today: maintain a steady focus on investors—particularly those who invest for the long term. At a minimum, this means ensuring that these investors are well represented in the discussion. Unfortunately, we have seen instances where long-term investors have gotten lost in the shuffle.

Across the Atlantic, for example, the Securities and Exchange Commission recently held a Technology and Trading Roundtable. We were disappointed that the event had no representation from those on the buy side who take the long view. It seems to us unlikely that industry advice gleaned from such an exercise will be balanced and fully reflective of the investor perspective.

A second key point for regulators: international coordination. Duplicative or conflicting requirements from country to country add harmful complexity to the markets. So we have consistently and strongly urged regulators to make harmonization a priority.

While not strictly related to technology, this need for harmonization is particularly acute when it comes to the derivatives market. The current tussle between the US and the EU on the regulation of OTC derivatives is worrying to us and indeed worrying to regulators and market participants in Asia, who want to be part of sensible, workable arrangements at international level.

A final priority, if I may, for regulators: balance. I am suggesting to Verena and other regulatory authorities, I believe, nothing that they do not already know. Market authorities worldwide must take a measured approach. If regulations are too restrictive, they may unintentionally limit the use of evolving practices and technological developments, impeding funds' use of innovative trading tools to the benefit of their investors.

If regulations are too costly for some market participants, those participants may decide not to offer certain products or services. Or the cost of trading may increase as market participants shift the burden of compliance with new requirements to investors. The tried-and-true disciplines of cost-benefit analysis and evidence-based policymaking must be preserved, even in the difficult circumstances of demanding international timetables.

Investor focus, coordination, and balance. These are simple but powerful concepts for regulators and market participants alike.

We must foster and strive toward these ideals, so that when we ask ourselves the question—"do capital markets work well for investors?"—we can answer without hesitation, yes. Thank you.

I am now delighted and privileged to introduce my friend and former longtime FSA colleague, our featured speaker for this morning, Verena Ross, Executive Director of the European Securities and Markets Authority.

Verena took on her job at ESMA in June 2011. At the time, observers hailed her deep technical expertise, her strategic understanding of regulatory issues, and her experience in international financial regulation. That experience began in 1994 at the Bank of England, where Verena worked as an economist and then a banking supervisor. Four years later, Verena joined the UK's Financial Services Authority to run the Executive Chairman's office during the FSA's start-up phase.

Verena rose quickly in the Markets Division of the FSA, and then became the Director of the Strategy and Risk Division and subsequently Director of the International Division, a position she held until May 2011.

At ESMA, Verena has spoken strongly on a variety of issues, including the need to ensure that regulatory bodies have the resources and deep technical expertise they need to create standards that work for the EU's different markets.

Creation of such standards, of course, is a challenge as tough as any regulator has faced. Verena has articulated a forceful vision of what ESMA can and should accomplish. "This is not about the lowest common denominator," Verena said last year. "It is about genuinely finding the right answer for Europe."

Indeed, just so. Ladies and gentlemen, Verena Ross.
