



Holland Macro Views

Jamie Dimon stole my lunch (and livelihood)

Dear Sir

Your Lex article '*SocGen/Bernstein: eat what you kill*' demands a response from the independent investment research coal face. In your piece you observe "*the shrinking pool of market analysts suggests risks to market efficiency*". I would go further; this sector is being completely hollowed out. Most analysts have sought jobs outside the industry and will never return. This was a vibrant sector offering a real challenge to the investment banks pre-MIFID II changes. Indeed, its success was often highlighted by the FCA as to how successful its unbundling policies had been. Investment manager clients also loved the better-quality research at lower prices independent firms brought.

Your piece also highlights '*Independent research is being priced out of the market by cross subsidisation of research within investment banks*'. That Lex presents this cross subsidisation as a statement of fact is welcome, and overdue. When the FCA zealously implemented MIFID reforms it tried to claim that unbundling would still exist (i.e. between research and other banking functions inside a bank). To any of us in independent research this was clearly nonsense. Andrew Bailey, then FCA head, was so delighted with the savings he thought he was delivering to unit-holders he was uninterested in the obvious second order consequences that would follow. Investment banking cross subsidisation enabled them to kill off the independents who had become a thorn in their side. In short MIFID II implementation has not just reduced the quality of analysis, it has destroyed UK small businesses competing with large incumbents, most of which are US owned investment banks. That such a policy could have been implemented with so little thought by a UK regulator who had actively encouraged this sectors development is frankly startling.

Quite what information Investment banks provide to the FCA to prove standalone trading, banking and research services (and so justifying their low research pricing) I don't know. One must guess that they claim their investment banking and trading departments use research so are happy to pay for, say 75% of, its cost. Research revenues from portfolio manager clients therefore only need to make up the rest. Having worked in an investment bank for a decade before setting up my own independent research firm I can tell you this is fiction. If you had asked a trader or investment banker to take research as part of their cost base they would have laughed, hard.

Implementing a change that meant investment research need be paid for by Portfolio Managers rather than by unit holders may have been right. The assumption would then be that the best research would survive. The opposite has occurred. Large portfolio manager company CEOs were keen to protect their profits post incurring research costs. The way to do this was bulk buy. Such CEOs maybe chatted to their counterparties at investment banks and thus a deal was done. Blanket coverage research would be provided for a low price. The big beasts (Bank and portfolio manager CEO's & the regulator) will tell you all is well. Talk to the portfolio managers that look after, and care about clients' funds rather than just their company P+L, and the negative consequences are far easier to see. Such cheap blanket research does not provide the analytical insight they need.

Their ability to choose what research they get from where is now severely limited by both the price disparity and pressure from their CEOs to keep cost down.

When I try to describe to those outside my industry the mess these regulatory changes have made and the consequence to my business, I describe it thus. *“It is like being a milkman when Tesco decides to loss lead milk”*. As a strong believer in competitive forces, I feel I should not really complain. That said, I know my cost base is way lower than my investment bank competitors, but I still cannot compete. I also only entered this world of independence (that I love) because the regulatory umbrella of unbundling encouraged me to do so. Did I miss something and regulators became King makers rather than fostering greater competition? Sadly, Andrew Bailey has far too much on his plate today to have time to reflect on the carnage this policy has left behind.

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