

## ICI President and CEO Delivers Opening Remarks at Securities Markets Conference

# 2007 Equity, Fixed Income, and Derivatives Markets Conference

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Good morning. I'm Paul Stevens, President and CEO of the Investment Company Institute, and I'm pleased to welcome you to this, our ninth annual conference devoted to the structure and operation of the securities markets. Over the short life span of this conference, financial markets have undergone rapid and dramatic changes -- some of which, particularly those in the equity markets, investment companies have helped to shape.

Trading and investing in equities are, of course, bread and butter for our industry, and we remain fully engaged in the issues that arise in this marketplace. These issues will continue to have a critically important place on the agenda of the ICI and of this conference.

Contrary to popular opinion, though, there's more to investment companies than stocks. Bond funds have been a presence in the modern industry at least since 1926, when the Bond Investment Trust of America was organized in Boston.

In 1984, bond fund assets totaled \$46.2 billion. Last year, they had grown to \$1.5 trillion.

That growth is certain to continue. And with this in mind, ICI will do its part to encourage the smooth and efficient operation of the fixed-income markets just as we have for the equities markets. Here, too, we are committed to raising the voice of the buy-side of the market.

As a small symbol of that commitment, we have changed the name of this conference. What was the Equity Markets Conference is now the Equity, Fixed Income, and Derivatives Markets Conference. We thought about boiling that down to the acronym EFIDMAC, but the recent experience of other financial organizations shows that acronyms are a risky business -- so we won't go there.

Against that backdrop, let me touch on three related topics, very briefly.

First, ICI's involvement with issues important to the functioning of the fixed-income markets.

Second, money market mutual funds -- a part of our industry that has enjoyed remarkable success over many years, but has been tested in recent months.

And third, the shapes of things to come.

First, fixed-income.

As this audience is well aware, mutual fund investors have a wide and still growing range of investment options, including many in which fixed income securities comprise the entirety or a significant portion of the fund's holdings. And there is every indication that fund investors are taking advantage of this expanded menu.

Consider the following:

The latest government statistics show that in the first half of 2007 households bought, on net, about \$225 billion in bonds and commercial paper through mutual funds, including money market funds. In contrast, during the same period they bought, on net, only about \$36 billion of these same securities outside of mutual funds.

Between 1996 and 2006, registered investment companies' holdings of municipal bonds increased from \$445 billion to \$809 billion; of U.S. Treasury and Agency securities from \$475 billion to \$952 billion; and of U.S. and foreign corporate bonds from \$290 billion to \$1.1 trillion.

During the same decade, retail holdings of bond funds and hybrid funds almost tripled, from \$770 billion to almost \$2 trillion.

In recognition of these and other developments, regulators, to their credit, have acted to make the debt markets more transparent. Investors now have access to FINRA's Trade Reporting and Compliance Engine, or TRACE, for corporate bonds, and to the MSRB's Transaction Reporting System for municipal bonds. By the way, our first panel today is devoted to issues affecting the securities markets from the regulators' point of view, and we are fortunate to have with us Doug Shulman of FINRA, who was, as much as anyone, the progenitor of TRACE, and Lynette Hotchkiss of the MSRB.

Both the muni and corporate bond markets were all but invisible to mainstream investors before these two systems went on-line -- TRACE in 2002 and the Transaction Reporting System in 2005. Their introduction made it much easier to get up-to-date trade and price information about corporate and municipal bonds, moving the disclosure regime for those securities much closer to that for equities.

Transparency has led, in turn, to better prices for bond investors. Bonds that had been opaque before TRACE went online got cheaper afterward -- their spreads shrank. Not coincidentally, this was less the case with bonds that already had some measure of transparency.

In a recent speech and in a white paper submitted to Congress, SEC Chairman Christopher Cox has called for still further improvement in the quality of disclosure to investors in the \$2.4 trillion municipal securities market.

Much remains to be done. We look forward to working with the SEC, FINRA, and MSRB, as well as other market participants, on these and other issues. Continued improvements in the bond market are doubly important in light of the aging of the Baby Boom generation -- the leading edge of which begins to retire in 2011. As working Americans get older, many of them logically will shift some of their retirement savings into a variety of fixed-income securities and out of equities. We can expect continued growth in demand for those products for decades to come.

Money market funds, too, have registered big gains in popularity, and this is the second of the three topics I want to talk about today. Money market funds represent a remarkable chapter in the history of American mutual funds. Today, retail and institutional investors alike rely on these funds as a cash management tool because they offer daily liquidity and current yield. ICI estimates that between 1983 and today, \$140 trillion flowed into, and about the same amount out of, money market mutual funds, a testament to their success.

Money market funds represent an industry success story, and a regulatory success story. Since its adoption in 1983, Rule 2a-7 under the Investment Company Act has governed money funds quite effectively. In that 24-year period, money fund assets have grown over 1400 percent, from \$179 billion to \$2.8 trillion.

Among other things, Rule 2a-7 imposes exacting standards on money funds' portfolios and instruments, including credit quality, maturity and diversification. The rule has worked, as intended, to help money funds weather the occasional storm and maintain a stable net asset value of one dollar per share.

As you probably know, since Rule 2a-7 was adopted in 1983, only one money market fund has "broken the buck" -- that is, failed to achieve its objective of maintaining a constant NAV per share. That was a small institutional money fund in 1994. No retail investor has taken a loss in a money market fund since the rule was adopted, and investors' confidence in these funds has proved to be well founded.

This regulatory regime proved its worth yet again in the subprime mortgage crisis. Commentators in the press and elsewhere have expressed a fear that the crisis would spill over into money market mutual funds, but it hasn't. So far, they have weathered this particular storm reasonably well.

Still, there is no room here for complacency. It is critically important that this record of success achieved under Rule 2a-7 be sustained for the benefit of investors. During the recent market disturbance, ICI has been in regular contact with the SEC and the

Federal Reserve, providing them with current data and facilitating their efforts to monitor market developments. Government, of course, has a vitally important role. But maintaining the record of money market mutual fund success critically depends on the continued discipline and vigilance of fund advisers and boards operating within the framework of applicable regulations. ICI does all it can to support money fund advisers and boards in this process.

Similar discipline is required in light of the increasing use by investment companies generally of derivatives and other complicated financial instruments. Like a fund's other investments, derivative investments may entail various types and degrees of risk, depending upon the characteristics of the particular derivative instruments and the fund's portfolio as a whole. Our derivatives panel today will shed light on how funds and other institutional investors use derivatives, and the range of risks they can pose.

Finally, I'll say a few words about where things seem to be going. The pace of change in the capital markets since 1999, when this conference debuted, has been breathtaking. Back then, the "cutting edge" issues we focused on included how the Internet would affect trading desks, the prospect of for-profit exchanges, and the proliferation of ECNs and other alternative trading systems. Imagine, if you will, what issues will occupy this conference nine years from now.

As Yogi Berra said, "it's tough to make predictions, especially about the future." But I think I'm on solid ground in predicting that this wave of change will continue unabated for quite some time.

One harbinger of the future is the fevered pace of international exchange mergers. The New York Stock Exchange's acquisition of Euronext has precipitated a frenzy of activity, whose ultimate outcome is unpredictable. The only certainty seems to be that global trading venues and linkages will be dramatically changed in a very short time.

This is evidence of the fact that all the markets we're here to talk about today -- equity, fixed income, and derivatives -- are no longer domestic on either the buy-side or the sell-side. We now toil in a marketplace that is oblivious to borders and time zones. It's as if the Atlantic and Pacific Oceans had narrowed to the width of mere rivers, with Asia in full view to the west and Europe to the east.

This is what globalization is all about -- blurring national boundaries, connecting old to new, tradition to innovation.

It seems to me that making those connections is exactly what our industry has to do to remain competitive in a dramatically changed world. And I'm happy to say that investment companies and other financial services firms have been doing exactly that; many of our members now have global operations and are highly active in international securities markets. In fact, you can hardly open the business section of a newspaper today without seeing a story about an American investment firm setting up shop in Europe or China, or an American equities exchange trying in one way or another to win listings of foreign companies.

These developments are just the early phases of a process that will, over time, transform the world's securities markets. They are of vital interest and concern to all of us -- including, whether they realize it or not, the 90 million or so fund shareholders that our members serve. ICI expects to continue to chronicle all these developments in its conferences in years to come. Thanks to each of you for being a part of our 2007 proceedings.

Before we begin, let me add my special thanks to three ICI colleagues -- Ari Burstein, Jane Heinrichs, and Heather Traeger -- for their part in putting together today's outstanding program.

I am grateful for your attention, and sincerely hope you will both enjoy and benefit from this conference.