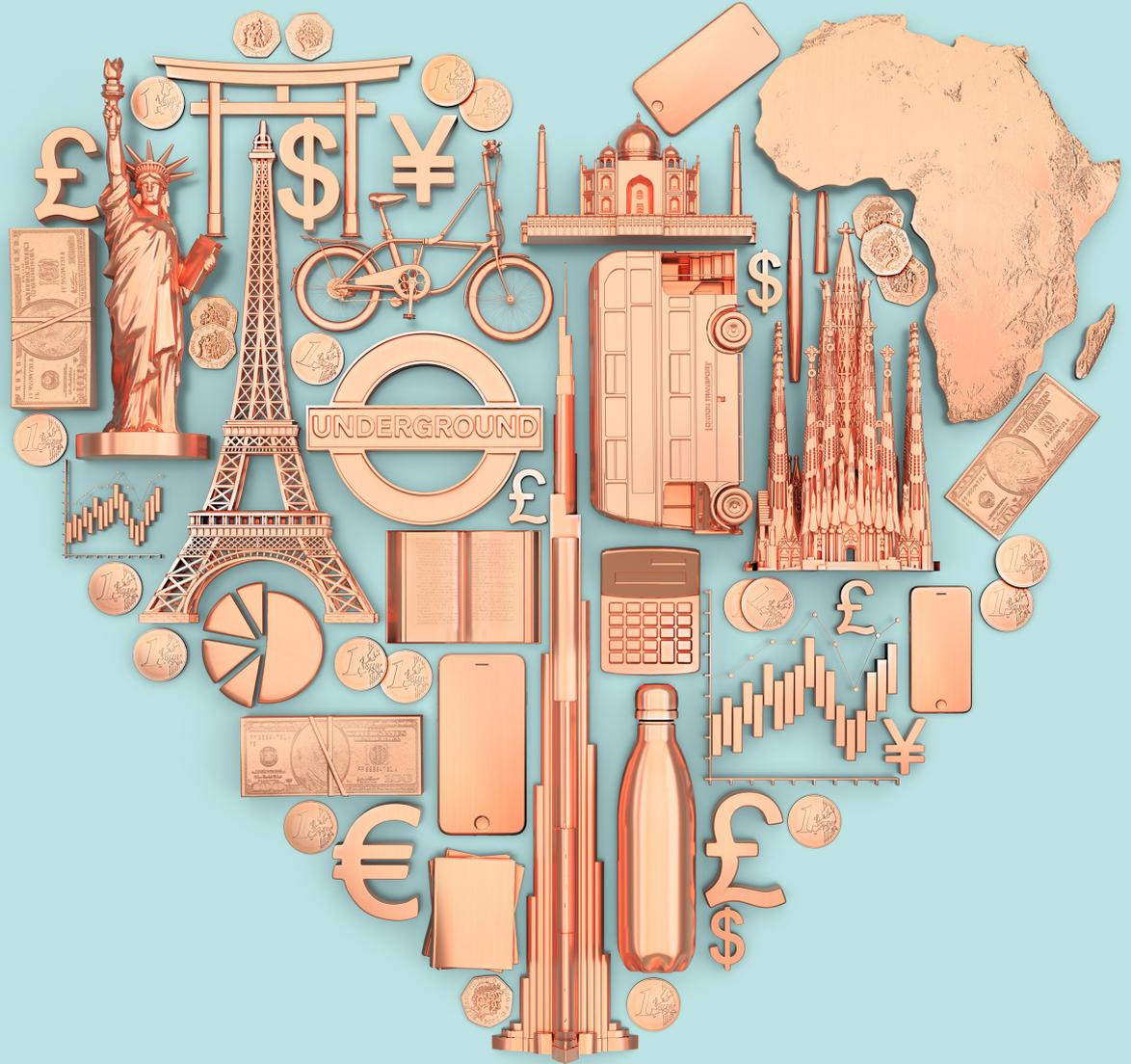


WHAT DOES THE NEW
EU COMMISSION HAVE IN
STORE FOR THE SECTOR?

HOW TECHNOLOGY
IS HELPING TO ADVANCE
FINANCIAL INCLUSION

GLOBAL BLENDED
FAMILIES AND
FINANCIAL PLANNING



Heart of the matter

WHY FIRMS WORLDWIDE ARE
PLACING PURPOSE AT THE HEART
OF THEIR BUSINESS MODELS

welcome

“Those firms with an established broader purpose aimed at benefiting all stakeholders will often be better placed to weather shocks”



With the world reeling from the human and economic costs of the ongoing Covid-19 crisis, “It may seem as though a broader purpose is now a luxury for many firms, who are currently focused partly or entirely on survival,” says CISI CEO Simon Culhane, Chartered FCSI. However, he says, “those firms with an established broader purpose aimed at benefiting all stakeholders will often be better placed to weather shocks and, crucially, to share value throughout the supply chain.”

Purpose – the ‘why’ of a firm – “sits at the heart of its business model, strategy and culture,” says the UK regulator, the FCA, in its March 2020 discussion paper *Transforming culture in financial services: driving purposeful cultures*. The paper presents the outcomes from a series of round tables instigated by the FCA between June and October 2019, two streams of which were run by the CISI, with Simon chairing the retail investment working group, and CISI chair, Michael Cole-Fontayn MCSI, chairing the wholesale financial markets working group. This feeds into our special report on pages 19 to 27, which looks at the global business case for purpose.

At a suitably social distance (we called South Africa from the UK), we had the pleasure of chatting to Gerhardt Meyer CFP®, chair of the Board of Directors of the Financial Planning Standards Board (FPSB), about his role at the FPSB and the unique perspective he brings to it from his legal background. Read his profile interview on pages 28 to 31.

Other highlights include an ethical dilemma about the reputational impact of individual actions on a firm (pp.46–47); a look at the priorities of the new European Commission (pp.32–35); and an assessment of the reasons for the ever-rising house prices in the UK, especially London, and what this means for clients (pp.60–63).

As ever, please get in touch with any comments or suggestions.

Jane Playdon
Review editor, CISI
jane.playdon@cisi.org

Review editor, Chartered Institute for Securities & Investment

Jane Playdon
20 Fenchurch Street, London EC3M 3BY
T: +44 20 7645 0648
jane.playdon@cisi.org

Editorial Panel

Claire Perryman, Chartered MCSI
State Street

Chair

Helen Anderson
Chartered Institute for Securities & Investment
Michael Cole-Fontayn MCSI
Chartered Institute for Securities & Investment
Simon Culhane, Chartered FCSI
Chartered Institute for Securities & Investment
Scott Dobbie FCSI(Hon)
Deutsche Bank

Sarah Elson CFP™ APP Chartered MCSI
Berry & Oak

Lee Glennan CFP™ Chartered FCSI
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Investec Wealth & Investment

Peter Land, Chartered FCSI
Walker Crips Investment Management

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George Littlejohn MCSI
Chartered Institute for Securities & Investment

Jacqueline Lockie CFP™ Chartered FCSI
Chartered Institute for Securities & Investment

Robert Lockie CFP™ Chartered FCSI
Bloomsbury Wealth

David Madgwick ACSI
SS&C Financial Services

Robert Merrifield, Chartered FCSI
WH Ireland

Tsitsi Mutiti, Chartered FCSI
Charles Stanley

Thomas Oakman, Chartered MCSI
Jarvis Investment Management

Frank Reardon, Chartered FCSI
JM Finn

Nigel Sydenham, Chartered FCSI
CCL Academy

Janet Walford OBE
Financial Planning Editorial Panel chair

Wardour contacts

Editor
William Monroe

Online editor
Bethan Rees

Group art director
Steven Gibbon

Designer
Annabel Gamble

Senior account director
David Poulton

Production director
Angela Derbyshire

Chief executive
Claire Oldfield

Executive chairman
Martin MacConnol

Advertising sales enquiries
David Poulton

T: +44 20 7010 0915

Cover: Hitandrummedia

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Watch



2020 Annual Integrity Debate: Outside the 9 to 5

The debate, held at Plaisterers' Hall in London on 12 February 2020 and filmed for CISI TV, features an expert panel discussing individual behaviour and ethical values, using scenarios from our Grey Matters ethical dilemmas, including the climate change protests mentioned in this edition's dilemma.

Log in to MyCISI to view it and earn 1.5 hours CPD.

MOST READ

Mental health and working from home

cisi.org/mentalhealthwfh

Selling your business: valuation and deal preparation

cisi.org/sellingbusiness

The challenges of examinations - and how to deal with them

cisi.org/examchallenges

MOST COMMENTED ON

Grey matters ethical dilemma: Most likely to...

cisi.org/mostlikelyto



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Our new virtual programme includes #CPDdaily social media posts every weekday, linking to content to help you with your CPD requirements, wherever you are. This includes elearning modules, videos and articles.

To read more, visit cisi.org/review



Read

WEATHERING THE STORM AND MENDING THE ROOF

The Covid-19 crisis has tested businesses' continuity planning to the limit. How well prepared have firms been for such an event, and how will their operations change in future as a result?

cisi.org/weatherstorm



VIRTUAL EVENTS

PARAPLANNER CONFERENCE 24-25 September 2020

cisi.org/ppc20

FINANCIAL PLANNING CONFERENCE

13-14 October 2020

cisi.org/fpc2020

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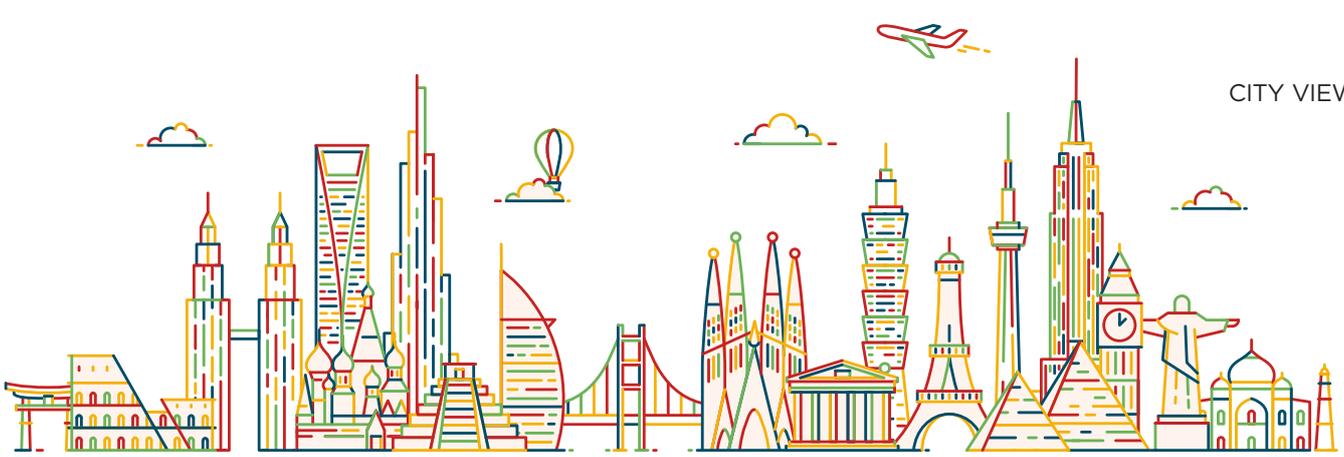
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Responsible finance goes mainstream

CLIMATE CHANGE WILL REMAIN HIGH ON THE AGENDA OF CLIENTS AND REGULATORS AFTER COVID-19

European securities regulators took a rare misstep in April when they watered down disclosure rules on sustainable investment, meant to give investors clear information on the environmental, social and governance risks in their funds. Fossil fuels, they suggested, should only cover coal, not oil and gas. This, said much of the sector, would confound efforts to halt ‘greenwashing’ – attempts to deceive investors into believing their funds are being channelled into environmentally sound assets.

This matters, because demand for the broad range of ‘responsible finance’ – environmental, ethical, faith-based, green, impact, social, sustainable, and their many cousins – has soared among both private investors, particularly at the top end of the market, and institutions, such as pension funds in many countries, driven in part in that case by sterner disclosure standards. Wealth managers, both front line and back office, and securities issuers, face a much better-informed and more wily client base than even a year ago. Regulations in this field have doubled in the past five years, says Bloomberg.

When the virus is vanquished, when we get back to the future, climate change (and its companion, biodiversity) will again come high on clients’ and regulators’ agendas. It will be the biggest risk for the coming decade; there will be no self-isolation; and we must act in advance of the real problems emerging. A colourful cast of characters would have us believe the climate threat is fake news. The chemistry, and other science, says otherwise: humankind’s dominion over Earth is as great as the forces of nature, and our use of this power has opened up a new geological epoch – the Anthropocene.

The finance sector has much to offer, exploiting its power and leverage, and there is great profit to be made by agile players. Sir Roger Gifford, banker and former Lord Mayor of the City of London, is a great cheerleader for responsibility in finance. In a statement on the Green Finance Institute’s (GFI) website he says,

“It is critical that financial markets and policymakers collaborate to create the solutions to move the global economy towards a more sustainable future.” And, while as chair of GFI he passionately believes that “bankers can save the world” (from a joint CISI, Chartered Banker Institute, University of Edinburgh Business School event in February 2019), his eyes are wide open to the commercial opportunities here for the financial world’s best and brightest.

But actions are overdue. Finance needs to bridge the understanding gap, avoid preaching to the converted, stop boxing ‘responsible finance’ as an alternative, rather than mainstream. We need to get back to basics, to develop clear responses to market and regulatory demands, rather than fluff up the ‘green’ marketing.

And data needs to be coordinated to provide relevant information to investors, particularly institutions and ultra-high-net-worth private capital owners. There is too much fragmentation.

Almost all wealth managers globally put wealth transfer among their main concerns, according to a recent global survey of the sector by Refinitiv. Consequently, the best wealth managers are focusing much effort on the next

generation, which takes the climate threat seriously. (Many grandparents, keen to be ‘good ancestors’ to their grandchildren, are no slouches when it comes to querying responsible credentials.) Most big firms have revised their client segmentation models to take those shifts into account. Citigroup’s chief European economist, Arnaud Marès, quoted in *The Telegraph* (29 April 2020), believes that the psychological and social shock of Covid-19 will accelerate the way people quantify the climate threat: “The pandemic is in effect the first systemic ecological crisis in modern times, with immediately visible and profound economic cost.”

Following the First World War, the victors planned “a country fit for our heroes to live in”. A century later, after this invisible enemy has been seen off, we want “a planet fit for our grandchildren to live on”. ●

// WHEN WE GET BACK TO THE FUTURE, CLIMATE CHANGE WILL COME HIGH ON REGULATORS’ AGENDAS //

AROUND THE GLOBE

The CISI's international network of offices looks after circa 44,000 members worldwide

80%

of exam candidates passed our level 6 Certificate in Advanced Financial Planning narrative exam, sat in spring 2020

UNITED KINGDOM

Chief executive officer: Simon Culhane, Chartered FCSI



The UK's community of CERTIFIED FINANCIAL PLANNER™ professionals has come together to offer financial guidance pro bono in a series of money guides for the consumer, published on our CISI Wayfinder website.

The guides contain tips from our CFP™ professional members on managing finances during this uncertain and challenging time. They have been produced to help all consumers, including those who are employed, self-employed, and small business owners, financially cope with one of the most difficult periods they are ever likely to navigate for themselves and their families.

The guides are available free for all to download.

Financial guide for the employed: cisi.org/c19fp

Financial guide for the self-employed and small businesses: cisi.org/c19fpbusiness

GIBRALTAR

Senior international manager: Karolina Pajor



Alvaro López Lería, legal and compliance officer, Altarius Capital; Mary Boyd ACSI, group head of risk at Blacktower Financial Management (International), NAC vice president; Michelle Walsh, head of compliance, risk and regtech at Ince Gibraltar

On 11 March we announced the launch of our National Advisory Council (NAC) for Gibraltar. The council will support CISI membership in the region and steer our activities in developing professional standards across its finance sector.

The NAC president is Ian Woods, Chartered MCSI of Bank J. Safra Sarasin (Gibraltar). Three of the four NAC members are pictured above. The other NAC member, Tyrone Vinet, policy and risk manager at Turicum Private Bank, is not shown.

The CISI has been working with the Gibraltarian financial services community since 2010. In 2018 the Gibraltar Financial Services Commission confirmed the CISI level 4 Investment Advice Diploma compliant for advisers to meet the ESMA knowledge and competence guidelines.

For further information on the CISI programme in Gibraltar contact karolina.pajor@cisi.org

KENYA

Senior international manager: Lisa Elo



Mathew Sirma, director, management development center, KSMS; Kimacia Gitau ACSI, CISI East Africa region representative; Dr Joshua Kimoro, director, KSMS; John Kihoro, sales, Ardipiko; Irene Tuda, procurement services, KSMS

On 3 March we signed a memorandum of understanding (MoU) with the Kenya School of Monetary Studies (KSMS), aimed at enhancing professional standards in the area of credit risk management.

KSMS will be offering training for Fundamentals of Credit Risk Management, a stand-alone qualification that has been developed specifically for the Kenyan market in partnership with the Chartered Banker Institute and Financial Sector Deepening Africa, and endorsed by Kenya Bankers Association.

KSMS is fully owned by the Central Bank of Kenya and the Ministry of Finance and is mandated to carry out capacity building for sound management in the financial sector.

TANZANIA

Senior international manager: Lisa Elo

In May we signed an MoU with the Tanzania Institute of Bankers (TIOB), with the aim of advancing professional development in the Tanzania banking sector. The following CISI qualifications will be offered to TIOB students and members: International Certificate in Wealth & Investment Management; Global Financial Compliance; Risk in Financial Services; Operational Risk; Managing Operational Risk in Financial Institutions.

Candidates will also receive 12 months' CISI student membership.

Damas Mugashe, TIOB director of finance and business development (pictured) said: "Running joint professional

programs membership will benefit both Institutes by bringing international professionally recognised accredited programs to its members in Tanzania."

TIOB is a member of the Alliance of African Institutes of Bankers. Other countries in the East African region are in the process of establishing their Institutes and will subsequently join this regional cooperation.

TIOB has 8,000 current individual members and serves more than 50 corporate members.



500+
learning resources in our virtual event programme to support members' CPD requirements, including CISI TV videos and online modules

THE PHILIPPINES

Regional head, CISI Asia Pacific: Andrella Guzman-Sandejas



On 18 May we announced that we have been formally accredited by the Anti-Money Laundering Council (AMLC) of the Philippines to offer an elearning and training programme that is written to the AMLC's exacting standards.

Our online cost-effective anti-money laundering and counter-terrorism financing (AML/CTF) professional assessment module comprises an elearning workshop and test, successful completion of which provides the AMLC with a unified record of compliance. Full access to this thorough, international, gold-standard assessment tool is available nationwide.

Mel Georgie B. Racela, executive director of the AMLC Secretariat, said: "We are always pleased to have partners in building AML/CTF capacity among our local stakeholders to ultimately eradicate money laundering and terrorism financing in the Philippines."

Online registration and assessment is now available.

For further information on how to access the AML/CTF modules, contact asiapacific.office@cisi.org.

DUBAI

Regional director Middle East: Matthew Cowan, Chartered MCSI



In May we announced a partnership with the Academy of the Dubai International Financial Centre (DIFC) to deliver internationally recognised continuing professional development (CPD) programmes through workshops and training sessions, aimed at building current knowledge and skills amongst professionals working at firms in the DIFC. This will enable members to comply with a recent CPD mandate by the Dubai Financial Services Authority and provide professionals in the country with a full range of world-class education choices.

The partnership includes regular seminars and workshops at the Academy, involving well-known speakers and trainers presenting the latest insights on critical topics.

CISI Middle East head Matthew Cowan said, "We are keen to achieve our common goal of taking the UAE's financial services sector to new heights through upskilling practitioners by way of this partnership."

Alya Hussein Al Zarouni, executive vice president of operations at the DIFC, said that through the partnership "we are putting the spotlight on CPD, an essential part of any profession but especially financial services, in order to ensure UAE residents and firms receive trustworthy and quality service from practitioners."

CISI AND INVESTMENT20/20 HELPING YOUNG PEOPLE GAIN EMPLOYABILITY SKILLS



Monday 24 February: CISI students attending a networking lunch at Guildhall, hosted by Deputy Keith Bottomley

For the past three years, we have partnered with the City of London Corporation to deliver the level 2 CISI Fundamentals of Financial Services qualification to sixth-form students studying at different London schools. The initiative aims to enable young people to gain a competitive edge when looking to start a career in financial services.

Those who completed the qualification in 2019 are now participating in the award-winning Think Investments programme, offered by Investment20/20.

Here, students develop the employability skills that investment management firms seek for their school-leaver, apprenticeship and graduate schemes. The hope is that a

number of these students will successfully apply for the roles that Investment20/20 partner firms offer.

In February, students in the first year of the programme enjoyed a networking lunch held at Guildhall in London, hosted by City of London Deputy Keith Bottomley. The students heard from financial services professionals from a range of disciplines and firms, which included Killik & Co, Santander, Citi, and Mitsui Bussan Commodities about how they began their careers in financial services.

We look forward to seeing how the students progress and develop during the next 18 months of the programme.

New chair of CISI Paraplanner Interest Group



Dan Atkinson APP Chartered MCSI, head of technical at EQ Investors, is the new chair of the Paraplanner Interest Group, having been a member of the group for four years. He takes over the role from Farida Hassanali CFP™ APP Chartered FCSI, financial planner at Paradigm Norton.

He has won several professional awards, including Money Marketing Best Paraplanner 2017, Professional Paraplanner Personality of the Year 2017, and IFP Paraplanner of the Year 2014. He recently passed the CISI level 6 Certificate in Advanced Financial Planning with distinction.

Dan said, "Together with the other committee members and the CISI team, we look forward to providing support and professional development opportunities to members, whatever their career path or position."

He contributes regularly to the financial planning trade press. Outside of work he is a deacon with his local church and married with a young daughter.

NEW PRESIDENT FOR THE CISI EAST MIDLANDS BRANCH



Andy Jervis CFP™ Chartered MCSI, chair and founder of Chesterton House Financial Planning, is the new president of our East Midlands branch. He takes over from David Spokes, Chartered FCSI, of Brewin Dolphin, who held the position for three years.

Andy was one of the first financial planners to qualify for the CFP certification in the area and has long experience in helping people to plan and organise their finances to be able to achieve their goals.

Andy has also served as Birmingham branch chair for the Institute of Financial Planning, so he brings valuable experience to his new role.

He is a Loughborough man, having been born a few miles from the town and, although his five children are all grown and independent, his six grandchildren help ensure that he has his hands full outside of work.

Andy said: "This is a brilliant time to be a financial planner, with strong and rising demand for advice and services from an ageing but increasingly wealthy population. The dramatic improvements in technology, changes in legislation and practice, and ever-developing client needs, make it essential for practitioners to be well-qualified, up-to-date and able to communicate expertly and clearly. The CISI is ideally placed to deliver training in these skills."

Virtual CPD Events Programme

July 2020

We've moved many of our CPD events into a new virtual programme so we can continue to help you meet your CPD requirements. Here are some of the live webcasts we have planned for you in July. You can click the event to be taken directly to the booking page.

For more live webcasts, visit cisi.org/events

All times are in BST (GMT+1). Event information is subject to change.

Contact our Customer Support team for any queries: CustomerSupport@cisi.org or +44 20 7645 0777.

Wednesday 1 July 9.30am
Risk Forum: Investment horizons 2020
Deepen your understanding of risk in the ever changing financial markets with a panel of senior sector experts

Thursday 2 July 2pm
Good conduct in FX
Understand the behaviour issues in the foreign exchange market and how this impacts the securities and investment sector

Thursday 2 July 3pm
Entrepreneurial thinking in the workplace
Find out how you can bring fresh ideas, approaches and techniques to help your business thrive

Tuesday 7 July 12pm Live from Ireland
CISI Ireland: Raising resilience through private markets
Explore whether private markets have a part to play in pension portfolios

Tuesday 7 July 2.30pm
Maximising your success through referrals
How can you identify the quickest path to more referrals and build productive partnerships?

Wednesday 8 July 12.30pm
US Qualified Intermediary regime: lessons for responsible officers
Experts share their extensive experience in supporting a US Qualified Intermediary to achieve compliance

Thursday 9 July 3pm
The next generation of progress
How are new digital technologies driving positive progress across a wide range of areas, from agriculture to healthcare?

Thursday 23 July 3.30pm
City of London Police: modern economic crime and fraud
How does the City of London Police want to develop its volunteers in this area?

Wednesday 15 July 3pm
An update from the Bank of England
Tune into an 'off the record' presentation of the current economic conditions and the outlook for the UK economy

Wednesday 29 July 5.30pm
Wealth Management Forum: A more sustainable decade ahead from cowboy to spaceman
How important are environmental, social and governance factors to investors?

Thursday 23 July 3.30pm
The economic backdrop and the longer-term implications
A former chief economist explains the factors affecting the markets

Tuesday 28 July 3pm
Investigating megatrends: longevity and its implications for Nigerian financial services
A look at the implications of an ageing population and its impact on financial services in Nigeria

Wednesday 29 July 5.30pm
Young Professionals Network: Communicate to get results
How can you communicate your messages loud and clear to get what you want and advance in your career?

“In the middle of difficulty lies opportunity”

Albert Einstein

Switch up your routine and challenge your brain by studying for a CISI exam
- from home and at your own pace.

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Find the one for you at cisi.org/qualificationsnavigator

2. Study online

CISI exam bookings include instant access to online learning materials as standard, enabling you to study remotely and flexibly.

Many of our Accredited Training Partners (ATPs) also offer virtual learning programmes for CISI exams.

3. Enhance your studies

Access a wealth of online member resources to complement your studies, including webcasts available both live and on demand via CISITV, the latest news via *The Review*, and 200 Professional Refresher elearning modules.

4. Sit your exam

Many of our test centres around the world are reopening to exam candidates with new safety procedures in place.

Find out more at cisi.org/testcentreprocedures
We are also developing a remote invigilation option.

CISI AGM 2020

This year's Annual General Meeting will be held on Thursday 8 October at the CISI head office, 3rd Floor, 20 Fenchurch Street, London EC3M 3BY, or by virtual means, from 10.30am to 11am.

A Member (MCSI) or Fellow (FCSI) of the Institute may be nominated for elected vacancies on the Board. Board members retiring by rotation may stand for re-election and the Board itself may sponsor candidates for any vacancies arising. Ideally, member nominees will have served on an Institute Committee or Professional Forum and they will be invited to meet with the Board Nominations Committee before going forward as a candidate for election.

Visit MyCISI or email AGM@cisi.org for a nomination form, ensuring you provide your membership number.

Details of how voting members can participate in the meeting will be confirmed in advance via MyCISI.

The closing date for nominations for Board membership is Friday 24 July 2020.

CORRECTION

In the regulatory section of the February 2020 edition, p.53, it says that the FCA has “imposed restrictions on whether retail investors can buy some products (such as binary options) and limited the sale of others to high-net-worth individuals or experienced clients, such as venture capital trusts” (VCTs), seemingly suggesting that the sale of VCTs is restricted.

The sale of VCTs has not been restricted. Rather, the FCA views them as illiquid and therefore high-risk investments and places a duty on advisers to ensure that they are suitable for the client.

We apologise for the lack of clarity.

QUICK QUIZ

The Review's quick quiz features questions from CISI Professional Refresher, an online learning tool. This popular product consists of more than 200 modules covering topics including anti-money laundering, the UK Bribery Act, information security and data protection. The answers are on page 49.

Which term is often treated synonymously with environmental, social and governance (ESG) and socially responsible investing (SRI)?

- A Green finance
- B Fossil divestment
- C Negative screening
- D Best-in-class investing

What is technical analysis?

- A Calculating mathematical statistics to predict past results
- B A guaranteed way of predicting future price movements
- C A framework in which traders study price movement
- D A framework in which traders study only downward price movement

What does the SMART acronym stand for?

- A Situational, mature, active, relatable, targeted
- B Specific, measurable, achievable, realistic, timely
- C Specific, meaningful, active, realistic, timely
- D Specific, measurable, active, realistic, targeted

Access to Professional Refresher is available on an annual licence basis. The full suite of modules is free to CISI members or £250 for non-members. If you or your firm would like to find out more, visit cisi.org/refresher or contact the CISI on +44 20 7645 0777.

Disciplinary sanctions

Mr Daljit Maker MCSI, 6 April 2020

Mr Maker notified the CISI that he had been subject to disciplinary action by his then employer and was requested to appear before a CISI Disciplinary Panel on 23 March 2020. Mr Maker was found to have breached a number of the principles contained within the CISI Code of Conduct in relation to his dealings with a specific client and was also found to be in breach of 16.1(a) and 16.1(d) of the CISI Membership Regulations (cisi.org/regulations):

Mr Maker received a severe reprimand that will remain on his record for 12 months and must also complete the CISI's IntegrityMatters test within a six-month period.

Chartered FCSI, 16 April 2020

A Chartered Fellow notified the CISI that they had been subject to disciplinary action by their employer and was invited to appear before a Disciplinary Panel on 1 April 2020. The member was found to be in contravention of several principles within the CISI

Code of Conduct, including the upholding of personal and professional standards at all times. The Disciplinary Panel also found the member to be in breach of 16.1(a) and 16.1(d) of the CISI Membership Regulations (cisi.org/regulations):

The member received a severe reprimand that will remain on their record for six months, during which time their Chartered status will also be suspended. The member must also complete the CISI's IntegrityMatters test within six months.

Disciplinary rules: important notice
CISI members agree to abide by the Membership Regulations. An important aspect of this is the obligation to promptly inform the CISI (by emailing standards@cisi.org) of any matter which may impact your suitability to remain a member. Failing to do so may be considered an aggravating factor in a disciplinary case.





Financial planning news

A snapshot of financial planning news and events, by Jacqueline Lockie CFP™ Chartered FCSI, CISI head of financial planning

FINANCIAL PLANNING FROM HOME

I hope you and your loved ones are all able to stay well in the coming months. CISI staff are now mostly working from home, and you will have seen regular communications from us about exam sittings as well as information about branch meeting cancellations and some filmed sessions with speakers instead.

There is lots of financial planning content on our platform. If you log into your MyCISI account you'll see a drop-down menu with the CISI categories listed. Select your chosen category to see a variety of content across all our channels, including digital articles on *The Review* platform, CISI TV videos as well as over 200 online Professional Refresher modules which give you an hour's structured CPD for each one. We are also releasing new CISI TV financial planning videos through the fortnightly ebulletins to the Financial Planning Forum, so look out for those (assuming you have your communication preferences in MyCISI set to receive them).

2020 CONFERENCES MOVING ONLINE



Our Financial Planning and Paraplanning conferences will be held online this year with delegates able to participate remotely. Both conferences will be spread out over two days allowing fellow professionals to join from other global locations. The format will be interactive and delegates will spend as much time talking to their peers about their professional practice as listening to others present.

Topics across both conferences will include technical content as

well as aspects of individual professional development and business development. We are pleased to be able to offer the same high-quality content and networking as had been planned in this new format and hope that it will enable even more of our members to join from the financial planning, paraplanning and planning-curious communities.

Members who have already booked a place on either conference will receive further information early in July.

cisi.org/events

CERTIFIED FINANCIAL PLANNER CERTIFICATION PATHWAY

Well done to all those who sat the level 6 Advanced Financial Planning exam in early March, and to the 80% who passed.

The next step for these individuals is for them to complete the final stage of the CFP pathway, a level 7 financial plan case study that candidates are able to request each quarter.

Now is a good time to take stock of where you are and where you want to be in the financial planning profession and which exams you feel you want to sit. If you have a little more free time now, why not think about embarking on the CFP pathway and studying for the next exam in September?

Full details are on our website at cisi.org/cfp.

ARE YOU A CFP PROFESSIONAL?

Consider giving something back to the financial planning profession we love by becoming a CFP certification case study assessor. Full information, training and support will be provided by the CISI. Please contact me in the first instance on jacqueline.lockie@cisi.org.

ACCREDITED FINANCIAL PLANNING FIRMS™ CONFERENCE

The AFPF conference was held in early March and was a fantastic day. We looked at the value proposition, discussing questions such as how to articulate the value you provide to your client, what a good client agreement looks like, and professional indemnity insurance, amongst others. The sessions were interactive and well received, with firms saying that they gained significant value from the conference. If you are not an AFPF, why not consider becoming one? If 50% of your directors are CFP professionals and you offer a full cashflow financial planning service to all clients who want one, then you might be eligible. Visit cisi.org/afpf if you are interested.

As always, I look forward to hearing from you if you have any queries. Please be sensible out there and I look forward to seeing you at an event soon.

IS YOUR CLIENT'S FINANCIAL JIGSAW MISSING A PIECE?



The cash deposits element of a client's portfolio is a topic that has until recently not been discussed enough in the financial advice sector, but has now come to the forefront.

Following the Retail Distribution Review and the growth in the holistic financial planning model, financial planners should no longer consider cash deposit savings as the last piece of their client's financial portfolio. It should instead be viewed as an integral part of the puzzle.

Clients now have higher expectations of their financial planner, including managing all their savings and investments, looking after all service aspects of their portfolios, and contacting providers on their behalf, to name a few.

To help financial planners manage this expectation, NS&I has launched a new

online service. This gives advice firms easier and faster access to view their clients' NS&I holdings, with onward benefit to the service that financial planners provide to their clients.

The service allows firms access to:

- valuations on all NS&I holdings
- their Premium Bonds prize history
- copies of clients' NS&I statements and other communications.

Since the launch of the service, over 550 firms have registered. This is encouraging, but there is good reason for more firms to register. This is because most firms will already have clients with NS&I products.

We expect that our online service will deliver a step change in our engagement with financial planning firms. Many planners already view NS&I as the default home for cash, due to our unique 100% security guarantee (backed by HM Treasury) for all funds, and our unique products, such as Premium Bonds.

To register with NS&I's new online service, visit nsandi-adviser.com/obtaining-client-information and make the most out of the secure, fast and easy access to your client's NS&I holdings.

CISI FINANCIAL PLANNING CORPORATE SUPPORTERS JUNE 2020

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WHAT A GLOBAL CRISIS MEANS FOR CONTRARIAN, BOTTOM-UP INVESTORS



The coronavirus crisis has dominated both news headlines and markets and has been touted as the biggest crisis the world has faced since the Great Depression. As fear has progressed to panic, contrarian investors, like us, are looking for opportunities in the eye of the storm.

Extreme market volatility is always unnerving. But turbulent times can create compelling investment opportunities if panic-selling has been indiscriminate and price declines for some stocks have been disproportionate to the impact on their long-term fundamentals. As bottom-up investors, that is what we spend our time researching and analysing.

For some companies, the short-term impact is clearly negative. For example, Honda Motor's profits were hurt by the closure of factories and car dealerships in China. But people in China will resume buying cars,

and factories will resume producing them – to say nothing of Honda's auto businesses elsewhere, its world-leading motorcycle business, its prudently profitable financing arm, or the cash on its balance sheet.

For other companies, such as NetEase which makes and operates online games in China, and its subsidiary Youdao that offers online education services, the financial impact may not be negative at all. The key is to focus on the relationship between market prices and company fundamentals, and on the long term rather than the next month or quarter.

At times when others are fearful, a long-term perspective is not just a bulwark against emotional decision-making, but a source of opportunity for contrarians looking in even the hated sectors, like airlines and hospitality today, for discounted companies that offer undiminished long-term value.



Designing your future in advance® with lifestyle financial planning

CRAIG CHAPMAN CFP™ CHARTERED MCSI, FOUNDER AND MANAGING DIRECTOR AT THE FUNDAMENTAL GROUP, EXPLAINS HOW THE FIRM ENABLES CLIENTS TO ALIGN THEIR WEALTH WITH PURPOSE

WHY DID YOU DECIDE TO BECOME ACCREDITED AND WHY SHOULD OTHERS SEEK TO DO SO?

There is no better way of confirming our ethics, processes and quality to the outside world than to become an Accredited Financial Planning Firm. It demonstrates that despite our size – we are a smaller boutique firm – the quality of our work is at the highest possible standard in the UK. Other firms should seek to do so as the criteria and requirements to become accredited ensure absolute best practice and demonstrate that true financial planning is being offered to clients.

WHAT SORT OF BUSINESS IS IT AND WHAT SERVICES DOES IT OFFER? WHAT'S YOUR USP?

We are a lifestyle financial planning business. We passionately believe in the power of financial planning and the good that it can do for many families.

We remain small on purpose. This is reflected in the clients we work with; it is very much about quality over quantity. Our trademarked slogan is **Designing your future in advance®**, which captures

beautifully what we are about. We don't rush in with solutions to immediate client problems but instead spend time discovering exactly what future our clients are aiming for and how best their wealth can support them.

Our service is focused on providing personal financial planning to business owners and their families. We have developed this specialism over the years and it is an area that I particularly enjoy. Business families have unique requirements and it's impossible to separate 'the business' from 'the family'.

We are unique in that my partner Kasia is also a life coach, and her skills and expertise are a great asset to the firm and lead to really meaningful client conversations.

HOW DID YOU GET INTO FINANCIAL PLANNING?

I had a varied career prior to financial planning, with a background in engineering and motorsport. I joined the family business in 2009 with zero experience, learning on the job while working my way through exams. In the first few years, the business was very much a transactional service with a

// I TRY TO PRACTISE WHAT I PREACH TO CLIENTS, SO I LEAVE PLENTY OF TIME EACH DAY TO WALK MY DOG, BE OUTDOORS AND KEEP FIT //

lesser focus on financial planning. In 2013, I was introduced to Paul Armson, founder of an online training programme for financial advisers, who changed my perception of what financial planning was about and the immense good that it could create in clients' lives. Discovering that my newfound passion for real financial planning wasn't going to fit in with the family firm, I started out on my own from scratch in late 2014. I gained my CERTIFIED FINANCIAL PLANNER™ certification in 2017 and have kept the momentum going ever since.

WHAT'S THE BEST THING ABOUT BEING AT A FINANCIAL PLANNING FIRM?

Giving the gift of listening. Our profession allows individuals and families the space and time to share their deepest concerns and ambitions. Quality financial planners show a level of personal attention and empathy for clients rarely seen in providers of other products and services. It gives me great joy to know that our clients trust me and my team with their family's future and it is a privilege to be part of their lives.

WHAT ARE YOUR BIGGEST CONCERNS FOR YOUR CLIENTS OR THE FINANCIAL SERVICES SECTOR IN GENERAL?

For my clients, my concerns are always about their level of preparedness for the future. Do they really appreciate that they will have to fund a minimum three-decade retirement, and that the cost of their lifestyle beyond work is most likely to be a lot more than they anticipate?

We discuss these concerns at our regular forward-planning meetings, where we aim to get clients back on track with a plan that ensures their future lifestyle requirements are met where possible.

For the financial services sector in general I have many concerns. I believe that the sector as it stands is a ticking time bomb. Many firms have built businesses based on outdated practices, which were tidied up somewhat for the Retail Distribution Review, but are still not providing a service valuable enough to justify the percentage of asset under management fees that are being charged. I don't think this is going unnoticed and anyone still in this world is very much on borrowed time.

Overall there is still far too much focus on the tools used, the products, the investments, and the funds. It is difficult still for advisers and firms who have a

desire to break free from this world and deliver genuine financial planning with no conflicts of interest. Financial planners are being pulled in many directions by the financial services sector, product providers and the regulator.

WHAT IMPACT HAS REGULATORY CHANGE HAD ON YOUR BUSINESS OVER THE PAST FEW YEARS?

Many changes have had a positive impact. We introduced call recording in preparation for the revised Markets in Financial Instruments Directive, and I am also supportive of the recent changes to annual suitability reporting – this is another opportunity for good firms to reconfirm what they are doing and remind clients of this.

WHAT DO YOU LIKE ABOUT THE CISI?

It is a professional and progressive organisation that is always looking for ways to evolve and add value for its members. It is supportive of financial planning and it balances the interests of the financial planning community and the sector well.

WERE YOU INVOLVED IN CISI FINANCIAL PLANNING WEEK 2019? IF SO, WHAT DID YOU DO?

Yes, we offered complimentary 'surgery' type calls for anyone new to financial planning, which resulted in follow-up calls and relationships being built. I still think we can do more as a profession to raise awareness of what we do, and it shouldn't just be limited to one week per year.

WHAT DOES A TYPICAL DAY LOOK LIKE?

Overall, I'm not one for routine, but of course there needs to be structure. I schedule meetings for the morning when possible, as I believe both myself and my clients are fresher. I also try to limit financial planning meetings to two per day as it isn't possible to listen intently for any longer.

We group client meetings together, in particular our review and forward-planning meetings, which we conduct twice a year. This allows me to work on other key projects and develop the business further.

I split my time between Aberdeen and London and have clients in both locations.

I try to practise what I preach to clients, so I leave plenty of time each day to walk my dog, be outdoors and keep fit. This is

especially important during the working week; it shouldn't just be confined to evenings and weekends.

WHAT ARE YOUR KEY TIPS FOR OTHER PLANNERS?

Take inspiration from others but don't copy. Be authentic and be yourself. Clients will appreciate it.

Find out what type of work you enjoy and who you enjoy serving – then have a laser focus on this.

Don't underestimate the benefit of continuing education and self-development – don't try to run before you can walk.

Try not to take life too seriously. It's easy to deliver financial planning and make it 'heavy' for both planner and client. Be confident in what you do and have fun with it.

Keep the focus on your client and constantly think of ways in which you can serve them and add value. ●



CRAIG CHAPMAN
CFP™ CHARTERED
MCSI

Craig is an experienced financial planner and a Chartered Wealth

Manager. He is known for his intrinsic ability to see past the obvious, translating the contents of a complex conversation into a plan that will achieve the desired outcome.

On behalf of the CISI, Craig assesses and marks financial plans submitted by CFP certification candidates.

Craig recently joined the Family Firm Institute, an association for professionals who serve family enterprises. He is also an associate member of the Society of Trust and Estate Practitioners (STEP). By July 2020 he will have completed an advanced certificate in Family Business Advising awarded by STEP.

He lives with his partner Kasia and their cocker spaniel, Coco. When not working, Craig spends his time mountaineering, mountain biking and playing guitar. His lifelong passion is motorsport, in which he has previously competed at international level.

Searching for the lost



JOHN YUE, CHARTERED MCS1, REGULARLY STEPS OUTSIDE HIS COMFORT ZONE TO HELP LOCATE VULNERABLE MISSING PERSONS. BY **LORA BENSON** MCIPR, CISI HEAD OF MEDIA

Research by the Office for National Statistics shows that construction workers are over three times more likely to take their own lives compared to the national average. It's a statistic that John Yue, Chartered MCS1, finance director at Quilter Cheviot Investment Management, is grimly familiar with as a frontline volunteer with London Search & Rescue (LONSAR).

LONSAR is a registered charity and is run entirely by volunteers. It operates what is known as a Lowland Rescue Service, covering the territory between mountains and seas. Lowland Rescue teams have been around for years, with almost 2,000 volunteers across the UK and 35 search and rescue units covering most counties, working in close symbiosis with the emergency services. LONSAR is the newest addition to the Lowland Rescue network, established at the end of 2017 to assist the Metropolitan Police. The team became fully operational in November 2018.

John became involved in early 2019 after stumbling across the LONSAR website while planning a holiday. "I had been looking for something that would take me outside my usual professional environment," he recalls. "I signed up for an introductory meeting and by June 2019, after five months of classroom-based training and practical sessions and a simulated search, I passed the initial assessment and went on probation as a search technician, which is the first stage of qualification for operational personnel, and, as the more 'seasoned' members of the team would say, the 'bag carrier'!"

John received a red alert call-out recently when his family was visiting, just as they



John and fellow LONSAR volunteers on a training exercise

were sitting down to eat. "It was a potential suicide case. Following a swift drive across London, police briefed the team that their missing person was a builder who'd abandoned his van nearby. He'd left his telephone, wallet and rings at home – typical behaviours in the case of a suicidal person. We were out searching for five hours and were told to stand down at about 2.30am. I got home at 4am and was up at 7am to do my day job. The search continued for several more days and everyone was fearing the worst, but thankfully he eventually returned home."

Of the five call-outs John has been on since becoming operational, three have had the desired outcomes. One person was located by a dog team, a 12-year-old child with Down's syndrome was found by a search team, and a patient with dementia turned up at a hospital on the opposite side of London to where they had gone missing.

In the past, those with Alzheimer's disease and dementia used to be the number one category for a missing person. But this is being significantly overtaken by what is known as 'despondent' mental health cases, including suicidal people.

"It still amazes me that services such as Lowland Rescue, the Air Ambulance and the RNLI are self-funded charities. The broader issue is that with more funding in the area of health, social care, and mental health services, there would be less need for the involvement of the emergency responder and Lowland Rescue units."

LONSAR has a broad and diverse range of volunteers, including teachers, NHS medical staff, a taxi driver, an actor, and even police and ex-military, plus a few current serving reservists. Many volunteers are retirees from various walks of life.

A typical foot team comprises four people: team leader, medical first responder, navigator, and radio operator. "Training also includes crime scene management and missing persons' behaviour," says John.

John has been volunteering with LONSAR for six months and describes his most difficult search, so far, as negotiating water-logged woodlands on Halloween, looking for a despondent and potential suicide case. "I haven't experienced the range of challenging situations many of my colleagues have encountered. Many have been involved in heartbreaking situations and yet continue to help others. They're inspiring and great to work with."

Transferable skills between John's role at Quilter Cheviot and his volunteering include "operational/project planning, briefing and debriefing, risk assessment and post-operations review so that people know exactly what the goals and targets are".

John concludes: "It's like having a second job – you need an understanding family. My employers are incredibly supportive to individuals who volunteer and are quite vocal about staff wellbeing and mental health awareness issues." ●



Contact jane.playdon@cisi.org if you have a hobby you think will interest other CISI members. You will receive a £25 voucher if we publish your story.

For a life-threatening mental health emergency, contact the emergency services of the country you're in. In the UK, dial 999.

www.londonsar.com

LONDONSARUK

London Search & Rescue

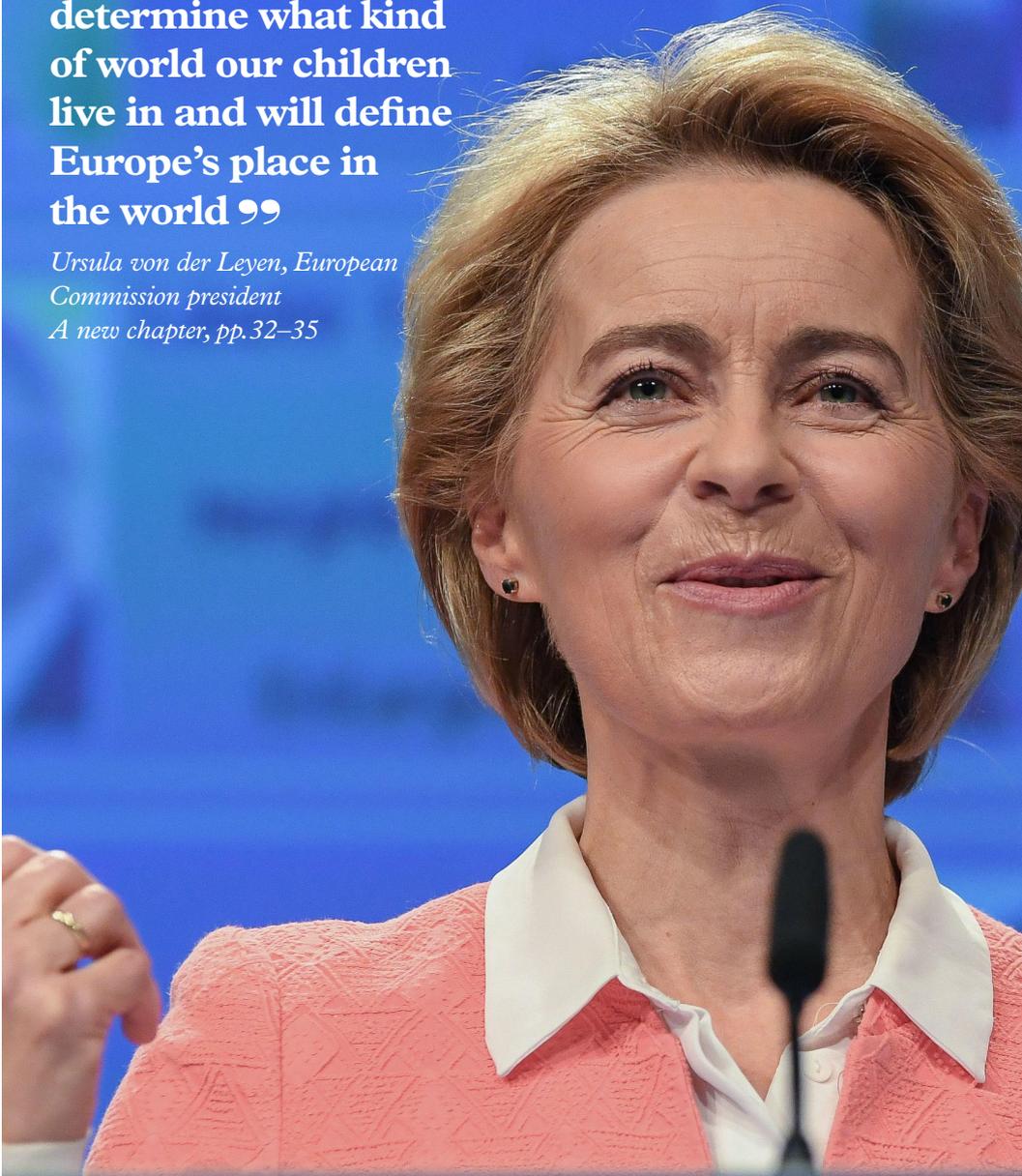
LONSARUK

londonsearchandrescue

“

What we do now will determine what kind of world our children live in and will define Europe's place in the world”

*Ursula von der Leyen, European Commission president
A new chapter, pp.32–35*



global insights

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Global blended families

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Financial inclusion and tech

PHOTOGRAPH: XINHUA/ALAMY



FIRST PERSON

A creative vision

Anthony Hilton
FCSI(Hon)

EDUCATION NEEDS TO CHANGE ITS APPROACH IF THE UK IS TO REAP THE BENEFITS OF CREATIVITY

“ At a conference in Prague a couple of years ago, one of the speakers startled his audience of largely middle-aged men by saying, “Knowledge is so 20th century; what we need now is imagination. Google will bring you most of what is known, but Google will not bring you what is not there yet.”

Once they got over their initial shock, the audience realised the speaker had a point. Since the days of the British Empire, schools have taught as much knowledge as teachers can usefully cram into their pupils. Universities have followed suit. They have encouraged students to read more and think for themselves but everything has been knowledge-based – and is even more so now, given many universities are under pressure to become degree factories, churning out only what is in the standard textbooks.

The chief economist of the Bank of England, Andy Haldane, touched on this in a speech in 2018 titled ‘The creative economy’. He said that knowledge and imagination are two different things: “To have knowledge is to know about things that exist. To have imagination is to conceive of things that don’t yet exist. Knowledge is vital for school exams and pub quizzes. Imagination is vital for ideas and innovation.”

Knowledge inculcated by universities served its purpose for work in management and administration when there were rule books that had to be obeyed, and when there were not, then people had the background to manage anyway. It worked elsewhere too. As the economy developed, it did so in a conventional way. Most people were happy with doing what they had to do. Even when new machines replaced the old, most knew roughly how these machines would work, even if they did not always like the results.

But the world has changed. The First Industrial Revolution was built on the steam engine, the spinning jenny and the water frame from the late 18th century. The Second Industrial Revolution was born of sanitation, electricity and the combustion engine around the 1880s. The third turning point was the advent of computer power in the 1960s. All these revolutions, even computers, took a long time to get established, but they then had longevity.

The Fourth Industrial Revolution – with its trappings such as the iPhone, machine learning, big data, biotechnologies and artificial intelligence – is now upon us, but it is moving much faster than anything seen before. People – and companies – will find it hard to adjust. Some

academics and several respected consultancy firms, including McKinsey and PwC, say that millions of jobs will be lost because of these innovations. They hope new jobs will be created to make up for the old. But if these new jobs are to come about, people will not need knowledge of the old ways of doing things. They will need the imagination to envisage and work with the new.

Haldane suggests that, between now and 2030, demand for creativity as a key skill could increase by between 30% and 40%. Nesta, a UK-based global innovation foundation, puts the number of people currently in creative professions at between a fifth and a quarter, but Haldane estimates that by 2030 this could increase to more than a third.

Education needs to change if Britain is to reap the benefits. The knowledge-based factories producing knowledge-based students will have to go. Instead of producing people who can get from A to Z, we want people who can navigate anywhere. Universities need to get away from being

“ Creative breakthroughs are often a result of innovators straddling disciplines ”

narrowly subject-based, because creative breakthroughs are often a result of innovators straddling disciplines. Equally, Haldane says, universities should recognise subjects like creativity and digital literacy, emotional intelligence and empathy, entrepreneurship and design. In short, what is needed is a creative workforce producing creative economies.

We need to realise too that imagination and creativity can be taught, at least in part. Creativity rarely constitutes a random flash of inspiration. Instead, it is about creating the right environment for lightning to strike in the first place. We don’t necessarily need an apple to fall on the head of a genius, but we do require an environment where non-geniuses can discover things too. But schools (and increasingly universities) tend to teach creativity out of children, not into them.

Unfortunately, we do not seem to recognise this. People say the UK’s school system needs improvement – and as 16% of adults in England have very poor literacy skills, according to the National Literacy Trust, they have a point. But politicians and others tend to look back with rose-tinted spectacles at the days when they were taught. Their changes, therefore, try to make today’s schools an idealised version of what they had then. This is wrong. We need to look forward, not back. ●

ILLUSTRATION: PADDY MILLS/SYNERGY



Progressing with purpose

PURPOSE CAN HELP FIRMS ACHIEVE LONG-TERM GROWTH AND SUSTAINABLE SUCCESS BEYOND A SOLE FOCUS ON PROFITS.

ALEXANDER GARRETT AND
WILLIAM MONROE REPORT ON
WHY PURPOSE IS SET TO
TAKE CENTRE STAGE

ILLUSTRATIONS: HITANDRUNMEDIA

Barclays sums it up as “creating opportunities to rise”. For Lloyds Banking Group it’s about “helping Britain prosper”. BlackRock wants “to help more and more people invest in their financial wellbeing”. And for Peruvian bank Caja Rural de Ahorro y Crédito Los Andes, in the words of founder and chair Rosanna Ramos-Velita, quoted in chapter two of *Rehumanizing leadership: putting purpose back into business* (published March 2020), the aspiration is nothing less than “to eradicate poverty”.

What each of these financial services firms is talking about is their ‘purpose’, a term that has gained traction in the corporate lexicon.

Purpose in context

The UK’s Financial Reporting Council (FRC) and the FCA have both introduced purpose into their supervision regimes in the past two years.

In 2018, the FRC’s UK Corporate Governance Code was revised to make establishing corporate purpose a board responsibility. In 2019, the FCA introduced culture and purpose as key components of its Firm Assessment Model, which is at the heart of its approach to supervising some 58,000 firms. In its final April 2019 report on its *Approach to supervision*, the FCA says: “We look at the purpose of a firm to understand what it is trying to achieve in practice, not just what is written in its mission statement. A strong understanding of firms’ business models allows [us] to identify where there is poor alignment between firms’ profit incentive and the interests of consumers and markets functioning well.” And in its Firm Assessment Model the regulator asks: “How effective is the firm’s purpose in reducing the potential harm arising from the firm’s business model?”

In its *Business plan 2019/2020* (p.13), the FCA identifies purpose as one of four drivers of behaviour in a healthy business culture, alongside leadership, reward and managing people, and governance. In France, too, the PACTE (Action Plan for Business Growth and Transformation) law made a provision similar to the UK Corporate Governance Code during 2019.

But the growing emphasis on purpose is also the consequence of a shift in outlook within the business

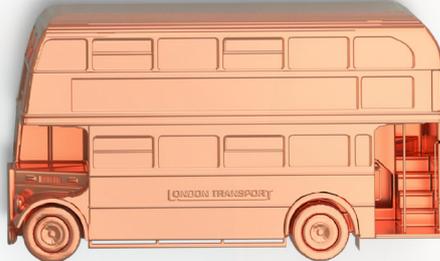
community itself. In May 2019, Quartz Insights and WE published *Leading with purpose in an age defined by it*, a global study based on a survey of 254 management and C-suite leaders encompassing a range of sectors. Some 73% of respondents believe purpose leadership will become as important as financial performance.

// WHAT’S REALLY DRIVEN THIS IS THE SENSE THAT THERE’S GOT TO BE MORE TO LIFE THAN JUST MAKING MONEY //

In August 2019, the Business Roundtable – an organisation comprising CEOs of leading corporations in the US – redefined the purpose of a corporation from serving shareholders to serving all stakeholders, including customers, employers, communities and suppliers. In the same year, the *Financial Times* produced a series of articles on putting purpose before profit, and a City law firm, Bates Wells, published a draft Company Purpose (Amendment) Bill, designed to replace s172 of the UK Companies Act 2006, which sets out that the default purpose of companies is not simply to benefit shareholders. Rather, the Bill is based on the premise that businesses should adopt a ‘triple bottom line’ operational approach that will benefit wider society and the environment, rather than just an organisation’s shareholders.

It would be easy to point the finger at the 2007–2008 financial crisis, or an even more recent so-called ‘crisis in capitalism’ – whereby large companies become ever more powerful at the expense of workers – as further triggers for the new focus on purpose. Mark Goyder, founder of Tomorrow’s Company – a London-based think tank that set out to enable business to become a force for good – and co-author of a recently published book called *Entrusted: stewardship for responsible wealth creation*, acknowledges that the financial crisis has prompted renewed attention with regard to purpose, but he suggests a deeper and more fundamental explanation for the current focus: “What’s really driven this is the search for meaning and the sense that there’s got to be more to life than just making money.”

Mark took part in an FCA-instigated series of round table working groups between June and October 2019 to explore the business case for being purposeful, looking at how it can improve culture and success, as well as



the barriers and how these could be overcome. The round tables covered seven financial services sub-sectors: retail banking, wholesale financial markets, general insurance, retail lending, pensions and retirement income, retail investment, and investment management.

Results of these discussions fed into essays written by participants – and courtesy of contributions from academics and others – and published in an FCA discussion paper (DP20/1) in March 2020, titled *Transforming culture in financial services: driving purposeful cultures*. In the introduction, the FCA says that the “purpose of a firm sits at the heart of its business model, strategy and culture” – a point echoed in many of the essays. CISI CEO Simon Culhane, Chartered FCSI, who chaired the retail investment round table working group, co-wrote the retail investment sector essay in DP20/1 with Mark and Quilter CEO Paul Feeney.

The essay, titled ‘Restoring trust – the case for the financial services industry to rethink its purpose’, proposes a common statement of purpose for the financial services sector that would commit every signatory to a number of shared values, including dealing with customers fairly and ethically, investing in employees, and supporting communities and the environment – as well as generating long-term value for shareholders. It says: “Imagine how powerful it would be if, while acknowledging that every company will define its purpose in its own unique way, every firm publicly accepted that it had a purpose that went beyond an exclusive commitment to shareholder value? And having made that statement, every firm committed to living up to a common approach to the principle of how a firm should operate? Think of it as a recalibration of capitalism.”

Charis Williams, research manager at the CISI, which ran two streams as part of the FCA culture programme, says one of the key points that came out in the discussions with practitioners is the importance of purpose being understood at every level.

“The clear message from practitioners is that, whether you are a senior member of the board or a junior member of frontline staff,

purpose should be equally important to you,” Charis says. “Frontline staff are particularly responsible for making lending decisions to customers. If they are aware of their organisation’s purpose, they are more likely to take ownership of their decisions and only lend sensible amounts in appropriate ways.”

Purpose and the Covid-19 crisis

The Covid-19 pandemic has had a severe impact on economic activity, with the International Monetary Fund predicting that the global economy will contract by 3% in 2020.

A clearly defined sense of purpose could provide an invaluable framework for companies in the months and years ahead, as the sector seeks to absorb the shockwaves. Handelsbanken, another organisation that authored an essay in DP20/1, titled ‘When what + how = why’, is an example of a firm with a ‘top-to-bottom’ purposeful model. The model, which was implemented five decades ago, aims to embed shared purpose throughout the bank by aligning its business model with two fundamental values: trust in the individual and taking the long-term view.

Tracey Davidson, Chartered MCSI, deputy CEO of Handelsbanken in the UK and a CISI Board member says: “Handelsbanken was one of very few European banks not to request or receive any taxpayer support during the global financial crisis. This is because we stuck to our values-led model during the years leading up to the crash, just as we have done ever since. We understand our purpose: why and how we should serve each other, our customers and communities.” She continues: “In our experience, having a deep-rooted understanding of the role we play for our customers and colleagues is particularly valuable in challenging times, such as the current [Covid-19] crisis. It helps guide sound decision-making all over the organisation. But you also need the best conditions to be able to make these decisions together. That’s why it’s so important that our core values translate directly into our everyday operating model, with no friction or contradictions.”

The FCA says of purpose

“The purpose of a firm sits at the heart of its business model, strategy and culture”

Source: FCA discussion paper 20/1: *Transforming culture in financial services*

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>> With the world in the grip of a pandemic, actions in the financial services sector will speak louder than words. CISI chair Michael Cole-Fontayn MCSI, who chaired the wholesale financial markets round table working group – see quotes from participants on pages 26 to 27 – says: “All stakeholders are judging every aspect of corporate behaviour in a heightened way during this pandemic and determining how companies are serving society.” Purposeful firms such as BlackRock, which contributed an essay in DP20/1 titled ‘Purpose: at the heart of profitability’, are issuing strong responses. BlackRock has committed US\$50m of funding to global relief efforts, with a particular focus on communities where it operates, while hundreds of asset management companies have signed up to the Investor Statement on Coronavirus Response, an initiative by the Interfaith Center on Corporate Responsibility that aims to promote the need for businesses to adequately protect their workforces and communities.

// STAKEHOLDERS ARE JUDGING EVERY ASPECT OF CORPORATE BEHAVIOUR IN A HEIGHTENED WAY DURING THIS PANDEMIC //

Notably, the FCA has announced its intention to double down on its focus on purpose in its *Business Plan 2020/21*, which was published on 7 April 2020. Despite an inevitable revision of immediate priorities, the report makes it clear that work to address corporate culture will continue in the areas that the regulator classifies as key cultural drivers in organisations. The FCA says that it “will continue to focus on the four key culture drivers in firms – purpose, leadership, approach to rewarding and managing people, and governance – and their effectiveness in reducing the potential harm from firms’ business models and strategies.”

Simon Culhane notes that many purposeful firms already have a model that will enable them to “weather disruptions such as those caused by the pandemic”. He continues: “Those firms that have previously focused entirely on profit will, by definition, have hitherto prioritised short-term gains. This is likely to have left them ill-equipped to deal with the longer-term challenges posed by the pandemic. By contrast, those firms with an established broader purpose aimed at benefiting all stakeholders – from their suppliers to their employees – will often be better placed to weather shocks and, crucially, to share value throughout the supply chain.”

Purpose and corporate culture

The idea of corporate purpose stems from the recognition that companies that enjoy long-term success are driven by more than simply generating profits for shareholders. There’s no single definition of what is meant by corporate purpose, and it’s easy to confuse with all those other high-minded company statements, such as mission, vision and values. Alex Edmans, professor of finance at London Business School and author of a new book, *Grow the pie: how great companies deliver both purpose and profit*, says: “The way I would define it is: how is the world a better place by your company being here?” Purpose is about the company’s core business – does it generate profit as a result of serving society?

Jonathan Davidson, director of supervision – retail and authorisations at the FCA, says, “We would define purpose as ‘why you come to work’, the ultimate motivator.” In any case, purpose is taken as shorthand for ‘purpose beyond profit’, since nobody doubts that profits will always be a key driver, and any company needs to make a profit to survive (a point made in a previous CISI City View article on the topic – see [cisi.org/purpose-profit](https://www.cisi.org/purpose-profit)). What the focus on purpose recognises is that making a profit is not, or should not be, the sole driving force in an organisation. For Mark Goyder, “the important bit is purpose beyond profit, the purpose that gives people who work for the business a sense of meaning, of adding human value.”

Purpose beyond profit

Jonathan explains why the FCA is choosing to place increased emphasis on purpose. “We did a lot of reflection and research on the main drivers of harm in firms,” he says. “Typically it’s either that they have a business model where there is a huge incentive to do something bad that gives poor outcomes – for example, making a lot of money by giving poor advice – or it is down to the culture and the behaviour of the individuals.”

Culture within every financial firm broadly fits into one of three categories, he says: those where firms set out to make money at any cost; those that are compliant but still overwhelmingly profit-driven; and those that are purposeful in a more inclusive way towards other stakeholders. “We are saying it is good for you as a firm if you are purposeful,”

Jonathan continues. “It will be healthy, profits will be sustainable, you won’t suddenly have some terrible regulatory



intervention, you will have a queue of people wanting to work for you, and customers who say they trust you and feel you are on their side.” The FCA won’t sanction firms that don’t show they are purposeful, he says, but it will play a significant part in risk-rating individual firms and the amount of supervisory attention they receive.

— We’ve already seen that purpose beyond profit has powerful traction in the US, with its adoption by the Business Roundtable, but it is also making waves elsewhere. In Sweden, start-up Doconomy offers a digital banking service where a consumer’s spending and savings are measured by their impact on the planet. The firm’s CEO and founder Nathalie Green says: “Our vision is to enable a sustainable lifestyle for all. By creating a global standard for measuring the impact of consumption, Doconomy wants to inspire change in behaviour and reduce unsustainable consumption and carbon emissions.” In order to be a sustainable company, it’s necessary to be profitable, says Nathalie. She adds: “For Doconomy it is important to show that we as a company and brand need to be a first mover and be taking responsibility for our planet.”

Italian insurance giant Generali is also backing up its statement on purpose – the firm declares on its website that its “purpose is to actively protect and enhance people’s lives” – with actions, having set up an Extraordinary International Fund on 13 March 2020 that will provide up to €100m of funding to help fight the Covid-19 pandemic. However, some international firms have



expressed the view that it is a struggle to have a common purpose across all parts of their business in all countries in which they operate. Tech companies such as Google, for example, have found it difficult to reconcile a purpose that involves universal access to information with state censorship in China.

As a result of the FCA initiative, the CISI is now reviewing its own purpose as an organisation and is in the process of holding a series of events with various stakeholders, including CISI staff, clients and members. The calendar of events has been paused in light of Covid-19, but is set to resume in the near future. “Our aim is to come up with a clear statement of purpose that will inform our future activities,” says Charis Williams.

There are good reasons why purpose should be an important priority for financial services firms. Jonathan says that “it is critically important because there is a huge amount of wellbeing tied up in financial services.” He continues: “If you’re being advised by an adviser, it can have a huge impact on your life. It’s important that it’s done in a purposeful, competent and professional way.”

Alex Edmans adds: “The financial sector comes under attack more than any other. But I do think it serves a great purpose. Financial services firms allow people to save for their retirement, and help them to plan for their future and their children’s future. Some of the world’s most purposeful companies might not be around if it weren’t for financiers who were willing to finance them.”

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CASE STUDY

George Latham, managing partner at WHEB Asset Management, explains how purpose is an essential part of the impact investor’s DNA



WHEB Asset Management was relaunched in 2012, with the intention of building a mission-driven business where a sense of

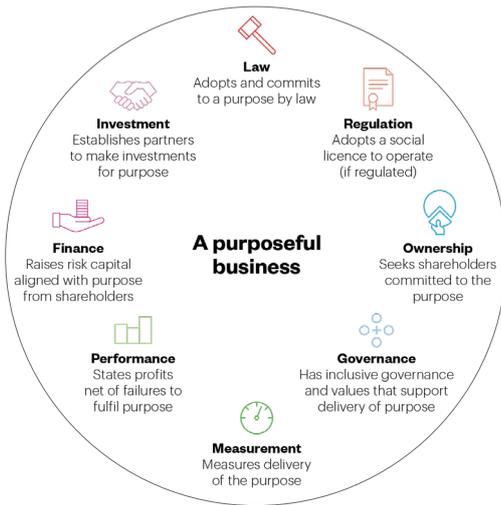
purpose, which sits at the core of the investment strategy, also runs throughout the whole organisation. When we first certified as a B Corporation in 2016, we realised that our mission was buried in a strategy document, gathering dust in a file. So we tore it up and started again, and the whole team co-wrote the new mission together, starting with post-it notes on the wall.

Although we’ve had new colleagues join since then, there is a sense that our mission is co-owned by all, rather than handed down from on high.

Internally, having a clear sense of our purpose helps guide us when making decisions in all market environments. People want to work for purposeful organisations, and so it helps us to attract and retain the most talented colleagues. It helps us build stronger relationships with our clients, which is supported by our focus on transparency and other ways we align our interests with those of our clients.

Our mission is to advance sustainability and create prosperity through positive impact investments. We start with our mission, which encapsulates our purpose, and then our governance, strategy and values flow from there. Because it is so key to both our investment strategy and our business philosophy, it underpins everything we do. We don’t believe there needs to be a conflict between having a mission and a sense of purpose and creating a profitable, successful and valuable business. Quite the reverse; we believe there can be a symbiotic and positive relationship between the two.

WHAT DOES A PURPOSEFUL BUSINESS LOOK LIKE?



Source: The British Academy, Principles for purposeful business

>> The finance sector, through its investment muscle, has a significant part to play in ensuring that purpose beyond profit is embraced across the corporate landscape. In his 2019 annual letter to CEOs, BlackRock’s CEO Larry Fink writes: “A company cannot achieve long-term profits without embracing purpose and considering the needs of a broad range of stakeholders. A pharmaceutical company that hikes prices ruthlessly, a mining company that short-changes safety, a bank that fails to respect its clients – these companies may maximise returns in the short term. But, as we have seen again and again, these actions that damage society will catch up with a company and destroy shareholder value. By contrast, a strong sense of purpose and a commitment to stakeholders helps a company connect more deeply to its customers and adjust to the changing demands of society. Ultimately, purpose is the engine of long-term profitability.”

The business case for purpose

Making a business case for purpose entails measuring aspects such as attracting staff, retention of employees and consumer trust – all of which can ultimately lead to greater profits. But, Alex says, the benefits may be hard to measure. Far more important is that it provides a clear framework on which to make decisions. He cites the example of French energy company ENGIE, which made a difficult decision to close a coal-fired



power plant in Australia, as it didn’t align with the firm’s future vision for sustainable energy. “Because it had a clear purpose to move towards a low-carbon economy, that helped it take that tough decision,” Alex says.

The *Global leadership forecast 2018* – a three-way collaboration between Development Dimensions International, The Conference Board and EY that includes data from 25,812 leaders and 2,547 HR professionals across 2,488 organisations – offers tangible data regarding a business case for purpose. The report reveals that purposeful companies – companies that actively put purpose into practice – outperform the market by 42% when it comes to financial performance. This is in contrast to companies that have a purpose statement, but don’t ‘walk the walk’. These companies merely perform at the mean of organisations, while companies without a purpose statement underperform by 42%.

// COMPANIES THAT ACTIVELY PUT PURPOSE INTO PRACTICE OUTPERFORM THE MARKET BY 42% WHEN IT COMES TO FINANCIAL PERFORMANCE //

The report also reveals that company performance is intrinsically linked to employee engagement with purpose. It finds that engagement levels are 12% higher and employees’ intent to stay is 14% higher among purposeful firms. Of the 1,500 global C-suite executives surveyed, 84% say that their business operates in an increasingly disrupted environment, and that’s not accounting for Covid-19-induced headwinds.

The report states that in such a world, employee buy-in “enables a purposeful organisation to respond more quickly and effectively when opportunities arise or danger threatens”. Agility in such scenarios is 50% higher than non-purposeful organisations. The report makes a clear case for purposeful companies amid the Covid-19 environment: firms can use purpose as a “North Star – a fixed point to help navigate through change and uncertainty”.

Putting purpose into practice

At financial planning firm Paradigm Norton, the first step in making the firm’s purpose and values come to life is at the recruitment stage, and employee engagement is key.

“When we recruit graduates it’s really all around purpose and values – there’s nothing more than that,” explains Paradigm’s founder and CEO, Barry Horner CFP™ Chartered MCSI. “If they have a good university degree in economics or maths, we don’t need to question their academic ability, but we do need to work out if they align with the purpose of the company and if our values resonate with them.”

Tracey Davidson says that employee engagement is vital to Handelsbanken’s purpose as an organisation. The current crisis has, inevitably, highlighted the value of human capital. Tracey believes that employee buy-in allows Handelsbanken to be more agile and better able to adapt to the current climate: “An unshakeable belief in the individual gives us the confidence to devolve decision-making power and accountability to colleagues all over the bank. This in turn creates more engaged employees. By avoiding unnecessary hierarchy or bureaucracy, we end up with a naturally agile, innovative organisation. Both we and our customers continue to feel the value of this culture during the current crisis.”

The round tables run by the CISI did provoke some scepticism from participants that purpose was too intangible, and that some firms would adopt a statement of purpose without actually putting it into action. This is clearly a crucial point. According to Mark, there is a systematic and comprehensive approach that firms can adopt. It involves identifying all your key relationships and looking at how you will bring the purpose and values to life in each one of these, identifying what outcomes should be measured and rewarded. Mark also has a simple litmus test: “I ask companies, ‘Can you tell me a recent occasion when you made a decision that sacrificed short-term gain for doing the right thing?’ If they can’t then I’m sceptical because it suggests they are still being driven by short-term results.”

Simon points to specific examples of firms adopting purposeful actions amid the pandemic: “The very tangible actions taken by many companies, which for many includes putting their employees’ health and financial security as a priority, and adapting operations to produce items such as personal protective equipment, provide excellent examples of the real-life application of purposeful business. Where a firm’s purpose is broader than merely profit, firms are able to take actions such as these,



which may not be profitable in the short term but which prioritise sustainability of both the businesses and wider society.”

Jonathan acknowledges that it can be a challenge to authentically assess how purpose-driven any individual firm is. “We are doing some work at the moment on how you might do that [assess the culture of firms] and there’s some interesting behavioural science,” he comments. “But we look at the evidence and make judgements based on our human experience. For example, we get access to the firm’s board minutes and, if the strategy documents say go for growth, and it’s all about profit and there’s no mention of value to the customer, we can start to draw conclusions about the overriding ethos.”

His advice to the leaders who have responsibility for thinking about the purpose of their firms is this: “As a starting point, ask yourself, why do I as a leader come to work? And when I’ve had a really good day and want to tell my family what’s so great about my work, what would I say? What is the ‘why’ for you?” Purpose beyond profit is not a fad, says Jonathan, and it is now part of the way the FCA assesses the firms it regulates.

// FIRMS CAN USE PURPOSE AS A NORTH STAR – A FIXED POINT TO HELP NAVIGATE //

Professional bodies also have a role to play when it comes to supporting ‘purposeful individuals’. In a thematic essay titled ‘Strengthening purpose in financial services: proud to be a professional’ in DP20/1, the Chartered Body Alliance (CISI, Chartered Insurance Institute, Chartered Banker Institute) says that members of professional bodies demonstrate purpose, both individually and collectively, through adherence to a code of professional conduct, professional qualifications, and a commitment to continuing professional development. The essay argues that “professional bodies provide aspirational standards and qualifications that give those members who achieve them a sense of meaningful professional pride and purpose beyond that bestowed by their firm alone.”

Fundamental to the purpose-driven approach is a growing belief that purpose and shareholder profit are not mutually exclusive; when you deliver value to all your stakeholders, that doesn’t mean there is less for shareholders. Doing the right thing, in other words, is ultimately good business. ●

Practising purpose

FOUR PRACTITIONERS WHO TOOK PART IN THE WHOLESALE FINANCIAL MARKETS ROUND TABLE WORKING GROUP OUTLINE THE BENEFITS OF PURPOSE – AND EXPLORE WHETHER THERE ARE BARRIERS TO ACHIEVING IT

KARIM HAJI, HEAD OF FINANCIAL SERVICES, KPMG IN THE UK



The success of most organisations, and KPMG is no exception, is driven by its people. The key in motivating employees, from small to large businesses, is to ensure that everyone has belief in

what the company is trying to achieve. This is where purpose is important. Employees with a strong sense of purpose are able to take real pride in the work they do because they can see the measurable benefit both to their organisation and wider society.

For firms like KPMG, where people are spread across a diverse range of projects and teams, it's important that everyone sees the purpose in the work that we do. This is so that we can all appreciate the part we play in its successes. One of the biggest challenges in galvanising large numbers of people behind a shared purpose is how to communicate it



One of the biggest challenges in galvanising large numbers of people behind a shared purpose is how to communicate it effectively

effectively, and this is about balancing relatability with simplicity.

Having a mission statement allows for plain-speaking communication of a firm's purpose, but the stories and examples behind this are what brings this to life.

KPMG is celebrating its 150th year, and learning about the impactful work done over the years has united many of us behind the values that fundamentally built our firm, and the ones that still drive it today.



JAMES BARDRICK, UK CEO, CITI



At Citi, we have seen the benefits of instilling a culture that aligns with our mission to enable progress for our clients and the communities where we operate. It is at the heart of everything we do, and we will also continue to develop this culture through our increasing focus on ESG.

Purpose is the thread that draws together all of our aspirations for being the best for our clients: high levels of employee engagement; exceptional service and product delivery; responsible risk-taking; and exhibiting the technological and financial ingenuity to provide solutions that are simple, creative and reliable.

Now, more than ever, we need to align personal, societal and corporate purpose to unlock the potential of our franchise and give our people the sense of individual fulfilment they deserve, and therefore this purpose must resonate with our employees, clients and stakeholders.

However, as a global bank operating in nearly 100 countries, aligning under a clear and consistent purpose while sustaining the benefits from this diverse team is challenging, and it requires incredible, authentic and trusted leadership throughout the organisation.



Purpose is the thread that draws together all of our aspirations for being the best for our clients

**DAVID GREEN, FORMER CENTRAL BANKER AND FINANCIAL REGULATOR,
AND ADVISER TO THE CHAIR OF RBS**

“
Defining an organisation’s purpose is valuable in terms of delivering greater cohesion amongst staff”



There is general agreement that defining an organisation’s purpose is valuable in terms of delivering greater cohesion amongst staff and explaining a firm to its stakeholders.

Some activities are much easier to explain than others. There is a particular challenge in achieving understanding of what wholesale markets are, what they do and what they are for. The wholesale markets do not have an external, public face towards the ordinary citizen and often have little profile within a larger financial group. In consequence, there is need for a good deal of education, both externally and within firms.

This involves explaining the central role they play in making possible services that are ultimately delivered by others: enabling farmers to know what prices they will be able to sell at; householders to fix the rate on their mortgage; exporters and importers to fix the exchange rate at which they can buy and sell; pensioners to be sure about the income they will receive

as long as they live; and so on. In short, the wholesale markets touch all corners of the economy and all the members of the society they serve.

Another challenge is to dispel the public image that emerged from the 2007 to 2008 financial crisis of unregulated, buccaneering wholesale markets. In fact, there have been many reforms, driven by both the regulators and the market participants themselves. The individual and collective sector initiatives that, for example, increase transparency, address conflicts of interest, and emphasise good conduct, are purposeful acts in themselves from which our widest societal stakeholders benefit through increased market efficiency.

The creation of new market standards, as well as continuing professional education initiatives by institutes such as the CISI, have played a key role. All this means, however, that there is work to do to explain both within firms and to the wider public that for wholesale market activity there is indeed ‘purpose’ that can rightly be promoted and adopted.

SUSAN REVELL, DEPUTY CHAIR & GENERAL COUNSEL, EMEA, BNY MELLON



An organisation that puts clear, meaningful purpose at the centre of its operating model drives an alignment of strategy and culture to the benefit of all stakeholders in an efficient and effective manner. It translates

into a positive experience for clients, shareholders and regulators, and encourages employee engagement and performance. Purpose, people and responsible performance combine in a virtuous circle.

BNY Mellon recognises the fundamental importance of articulating organisational purpose in a way that links our 236-year history with our strategy and market positioning. Our purpose is to power individuals and institutions to succeed across the financial world. Our purpose reflects our values and beliefs. It guides how we conduct our business and acknowledges our stewardship role in the financial services ecosystem.

The main barriers to achieving purpose arise when the organisation’s stated purpose isn’t

understood or doesn’t resonate with employees at all levels of the organisation. Purpose, and the values and behaviours that underpin it, need to be embedded in the fibre of the organisation through consistent and continuous reinforcement.

At BNY Mellon, our EMEA Conduct and Culture champions contribute to a programme titled ‘Living our Purpose’, which focuses on how personal objectives and attributes contribute to delivering a purposeful organisation. ●

“
The main barriers to achieving purpose arise when the organisation’s stated purpose isn’t understood or doesn’t resonate with employees at all levels of the organisation”



CV

2019 Chair of FPSB Board of Directors

2018 Chair-elect of FPSB Board of Directors

Head: technical support, PSG Distribution at PSG Konsult

2016 Joins FPSB Board of Directors

2014 Chair of FPSB's Regulations Advisory Panel

2012 Advice development and governance, Old Mutual

2005 Chair, Pension Lawyers Association of South Africa

2001 Board member, vice chair and chair of Financial Planning Institute of Southern Africa

1998 Legal adviser to an insurer and their advisers (Old Mutual)

Raising the standard

AS CHAIR OF THE BOARD OF DIRECTORS (BoD) OF THE FINANCIAL PLANNING STANDARDS BOARD (FPSB), GERHARDT MEYER CFP® HAS PLAYED A KEY ROLE IN SETTING GLOBAL STANDARDS FOR THE FINANCIAL PLANNING PROFESSION. BUT, AS HE TELLS **DAN ATKINSON**, MORE WORK REMAINS TO BE DONE.

Sitting astride the worlds of law and financial services, and with experience of setting standards in financial services globally and in his native South Africa, Gerhardt Meyer brings a unique perspective to the role of FPSB Board chair. This follows a spell as chair of an affiliate body, the Financial Planning Institute of Southern Africa (FPI), between January 2009 and February 2012. His current term of office, including his time as chair-elect, began on 1 April 2018 and runs until 31 March 2021. It has coincided with a period in which the financial advisory sector has been striving to maintain and improve its public image and, more importantly, to raise awareness of the ways in which its practitioners can help their clients to achieve their goals.

Gerhardt, who juggles his role at the FPSB alongside his role as head of the technical advisory services team at PSG Konsult, part of independent financial services group PSG, readily admits that he ended up in financial services almost accidentally, given he graduated in law from Stellenbosch University.

“I wasn’t quite sure what I wanted to do [after graduating in 1996] and I saw an advertisement for a junior role in a newly established investment business division at a large insurer. I thought I would work there for a while as a legal adviser and then make up my mind. I never left the sector after that.”

Gerhardt says that the main responsibility for setting standards for the global financial planning profession lies with FPSB’s Professional Standards Committee, which is tasked with constantly reviewing and – if appropriate – updating or crafting new proposed standards that are then put to the BoD. He explains: “The chair doesn’t get that involved at the drafting level, as it is a detailed topic that takes months of work at a time and the chair has many other responsibilities and board committees to attend to.” But he has been at the forefront of FPSB’s attempts to raise standards to the point that the public, governments and regulators recognise the value of the profession and consumers can easily identify practitioners who observe those standards.

Part of the challenge is defining what it is that financial advisers do. Everyone, Gerhardt says, knows what a doctor is, or a nurse. But what is a financial adviser? Is it the same as a financial planner? (See cisi.org/dfm-planners and cisi.org/blurredlines for more on this.)

Gerhardt explains that the role of financial planners has grown over the past few decades, from the 1980s when it mostly involved advice, to a more holistic modern-day approach that takes life goals into account. He also notes an increasing focus on professionalism: “As financial planning grows [in February 2020, FPSB announced a net rise in those with the CERTIFIED FINANCIAL PLANNER™ certification during 2019 of 6,744 to 188,104, taking the

average annual increase over the previous five years to 3.6%], practitioners increasingly want to be seen as professionals, adhering to the world-class professional standards that are upheld by FPSB.”

Another difficulty, he says, is that in contrast to doctors, nurses and other healthcare professionals, the public is generally less forgiving of failings by those in finance. They accept that medical mistakes such as misdiagnosis and mistreatment happen, and these sometimes lead to lawsuits, but when, for example, a “rogue bond trader who has run up huge losses” hits the headlines, the entire financial services sector, including financial advisers, can be tainted.

Regulation, regulation, regulation

In a sense, most modern regulatory roads lead back to the global financial crisis of 2008. Gerhardt, who chaired FPSB’s Regulations Advisory Panel between 2014 and 2017, having served as a committee member on the panel for four years prior to taking up the role, accepts that there was an increase in

regulation in its wake, but as to whether this amounted to over-regulation depends on who you ask. “It is a subjective thing,” he says.

Gerhardt explains that the South African Financial Sector Conduct Authority (FSCA) has a pragmatic approach to introducing new rules and systems. “[The FSCA has] a high regard for various other regulators, so often observes and consults with them on how regulatory changes work out for them before implementing them in South Africa,” he says.

One example is the UK’s Retail Distribution Review (RDR), followed by a similar Australian reform. Both aimed at an overall change of many aspects of the sector, but to a large degree focused on moving from rules-based to principle-based regulation and shifting from commission to fees. Gerhardt says: “South Africa subsequently implemented its own RDR programme [with the first phase having begun on 1 January 2018] but has only been introducing bits and pieces of it, as it continues to observe successes and failures elsewhere.”

More generally, he says, FPSB is in constant dialogue on regulatory matters with local, regional

// PRACTITIONERS INCREASINGLY WANT TO BE SEEN AS PROFESSIONALS //

GERHARDT’S TOP TWO PIECES OF ADVICE FOR FINANCIAL PLANNING PROFESSIONALS

1. Now, more than ever before, it is so important for the professional financial planner to help clients stay on track. They should review financial plans regularly to ensure they remain relevant and avoid decisions based on greed and fear.
2. They should get up in the morning with the sole aim of doing the right thing by their clients. This should become instinctive, moving from an attitude of ‘the law says’ to one of ‘the law is supporting our profession to do the right thing’.

PHOTOGRAPHY: COURTESY OF FPSB. ALL PHOTOGRAPHY TAKEN PRE-LOCKDOWN

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>> and global regulatory bodies, including the International Organization of Securities Commissions. “They take input from us and others in the sector seriously, and I really like that. There is a lot of listening and a lot of talking between regulators and market participants, more so than two or three years ago.”

Gerhardt believes that the emphasis has shifted from turning out pages of regulations or explanations that the consumer won’t read to a more practical approach, based on broader principles rather than detailed rules, and a lot of this is attributable to the increased dialogue with bodies such as FPSB.

He accepts that this may be an overly optimistic take on the current regulatory situation and how it impacts ordinary financial planners. “I’d add a note of caution, which is that my perspective as FPSB Board chair may not tally with that of a two- or three-person financial planning practice. Its perception may be that the burden of regulation is still onerous.”

Easing the compliance burden

For a number of small firms around the world, he adds, it is certainly true that the cost of compliance is still a problem, something which he has become aware of in discussions with FPSB’s affiliate organisations and practitioners globally. To help cope with this, he says, FPSB is urging all financial planning businesses to move away from a mindset in which ‘compliance’ and ‘business’ are separate functional areas and in which financial planners reluctantly drag themselves away from ‘real’ business activities to engage in the tiresome but mandatory activity of compliance. That, he believes, is a recipe for making regulation into something far more burdensome than it need be.

Far better to integrate both business and compliance in order to create what he calls a streamlined ‘compliant business process’, in which both halves of the equation



// THERE IS A LOT OF WORK TO BE DONE TO EDUCATE THE PUBLIC ABOUT THE VALUE OF FINANCIAL PLANNING STANDARDS AND PROFESSIONALISM //

mesh together seamlessly and compliance ceases to be a tedious chore and, instead, becomes an automatic and routine part of the operation of the business. He adds: “Some firms have done great work in this area. I have seen small independents in

South Africa take the plunge and become compliant business entities, and years later they are selling thriving planning businesses to larger corporates.”

A common standard

At the opposite pole from extensive, possibly excessive, regulation has been the notion that, given that defrauding clients is a criminal offence in all jurisdictions, there is no need for a professional financial planning body that sits between the law and the regulator on the one hand and the market on the other. Should we not return to the old verities of jail for fraud but caveat emptor for everything else, especially as personal financial advice is so bespoke and subjective?

Gerhardt thinks not. “No one has ever suggested to me that we don’t need norms and standards.” But he goes on: “And maybe the opposite is true – some people might suggest where a financial planning professional body exists there is no need for additional (excessive) regulation. They say: ‘I am a CFP professional, why do I need a regulator too?’”

He does not himself take this view, preferring to see a clear distinction between regulators and professional standards bodies, with each responsible in its own sphere. It all loops back, he says, to the need to bolster public confidence in financial planning and to raise awareness of the worth of financial advice. Here, Gerhardt says, regulators worldwide have an opportunity to partner with FPSB, and the financial planning professional bodies that make up the FPSB network globally, to educate the public as to the value of financial planning standards and professionalism as upheld by FPSB and CFP professionals worldwide. “There is a lot of work still to be undertaken.”

A more down-to-earth rationale for the existence of FPSB is, he adds, that any regulatory models that are developed need to ensure the opportunity for growth and innovation to serve the public. “Effective regulation of professional services such as financial planning is best achieved through a collaborative effort among governments and professional bodies, where governments set the regulatory expectations of practice, market integrity and consumer protection, and professional bodies determine professional norms, conduct expectations and education, and certification requirements that foster consumer and government confidence in the profession.”

Successes and challenges

Asked about the high and low points of his time as FPSB Board chair, Gerhardt replies that these can be two sides of the same coin, because meeting the challenge and resolving the issue can be immensely

satisfying. He finds more broadly a constant high point in the general atmosphere at the FPSB BoD and among the FPSB team. The combined BoD and core team is small, he explains, around 20 people at any one time, but “people commit a lot of time on a voluntary basis”, working on areas such as standards-setting and global strategy for the financial planning profession. It is not unusual, says Gerhardt, to have people on the other side of the world joining in calls in what, in their time zone, are the small hours of the morning.

FPSB BoD members are volunteers, and there is often a sense of sadness when a long-serving member is coming up for their last meeting. But he adds, “On the bright side, they often surface again two or three years later in a new volunteer role within the global profession, which is good!”

In November 2019, Gerhardt welcomed CISI’s head of financial planning, Jacqueline Lockie CFP™ Chartered FCSI, to FPSB’s Chief Executives Committee – which is accountable to the FPSB BoD for execution of current year priorities within the FPSB network.

A distinguished pedigree

As noted above, Gerhardt has both a legal background and previous experience in standards-setting and the advocacy aspect of building the financial planning profession. Asked if his lawyer background means he approaches his role as FPSB Board chair in a different way from someone with, perhaps, a purely financial background, he replies: “A short answer would be: not as much as one may think, for the simple reason that most of my legal life has been spent in the financial services sector.”

But, he adds, there are some nuanced differences of which he is aware, and slight differences of approach. The law is a discipline, says Gerhardt, so, for example, it has always prompted him to recognise the importance of getting things done in a timely manner. Similarly, once the participants in a meeting are in agreement, he is keen to get it all written down straight away: “I feel a constant imperative to dot the Is and cross the Ts.”

His time at the FPI, which involved engaging with the FSCA, was a good grounding for his work with FPSB. “The FSCA is progressive and engages with the sector a lot, which allowed me lots of opportunity to understand how the regulatory process works and how professional standards dovetail with regulatory standards.”

Operational efficiency

Looking at FPSB, and whether it could operate more effectively, Gerhardt says the BoD works well (“but you may reply that I would say that!”), while accepting that there is always room for improvement.

Ideally, he says, one change for the better would be if the BoD could meet face-to-face more often. “But that is very hard, for logistical and cost reasons.” As a result,



FPSB Board of Directors,
as at April 2019

he says, the BoD relies a great deal on videoconferencing. It is really helpful to have board members from around the world.”

To conclude where he began, Gerhardt returns to the key question of public confidence and trust in financial advisers. Are consumers reassured by FPSB’s vision, mission and strategy? Are they aware of its existence?

He says: “I feel we have been pretty successful in getting our story out there. Our global community meetings, for example, are very well attended by affiliate organisations’ leadership who, in turn, help feed the message out, through social media and subsequent public speaking engagements, to the global profession and to clients.” These meetings are held twice a year and involve the FPSB BoD, the leadership (both volunteer and paid) of FPSB affiliates from around the world, and various support bodies including the Chief Executives Committee, the Member Advisory Group, the Asia-Pacific Forum and FPSB Europe, along with a professional standards committee. Due to the Covid-19 pandemic, FPSB will not hold in-person meetings in 2020, but through videoconferencing and other digital means it will continue to engage the global FPSB network in long-term strategic planning for the financial planning profession and CFP certification standards.

All of this, Gerhardt says, is important and helps assure the public that there is a professional standards-setting body overseeing the global financial planning profession and promoting standards of excellence in the public interest. Gerhardt says: “Of course, we can always do more and do better. However, I can say I am proud of the great deal that we have achieved.” ●



A new chapter

THE EUROPEAN COMMISSION IS UNDERGOING A SERIES OF IMPORTANT CHANGES UNDER THE LEADERSHIP OF ITS NEW PRESIDENT, URSULA VON DER LEYEN. HOW WILL HER AGENDA AFFECT THE FINANCIAL SERVICES SECTOR? **DAVID BURROWS** REPORTS

The European Commission has a fresh look and several new challenges. With the UK locked in post-Brexit transition talks with the EU, and with climate change and the global Covid-19 crisis an overriding consideration, the new president Ursula von der Leyen – who was elected in July 2019 and took up her post at the end of the year – holds the reins at a pivotal moment.

Many of von der Leyen’s major commitments in her manifesto *A Union that strives for more*, published in October 2019, are relevant to the financial services sector. Among them are a new Green Deal, further commitment to a capital markets union (CMU) and a banking union, as well as a fintech action plan and a strategy to help small and medium-sized enterprises (SMEs). More on these in a moment.

There is plenty for CISI members working across Europe to take on board. Von der Leyen’s pre-Covid-19 manifesto promises a marked shift in focus from the Commission’s two previous policy cycles, where the key driver was a response to the 2008 financial crisis. One of the first acts of the previous Juncker Commission was to centralise “existing expertise and responsibility” in a new directorate, covering “financial stability, financial services and the CMU”. The rationale was to “ensure the Commission remains active and vigilant in implementing the new supervisory and resolution rules for banks”. The presidency of von der Leyen’s predecessor Jean-Claude Juncker, from 2014 to 2019, was generally a good one for investors. The blue-chip Euro Stoxx 50 index of ‘supersector leaders’ in the eurozone rose from an

average of 3,013 in December 2013 to an average of 3,715 in December 2019.

Under von der Leyen, the themes of sustainability and global competitiveness were set to take centre stage, although the Covid-19 pandemic has necessitated a revision of priorities as Europe seeks to weather the storm. An overview of the Commission’s response indicates that it is “working on all fronts to contain the spread of the coronavirus, support national health systems, protect and save lives, and counter the socio-economic impacts of the pandemic”.

In an emotive speech to the European Parliament on 16 April 2020, von der Leyen promises to “use every available euro we have – in every way we can – to save lives and protect livelihoods of Europeans.” She also speaks of kick-starting economies and driving recovery “towards a more resilient, green and digital Europe”, which includes “doubling down on our growth strategy by investing in the European Green Deal”, making the point that “global warming will not slow down” as the “global recovery picks up”.

Von der Leyen in context

Von der Leyen has an uncomfortably narrow majority in the European Parliament, but prioritising sustainability may keep the increased numbers of elected Greens and liberals onside. The Commission president won ratification in Parliament by 383 votes to 327, surpassing the required 374-vote threshold for an absolute majority.

While Pablo Portugal, managing director of advocacy at the Association for Financial Markets in

ILLUSTRATION: MARK AIRS/IKON

Europe (AFME), believes the changed make-up of the Parliament brings a different dynamic to the new Commission's agenda, he suggests sustainability was already proving a unifying theme for those on the left and right of the European political spectrum. He points to the introduction of the Sustainable Europe Investment Plan in 2018 and the European Green Deal Investment Plan in January 2020 as evidence of the strength of commitment and level of consensus in general across the EU in this area.

Regarding what to expect from von der Leyen over the coming years and her track record on supporting the financial services sector in the past, Graham Bishop, a highly respected independent consultant on European integration, notes that she does not have much direct experience with financial services in her career to date. Von der Leyen is a German citizen who was born in Ixelles, a suburb of Brussels. She graduated from medical school in 1987 and lived in the US for four years while husband Heiko took up an academic appointment, before returning to Germany in 1996.

Back in Germany, she became involved with the centre-right Christian Democratic Union party and in 2005 was appointed minister of family affairs. In 2009, she moved to become minister of labour and social affairs, then, in 2013, became Germany's first female minister of defence. In 2019, she emerged as the successor to Jean-Claude Juncker as Commission president.

Pablo expects her to champion a pro-integration stance in finance and taxation policy. This was foreshadowed by her letter of 1 December 2019 to Commission vice-president Valdis Dombrovskis, in which she sets out priorities in areas including tax harmonisation, anti-money laundering (AML) and CMU, which are expected to be subject to a more European-wide outlook, rather than a member state perspective. For instance, proposals are being formulated for a new AML body that will take power and supervision from the EU nation state to the European centre.

If von der Leyen is something of an unknown quantity with regard to dealing with the financial sector, the same cannot be said of Dombrovskis, who has retained his role overseeing CMU and banking union, providing continuity and direction in key areas. The former Latvian prime minister has served as a commissioner since 2014, first as vice-president for the euro and social dialogue. He kept this role after the UK's Brexit vote but also took over responsibility for financial services, formerly held by the UK's commissioner.

In the letter, von der Leyen gives him the brief of "executive vice-president for an economy that works for people", telling him: "What we do now will determine what kind of world our children live in and will define Europe's place in the world."

Are the European Commission's new manifesto commitments on CMU, banking union and

sustainability good news, overall, for the financial sector? Possibly, but the key to the first two will be in delivery, given talk of creating a 'single financial space' in Europe dates back to the Commission presidency of Jacques Delors, which ended in 1995.

Taxonomy and the Green Deal

The Green Deal has received a boost from the 'taxonomy agreement' thrashed out by EU member states in December 2019. This establishes a common classification system and rules laying out what is and is not an environmentally sustainable economic activity. The agreement says it "will enable investors to reorient their investments towards more sustainable technologies and businesses". On 9 March 2020, the technical expert group (TEG) on sustainable finance, which was set up in June 2018, published its final report on the taxonomy, outlining the TEG's final recommendations to the Commission. The recommendations cover the overall design of the taxonomy, as well as implementation guidance for financial firms and a technical annex that details updated technical screening criteria for climate change mitigation and adaptation activities.

All technologies covered by the taxonomy will be subject to the strict test of the 'do no significant harm' principle. Further development of the taxonomy will take place via a new Platform on Sustainable Finance, which is expected to launch in the autumn of 2020.

As Graham Bishop outlines, the taxonomy agreement may be a first step, but it is a hugely important one. It enables the Commission to progress its Green Deal because it defines terms. Is an investment green? "Yes" or 'no' depends on the taxonomy – you build it up from there," says Graham. He

adds that the EU aims to make the Green Deal the gold standard on sustainability for others to follow. For instance, if a US company wants to issue bonds in Europe, it will need to certify that it is 'green' based on the EU criteria that the TEG on sustainable finance set out in its final report in March 2020.

The report insists that proceeds from EU green bonds should finance 'green projects' that contribute substantially to at least one of the six environmental objectives of the EU Taxonomy Regulation.

These objectives are:

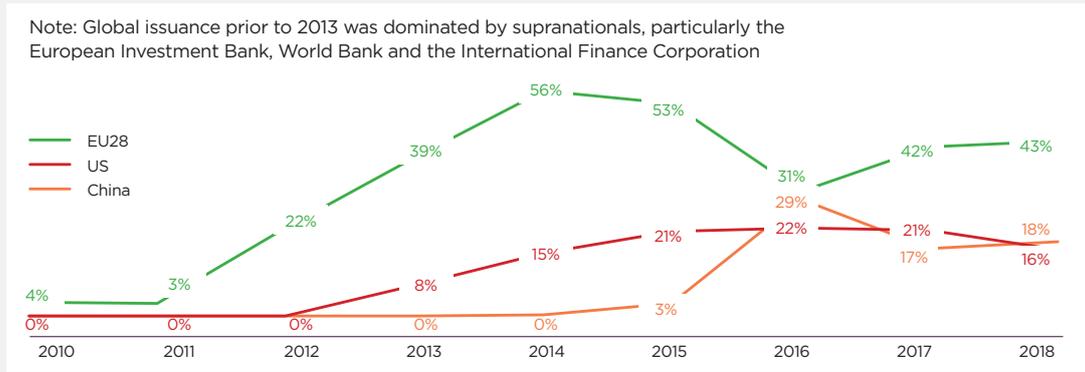
- climate change mitigation
- climate change adaptation
- sustainable use and protection of water and marine resources
- transition to a circular economy
- pollution prevention and control
- protection and restoration of biodiversity and ecosystems.

Europe is already a global leader in sustainable finance, as is reflected in its issuance of sustainable bonds (see graph 1 on page 34). Figures cited in an AFME report

// WE MUST CONTINUE DEVELOPING THE GROWTH FINANCE MARKET FOR THE INNOVATIVE COMPANIES OF THE FUTURE //

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GRAPH 1: SUSTAINABLE BOND ISSUANCE AS A % OF GLOBAL ISSUANCE (EU28, US, CHINA)



Source: Climate Bonds Initiative, Dealogic, AFME's Capital markets union: Key performance indicators

>> published in October 2019 show that the EU issued 43% of global sustainable bonds in 2018 – significantly ahead of the US and China. The Commission aims to build on this as part of its overall commitment to the EU being climate neutral by 2050.

The taxonomy agreement also allows initiatives such as the EU climate benchmarks to progress. The EU Climate Transition Benchmark and EU Paris-aligned Benchmark are designed to increase transparency on investors' impacts, specifically in relation to climate change and clean energy. Until now, no established framework has emerged for measuring the alignment of an investment portfolio with a temperature scenario. The EU climate benchmarks will only comprise companies that can demonstrate that they comply with a global temperature increase limit of 1.5°C.

Whether asset managers can fully report on their EU taxonomy aligned 'climate change' funds will depend on the transparency levels of the companies in which they invest. If they want to market their fund as a 'climate-

focused' product they will have to report what percentage of their fund complies with the taxonomy. According to the European Commission: "Financial benchmarks have an important impact on investment flows. Many investors rely on them for creating investment products, measuring their performance and devising asset allocation strategies." This should provide an incentive for companies to comply.

Capital markets union

The previous Commission championed the CMU action plan, aiming to make it easier for companies to enter and raise capital on public markets. According to the EU press service, the completion of the CMU was "one of the Juncker Commission's top political priorities". But with the building blocks of the CMU largely in place, as per the manifesto, it is time to go further.

// THE TAXONOMY AGREEMENT MAY BE A FIRST STEP, BUT IT IS A HUGE IMPORTANT ONE //

It reinforces the EU's commitment to CMU, while a final report by the High Level Forum on the Capital Markets Union – established by the Commission in November 2019 – was published on 10 June 2020, setting out recommendations to move the EU's capital markets forward. Pablo is encouraged by this, saying that it indicates the Commission's commitment to taking CMU to the next level, which may include significant expansion of retail investor participation in capital markets. Essentially this would mean citizens investing in market instruments rather than keeping their money in deposits. Currently New York and London are the two main hubs of capital market activity, handling nearly 45% of global capital market activities, according to a recently published PwC report. Given the investor disruption triggered by the

Covid-19 pandemic, a robust and well-functioning CMU would seem to be more important than ever.

Losing London, its major financial market, further reinforces the evident need for the EU to develop more

capacity in capital markets. Pablo says there is a more urgent requirement now (given the UK's departure) for the EU to push for greater integration of its financial markets and improved connectivity between different international financial centres.

Progress on CMU is not just down to the EU – the financial services sector must also work constructively with the new Commission. "The sector has a huge role to play in developing capital markets," Pablo says. "It is not just down to regulation but about educating citizens on investing and how capital markets work."

But the new Commission president's concerns range beyond the world of large financial institutions. In her manifesto, von der Leyen stresses the importance of SME financing: "I want to make it easier for small businesses to become large innovators. We must continue developing the growth finance market for the innovative companies of the future."

Banking stability?

Referring to the Sustainable Europe Investment Plan in her manifesto, von der Leyen says: “Public finances alone will not be enough. We need to tap into private investment by putting green and sustainable financing at the heart of our investment chain and financial system.”

The new Commission is openly encouraging green loans as well as bonds and is in the process of examining whether banks should be encouraged to fund sustainable sectors via a potential softening of the EU’s rules on capital charges on their lending. The Commission taxonomy agreement from December sets out broad criteria for sustainable finance of all types, including climate change mitigation, pollution prevention and the protection of biodiversity and ecosystems.

While rewarding investments into clean technologies can clearly be seen as encouraging responsible finance, the loosening of capital requirements has set alarm bells ringing in some quarters. José Manuel Campa, chair of the European Banking Authority (EBA), recently warned of the dangers of over-incentivising such lending by perceptibly easing capital requirements for banks. “What the EBA chair is saying is that you can’t have a ‘green’ economy if the European banks become insolvent in the process,” Graham explains. “That is the danger when you lend to people on incorrect risk weights.”

The European Commission will remain focused on its 2050 climate neutrality target, but the stability of the banking sector comes into the equation if rules are softened and the onus for sustainable investing falls too heavily there. This is where the further development of capital markets could help as an alternative funding source. Safeguarding the stability of the banking sector in general is a challenge that has carried over from the previous Commission. The key piece in the banking union jigsaw remains the European Deposit Insurance Scheme (EDIS). If implemented, it would ensure citizens could be certain of the safety of their deposits up to €100,000, independent of their location.

As Graham points out, the basic need for banking union has not gone away. However, future progress may depend on whether Germany softens long-standing red

lines on EDIS, and how far other nation states (such as Italy) are prepared to compromise in other areas to break the impasse. The new Commission’s reiterated commitment to banking union is good news, but hard negotiation lies ahead – as Valdis Dombrovskis pointed out in a speech back in November 2019, where he spoke about a “further push during the next Commission’s mandate” for banking union.

Technology catalyst

Remaining competitive in a global and fast-moving marketplace is a prerequisite for EU financial service providers. Technology is the great enabler here. However, there is a significant gap between the EU27 and other countries (especially the US and China) when it comes to investment in fintech companies – for example, according to the AFME report mentioned previously, US\$120bn in the US since 2009, compared with US\$7.2bn in the EU27.

The Commission’s fintech action plan hopes to address this and help the financial services sector maximise rapid advances in technology such as blockchain, as well as strengthen cyber security. While increased investment in fintech may be important, it is as much about people as money. Graham also suggests the sector can work constructively with the new Commission, going forward, to increase this pool of people who understand fintech: “We have been a bit overtaken by Covid-19, but a key role will be played by professional bodies supplying training and examinations in their normal professional requirements so people have to learn about all this to become professionally qualified – and the Markets in Financial Instruments Directive requires them to be qualified to advise clients.”

Croatia, currently holding the rotating EU presidency, has declared upskilling a priority: “A dynamic labour market requires the acquisition of new skills and competencies that in turn require lifelong learning and training to increase productivity, innovativeness and competitiveness.”

As a member state, the UK has led the way within the EU in terms of facilitating fintech innovations. In its flagship publication on the sector, *Fintech state of the nation*, the British government writes: “The UK has long been at the forefront of financial services. However, in more recent times, the sector’s positive response to the fourth industrial revolution has truly set us apart.” But the landscape is now changing, and the UK may struggle to access (or attract) the necessary tech expertise from within the EU talent pool in the post-Brexit years.

As with most of the EU’s manifesto commitments in the financial sector, the Commission may have prioritised the correct areas, but significant headwinds, not least the Covid-19 pandemic, may stifle swift progress. Von der Leyen has a full agenda before her, of which the prospects of the financial services sector form just one part. Her experience of the sector is light so far, but her manifesto has committed her to progress on several fronts. The financial services sector will be hoping she follows through. ●



PHOTOGRAPH: XINHUA/LAMY

Financial planning for global blended families



FINANCIAL PLANNERS AND WEALTH MANAGERS OFTEN FIND THEMSELVES WORKING WITH CLIENTS FROM COMPLEX FAMILY STRUCTURES. **RITCHIE BANN** REPORTS ON THE CHALLENGES THAT CAN ARISE

Global blended families – couples with their own children and children from previous relationships, spread across the globe – add a layer of complexity for financial planners and wealth managers. This brings plenty of interesting challenges, some of which we’ll discuss in this article, while also looking at the role that CFPTM professionals, certified to a global standard of excellence in financial planning, can play in helping these families achieve their goals.

“Blended families can take on many structures,” says Farida Hassanali CFPTM APP Chartered FCSI, a financial planner at Paradigm Norton. “We find that drawing a family tree can help capture the nuances of each relationship.”

Questions to consider when advising such families may include: Should the education of and provision for the newest children take priority, or can there also be assistance for the older offspring, not least in terms of college fees and house purchases? How can the different jurisdictional issues be navigated? What are the implications for inheritance?

“We always encourage clients to be open and honest with new and previous partners and their children, especially if they are old enough to understand,” says Farida. “Blended families can create a lot of emotions around how best to manage

finances. Our role should be to help clients be practical where possible.”

Globalisation the driver

Global families are a by-product of globalisation, with workers heading to far-flung lands in search of opportunity. According to data from the World Bank, world trade as a percentage of global output increased from 27.32% in 1970 to 59.44% in 2018. But the movement of people to live and work outside their home countries is at least equally noteworthy. The EU’s statistics branch, Eurostat, reports that, in 2018, 3.9% of EU citizens of working age were living outside their country of citizenship.

Worldwide, according to a July 2018 report by market research, consulting and publishing company Finaccord, the total number of expatriates amounted to about 66.2 million in 2017, a figure that has grown at a compound annual rate of 5.8% since 2013, when expatriate numbers were estimated to be 52.8 million. Finaccord predicts that by 2021, the number will reach around 87.5 million, although it remains to be seen what effects the ongoing Covid-19 crisis will have on this forecast.

Compliance across multiple markets

Nicholas Khan-Roper, Chartered FCSI, chief investment officer for a family office in Dubai, says: “In tackling the key challenges that global blended families pose for wealth

// IT’S ALWAYS BEST TO ENSURE CLIENTS RECEIVE THE APPROPRIATE ADVICE FROM AN EXPERT IN THE RELEVANT TERRITORY //

managers and financial planners, liquidity is of critical importance. The answer is to always keep substantial cash balances.”

In parallel with this increase in the number of blended households across the developed world is the practice of high-net-worth families – defined in Capgemini’s *World wealth report 2019* as “those having investable assets of US\$1m or more, excluding primary residence, collectibles, consumables and consumer durables” – to base themselves in one location, but with their investment arms set up in financial centres such as Zurich, Tokyo, London, Sydney or New York.

Steve Sokić, who leads IQ-EQ’s private wealth segment worldwide, says that “as soon as family members and assets cross borders, a family’s wealth becomes exposed to different regimes – be it local regulation, residency rules, creditor exposure, property and succession law, marital regimes or tax systems – all of which need to be considered.”

He continues: “And no two markets are ever the same. This can, and most often does, have a knock-on effect in terms of asset preservation, protection and succession. Where wealthy families are spread across multiple countries and their wealth is also invested in multiple places, more complexity is added – and this, in turn, increases their risk exposure. While there is no ‘one size fits all’ in regard to mitigation, at a very high level, one common and prudent approach for these families is to adopt more of a governance focus and to centralise and structure their wealth in a reputable tax-neutral jurisdiction with a proper regulator, financial and legal infrastructure, and support. With such a global holding platform established, attention can turn to ensuring compliance and mitigating any risks associated with the legal and regulatory nuances of each country in which family members and/or assets are located.”

Certain countries, too, can prove more problematic than others for wealth managers and financial advisers. The US, for one, is renowned for its tax complications and difficulties. Within its Internal Revenue Service (IRS) is a Taxpayer Advocate Service, which, as the name suggests, stands up for the recipients of the IRS’s demands. In July 2019, the body released a ‘Taxpayer Roadmap’, like that of an underground or railway system, which highlights the “complexity of tax administration [in the US], with its

connections and overlaps and repetitions between stages”.

“Different countries can have vastly different requirements,” Farida Hassanali says. “It’s always best to ensure clients receive the appropriate advice from an expert in the relevant territory.”

Reciprocal arrangements with firms on the ground in other countries can sometimes offer a convenient way for clients to access location-specific advice through a single channel. “Broadly speaking, it’s tax and legal advice that’s the important thing to undertake locally,” says Nick Reeves CFP™ Chartered MCSI, head of UK wealth planning at Deutsche Bank. “We can usually help the client to coordinate the wealth management relationship centrally from London.”

Phil Billingham CFP™ Chartered MCSI, director at Perceptive Planning, agrees that reciprocal arrangements can benefit clients, highlighting the global value of the CFP certification: “By definition, these clients need expertise in more than one environment or jurisdiction. We have found that by partnering with other CFP professionals in Australia or South Africa, for example, the client can get a much more joined-up outcome, which is more robust as a result.”

Financial planners should never go above and beyond their own expertise and what their private indemnity insurance covers. Otherwise they risk falling foul of regulatory requirements in other countries.

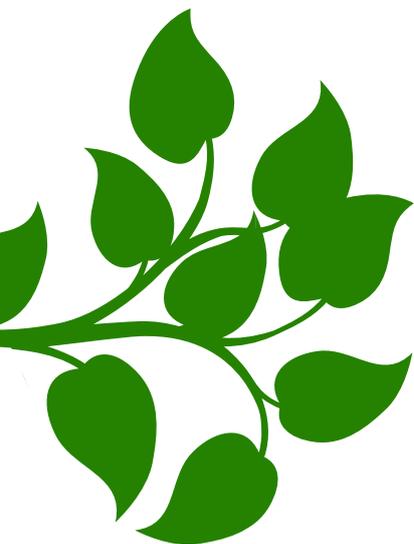
Keeping inheritance within bloodlines

Trusts, both offshore and onshore, are mechanisms that are typically used for holding wealth for these blended families. Other vehicles, such as family investment companies and open-ended investment companies, as well as private foundations and private funds within families, can also be appropriate, depending on the circumstances.

UK accountancy firm Saffery Champness has published a tax factsheet regarding family investment companies, and an article published in *The Review* in January 2019 (cisi.org/familyinvestment) also takes an in-depth look at such vehicles. “Really, the aim is to separate control of the assets from the beneficial owner,” Nick Reeves explains. “The head of the family typically wants to move assets on through the generations without relinquishing control. Traditionally, trusts have fulfilled this purpose. However, as taxes on trusts have become more punitive in recent years, we are seeing an

// BY PARTNERING WITH OTHER CFP PROFESSIONALS, THE CLIENT CAN GET A MORE JOINED-UP OUTCOME //

>>

// PLAN FOR LIFE
EVENTS, NOT
MONEY EVENTS //

>> increase in the use of corporate vehicles to achieve the same ends.”

Life interest trusts can also be used to keep wealth within bloodlines, especially when there's been a divorce. “A mother or father may have a new partner for whom they may want to provide an income, but a life interest trust stops any new partner inheriting the family's money outright,” Nick says. “Ultimately, on the death of both, the assets will revert to the children. It's an old-fashioned way of doing things in many ways, but it's still effective.”

In thinking about the interests of children from previous relationships, divorced parents need to consider whether prenuptial agreements with their new partners are the right mechanism to use, especially if significant assets are at stake. As Steve Sokić says, “you have to be sensitive to, and understand, family dynamics at all times.”

Tensions, and worse, can emerge over inheritance issues, and there are sometimes cultural and religious differences to be navigated, along with variations in law. In England and Wales, for example, people are free to leave their assets to whomever they like, while in France, by contrast, the law is very specific as to which family members get what percentage of the estate. Islamic law contains aspects of both approaches, in which someone has discretion to make personal bequests but a set proportion must go to family members such as spouses and children – they cannot be cut out of the will.

The great wealth transfer

The biggest wealth transfer in history is currently under way. Insurer Sanlam estimates in its 2018 report *The generation game* that £1.2tn will be inherited by millennials over the next three decades – this predicted cascade of assets down the generations is also highlighted in the Q1 2019 edition of *The Review*.

This handing on of assets to millennials is also a factor in the rise of philanthropy and of environmental, social and governance investing. It's beginning to shake up wealth management as we know it. Reasonable returns are still sought, but younger investors now want to know what impact their investments are having.

A survey conducted in August 2019 by asset manager American Century Investments reveals that the appeal of impact investing increased to 56% in 2019 in the US across all age categories, compared with 49% in 2018 and 32% in 2016. However, interest in impact investing is particularly high among millennials: it

appeals to some 72% of millennials in the US, while in the UK this figure stands at 65% for millennials, compared with an all category average of 59%.

Nicholas Khan-Roper says: “Most people look for low- or medium-risk investments, but they need to remember that, rather like a pension fund, they need to be able to meet their liabilities in terms of being able to fund their lifestyles.”

Any advice should be supportive, relevant and appropriate. Phil Billingham says that Perceptive Planning employs two key strategies to cater to global blended families: simplification and flexibility. “The challenge is that, while regulators, tax authorities and often advisers see their situation as unusual, or even exotic, for the families themselves their situation is normal. It's what they are living with. For us, the seemingly normal ‘offshore’ or ‘expat’ approach of using complex solutions is counterintuitive. These people have enough complexity in their lives, so we seek to simplify wherever we can.”

Phil's clients are ‘world citizens’ (see cisi.org/worldcitizens), and the mantra when advising them is, he says, to ‘expect the unexpected’. This is where flexibility comes to the fore. “They may well move jurisdiction again – there are all sorts of reasons why where they happen to live today may not be where they live tomorrow. So we employ flexibility and simplicity as far as we can. Always set up any arrangement with more than an eye on how you may change or exit from it – so no exit penalties or charges, be careful about allowing ‘pregnant gains’, watch your currency exposure, especially where you have assets and liabilities in separate countries from each other. In short, plan for life events, not money events.”

Whether you are dealing with a traditional nuclear family or one with burgeoning numbers that's spreading to the four corners of the world, advice over wealth shouldn't really differ. “Ultimately, it will always come back to what they are looking to achieve and how best to achieve that,” Steve says. “It's the first question we ask all our clients. It's just with globally minded and blended families the answers are a little bit more three-dimensional.”

Before the current pandemic, the pace of globalisation showed little sign of easing. The coming years will reveal the full effects of the virus on the globalisation trend, but it appears likely that this new world of cross-border wealth and asset structuring is here to stay in the long term. ●

Pressing the accelerator on financial inclusion



TECHNOLOGY HAS PLAYED A HUGE ROLE IN BRINGING PREVIOUSLY EXCLUDED PEOPLE INTO THE FINANCIAL SYSTEM AND WILL WITHOUT DOUBT CONTINUE TO DO SO. BUT TECHNOLOGY ALONE IS NOT THE SILVER BULLET. BY **PAUL BRYANT**

Globally, about 1.7 billion people remain unbanked, with nearly all of these people residing in developing countries, according to the *Global Findex Database 2017* (Findex), produced every three years by the World Bank. The situation has, however, been improving rapidly, with Findex reporting that 515 million adults worldwide opened an account at a financial institution or through a mobile money provider between 2014 and 2017, raising the percentage of adults with an account from 51% in 2011 to 69% in 2017 (63% in developing countries). The report says that “progress has been driven by digital payments, government policies, and a new generation of financial services accessed through mobile phones and the internet.”

The Covid-19 pandemic has thrown into sharp relief the advantages of digital financial services over a cash economy, not only in terms of reduced human contact but also the robust nature of automated payments systems over those reliant on bank staff.

Which technologies have had the most impact on financial inclusion, why is this, and what can we expect in the future?

Findex highlights research that illustrates the impact of digital financial services on financial inclusion in developing countries, such as helping people to save or enabling the transfer of money from distant friends and relatives; encouraging entrepreneurial activity and gender equality; and reducing ‘leakage’ from cash pension or benefit payouts.

However, Till Bruett, global practice lead, financial services and investment at development consultancy DAI (and previously secretariat director of the United Nations task force on the digital financing of the Sustainable Development Goals), cautions about getting too obsessed with numbers. “There has been a huge emphasis on ‘registration’ numbers when we talk about using technology to boost financial inclusion, which is understandable because rapid scaling is what makes technology so impressive – the ability to connect vast numbers of people very quickly,” he says. “But while financial product adoption is important, doing so superficially is not all that helpful. People must actively use the product, not just ‘sign up’, and that product has to have a positive impact on their lives. We don’t

THE IMPACT OF DIGITAL FINANCIAL SERVICES ON FINANCIAL INCLUSION IN DEVELOPING COUNTRIES

19% of adults in developing countries made a payment with a mobile money account

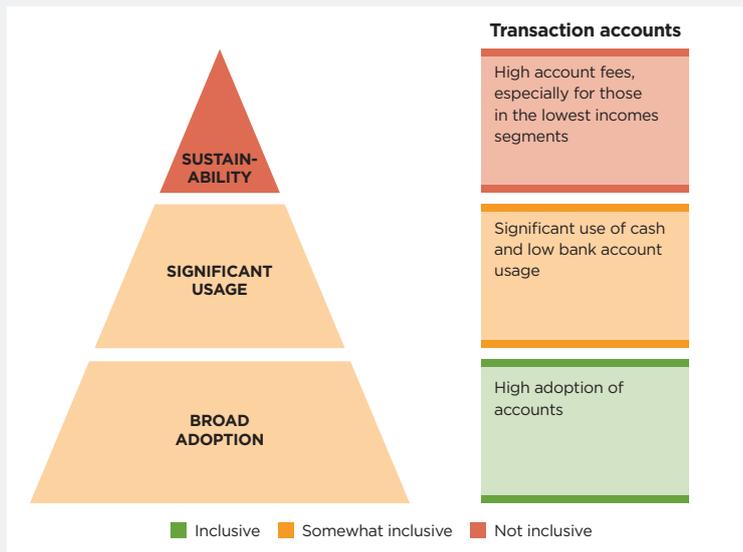
Access to mobile money services in Kenya helped **185,000** women develop business or retail activities

Biometric smart cards reduced leakage of funds for pension payments by **47%**

Source: *Global Findex Database 2017*

>>

FIGURE 1: AN ASSESSMENT OF SOUTH AFRICA'S SUSTAINABLE FINANCIAL INCLUSION



Source: BCG analysis

>> want digital credit being used to develop and fund a gambling habit, for example.” His point is illustrated by an example presented in the 2017 Boston Consulting Group (BCG) report, *How to create and sustain financial inclusion*: “In South Africa, 70% of adults have transaction accounts [a high share of the market considering South Africa’s overall economic profile], but more than one-quarter of account holders withdraw their wages as soon as they are deposited. These adults are not actively using the accounts to achieve financial goals, and they are not taking advantage of other financial services. Consumers may resent these accounts as conditions of employment or receipt of welfare and other public, or social, payments. Many view accounts as constraints, not enablers.”

BCG came to these conclusions after interviewing 1,500 low-income South Africans, 40% of whom said the reason they did not have an account was that fees are too high. One respondent commented that “the mattress doesn’t charge for small withdrawals”. Another commented that “a lot of scams happen over the internet” – a sentiment echoed by 33% of respondents who said they don’t have an account because of fear of fraud.

Foundations in mobile and digital ID
Jan Bellens, global banking and capital markets sector leader at EY, says that two

technologies in particular are foundational to financial inclusion – access to mobile phones (preferably, but not necessarily, an internet-enabled phone) and some form of digital identification.

Access to mobile phones has raced ahead of financial inclusion. Findex reports that globally, around two-thirds of all unbanked adults – 1.1 billion people – have a mobile phone, with a quarter of these having access to the internet as well.

Even a simple mobile phone can open up access to mobile money accounts. These electronic accounts, usually provided by a mobile telephone provider, are linked to a mobile phone number and may or may not be linked to a formal bank account. They allow users to store, send, and receive money using their mobile phone.

Probably the most successful example of mobiles being an enabler of financial inclusion is M-Pesa in Kenya (see cisi.org/mobilemoney). M-Pesa launched in 2007 as a basic payments system using existing SMS technology to allow people without bank accounts to deposit or withdraw cash at agent shops, transfer money person-to-person, and buy prepaid airtime.

Today, customers have access to not only mobile payments but savings accounts, overdraft facilities and loans, which is driving further growth. According to parent company Safaricom’s 2019 annual report, active M-Pesa users (those who used the service at least once within a 30-day period) grew 10% over the previous year to 22.6 million and, on average, executed 12 transactions per month (11% up on the previous year).

But while mobile phone adoption presents an opportunity in many countries, access to identification that satisfies financial services’ onboarding requirements remains a big problem. According to the World Bank’s Identification for Development (ID4D) initiative, nearly one billion people lack any legal identification (digital or otherwise), which mostly prevents them from opening a bank account. Findex also suggests that, even if access to basic identification is available, it is often insufficient with today’s ‘know your customer’ (KYC) demands, where additional documentation such as a utility bill with a home address is required, but often not available.

Digital ID is a solution to this problem. It can include a range of technologies and methods to verify and authenticate identity,

M-PESA MOBILE MONEY TRANSFER

Active M-Pesa users* grew 10% over the previous year

to 22.6 million and, on average, executed 12 transactions per month

rise vs previous year

*Those who used the service at least once within a 30-day period

Source: Safaricom’s 2019 annual report

including verification of personal traits (fingerprint, iris, face or voice); knowledge (PIN or password); and possessions (smart card, mobile phone, security token). It can also be deployed over a range of channels such as mobile phones, computers, or internet-enabled central authentication points (such as a bank ATM).

A 2019 report by McKinsey, *Digital identification – a key to inclusive growth*, says that dozens of countries are implementing digital IDs, often with mixed results. However, the Indian government’s Aadhaar programme, started in 2009, has achieved the highest participation rate at 95% of all adults (1.2 billion people). This is the world’s largest ‘biometric’ identity scheme.

Participation is voluntary (although benefiting from some public services can be difficult for those outside the programme), with Indian residents issued a 12-digit number after the completion of a verification process including demographic (such as name, date of birth and gender) and biometric information (ten fingerprints, two iris scans and a facial photograph).

According to *State of Aadhaar: a people’s perspective*, 49% of participants have used Aadhaar to access one or more services, such as bank accounts or pensions, for the first time.

Building on the foundations

Jan Bellens says these foundations, which are often used to get people into the financial system for the first time with a transactional banking or payments account, can then pave the way for rolling out more sophisticated financial products such as credit, insurance and savings. McKinsey has said a transactional account is commonly the start of a ‘digital trail’ (which would include an electronic record of transactions or even social media activity) that provides useful credit scoring data.

In this vein, the Aadhaar programme has provided a platform for the private sector to participate in and accelerate financial inclusion. Bharat Financial Inclusion (BFIL), the largest microfinance company in India according to the 2018–19 annual report of parent company IndusInd Bank, is one such company.

A BFIL press release from June 2017, describing the programme, says the company is in the process of rolling out 20,000 Kirana Points – a customer service point, typically equipped with a tablet, connected to a mobile network, with a fingerprint and card reader attached,

housed in a BFIL branch or an affiliated merchant store – across 16 states in India. Loan officers, trained by BFIL, help consumers to apply for a loan using a mobile device and “supporting tools like a biometric device or a card reader”. The system performs KYC and relevant credit checks and makes a lending decision in seconds.

The system provides multiple benefits, including easier and cheaper access to credit, as well as access to new financial services such as savings and bill payment facilities. BFIL improves its operational efficiency – customer meetings, typically done in groups, fall in duration from 45 minutes to 20 minutes, and fraudulent loans are reduced. Also, store partners can expand their businesses by earning fees from financial product facilitation and potentially benefit from increased footfall to the store.

According to McKinsey, the Aadhaar system has reduced onboarding and verification costs associated with satisfying KYC requirements in India from approximately US\$5 to approximately US\$0.70 per customer, by eliminating swathes of manual processing of paper documentation and in-person verification of the account holder’s identity.

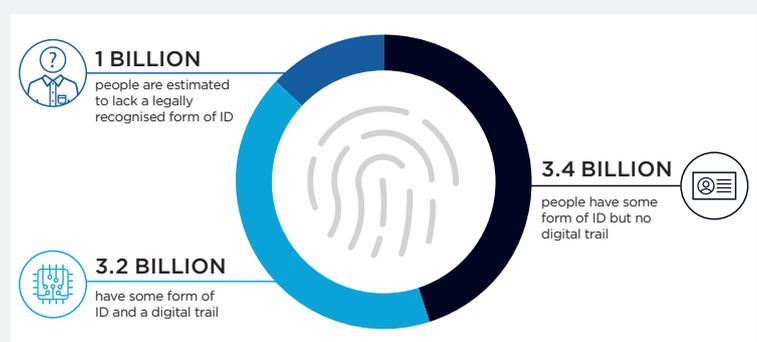
Till Bruett says the growth of digital credit is one of the more prominent trends in the world of inclusion, noting in particular the ‘savvy’ companies using basic data sets (such as a limited history of payments or even airtime purchases), or more advanced but ‘alternative’ data sets, such as the size of consumers’ social networks and the frequency of contact, to determine creditworthiness.

For example, in Indonesia, micro-financing company Amarta provides

// CUSTOMERS HAVE ACCESS TO NOT ONLY MOBILE PAYMENTS BUT SAVINGS ACCOUNTS, OVERDRAFT FACILITIES AND LOANS //

>>

FIGURE 2: UNLOCKING GLOBAL ECONOMIC VALUE



Source: *Digital identification: a key to inclusive growth*, April 2019, McKinsey Global Institute www.mckinsey.com. © 2020 McKinsey & Company. All rights reserved. Reprinted by permission

>> a peer-to-peer loans service and has developed a credit scoring algorithm based on a review of its credit-seeking businesses (typically a single-person business such as a food vendor or weaver, with the applicant known as a ‘micropreneur’), as well as demographic and personality data – gathered through psychometric testing. According to a 2018 conference paper *Psychometric credit scoring in Indonesia microfinance industry: a case study in PT Amarta Mikro Fintek*, Amarta applicants are required to respond to a set of 23 statements from field officers (necessary because some borrowers have limited literacy skills) which produces a personality profile correlated to creditworthiness.

Personality traits sought by Amarta include emotional stability, the capacity to process information, trust in the social environment, and trust in an individual’s own ability to influence their personal economic conditions. The algorithm becomes more refined over time using machine learning technology.

Lending is restricted to women, often in rural areas, who would struggle to raise credit through conventional means because of issues such as a lack of credit history. According to Amarta’s *Inspiring change: social accountability report 2018*: “Early marriage for girls has contributed to less decision-making ability for women in the family and reduction of future earnings by 9% (World Bank, 2017). With the spirit of empowering women, Amarta’s financial literacy and entrepreneurship curriculum have been designed to improve the decision-making of women in the family, especially with regard to budget allocation for children’s education, and health and sanitation needs of the family.”

Keep an eye on the tech giants

A potentially key development to look out for, according to Till, are further moves into financial services in developing markets by the global tech giants, with Chinese companies leading the way.

Ant Financial, a financial services company spun out of ecommerce giant Alibaba, has used Alibaba’s existing customer base to become a provider of payments to 1.2 billion people globally (900 million in China alone), and a provider of wealth management services, small and medium-sized enterprise loans, insurance and credit reference services to a further 740 million consumers and 28 million small businesses, according to the Alibaba Group 2019 Investor Day presentation.



Evidence of these companies expanding into international financial services is not hard to find. Ant Financial’s international operations include a partnership with Safaricom in Kenya, which allows Kenyans to purchase goods on AliExpress (an Alibaba-owned ecommerce platform selling mostly Chinese goods), using M-Pesa.

Despite its big contribution to financial inclusion, Jan stresses that technology itself should not be seen as a silver bullet, and that continuing the growth trajectory of financial inclusion will depend on finding the correct blend of technology, regulation, and human ingenuity.

He says: “The bottlenecks today are often not because of technology constraints, but in other areas, such as the ability of regulation to keep up (accepting digital IDs in a KYC process), financial literacy (not just education in terms of financial management and financial products, but literacy in terms of having trust in the financial system itself), and also the design of customer experiences, which, if done poorly, constrain the adoption and use of new technologies.”

There are encouraging examples of leaders to follow or learn from in these areas, such as India’s ‘Small Finance Bank’ regulatory regime, designed specifically to promote financial inclusion by lowering the capital requirements of lenders; and Amarta’s financial literacy classes, which were attended by all 110,392 new borrowers onboarded during 2018 before they received their first loan disbursement.

Finding that blend will be the key challenge, not only to financial and tech companies but to the public and developmental sectors as well. ●

// FINANCIAL INCLUSION WILL DEPEND ON FINDING THE CORRECT BLEND OF TECHNOLOGY, REGULATION, AND HUMAN INGENUITY //

“

More traders, able to trade in either direction, result in more liquidity, providing better conditions for all investors in a market ”

*Roy Zimmerhansl, practice lead, Pierpoint Financial Consulting
The state of securities lending told in fives, pp.48-49*



IMAGE: ISTOCK

pp.44-45

Helping clients to establish, and achieve, a life of purpose

pp.46-47

The reputational impact of individual actions on a firm

p.50

CASS audits: key elements and revisions to the standard

Living life with purpose

IMAGE: ISTOCK

IAN PAINTER CFP™ CHARTERED FCSI, MANAGING DIRECTOR AT AFFINITY INTEGRATED WEALTH MANAGEMENT, EXPLAINS THE VALUE OF HELPING CLIENTS ESTABLISH, AND ACHIEVE, A LIFE OF PURPOSE

THE BRIEF

Pat and Jennifer, both aged 54, were referred to us by an existing client. Pat, an architect, knew that he could soon begin to draw on his substantial pension benefits. He wanted to look at the option, and the affordability, of retiring early, having spent most of his working life in the same company, albeit one that had been through a couple of mergers. The latest senior management changes taking place at Pat's employer did not suit him; he was tired of work and the new obligations he was being asked to take on. He needed to know when he could step away and either retire or do something completely different, less time-consuming and less stressful.

Jennifer, a part-time self-employed physiotherapist, had some health issues and it was likely that these would get worse over time, meaning their ability to make full use of their holiday home in Italy would be curtailed longer term. They loved holidaying in Italy and wanted to spend more time together relaxing and enjoying life. They also wanted to help their three children get on the property ladder by funding their house deposits. All three were in their mid-20s, two were in rented accommodation and one was still living at home.

The plan

Ahead of our initial meeting we requested that Pat and Jennifer complete some documentation. This included a full expenditure breakdown that enabled us to begin building some basic cashflow modelling for them. We always like to demonstrate the impact of cashflow modelling to a potential new client using some of their own data, as it's a great way to bring things to life for them.

It was obvious at the initial meeting that Pat was exhausted, while Jennifer's recent diagnosis was also a bit of a game changer. While there was no immediate danger to her quality of life, the condition would mean that she would get progressively worse and less mobile over time. Things had to change, and they had to begin to live life with purpose while they were able. But the big question was: what sort of life could they afford to live?

Pat's pension was valued at £1.4m; it was their biggest single asset by far. Jennifer also had some deferred pension benefits under the NHS scheme and some smaller personal pensions with an old closed life office valued at around £30,000. Their home was valued at £600,000 with a £170,000 mortgage outstanding on it. Their property in Italy was valued at £100,000, and other than £10,000 on deposit, that was the entirety of their assets. They were still supporting their children from their income, which between them amounted to £115,000 per annum.

We discussed the type of lifestyle they wanted to lead. They had both become used to earning good incomes, yet had not managed to build up any significant savings outside of pension. They were spending all that they were earning, but where? After some probing questioning, we established that slowing down was what they both needed to do, even if this meant learning to live on a lower level of income.

Our subsequent detailed analysis of their finances revealed that they had spent a lot of money on their children's education, and were now helping them with things like rent. Pat stopping work would mean him spending a lot less on fuel and there were several other expenditures that were either not required or would naturally fall away.

We produced several 'what if' cashflow models with differing levels of expenditure, covering various scenarios like downsizing their house, selling the Italian property, and Pat doing some consultancy work. After running through these, we established that they could have a comfortable lifestyle by generating £50,000 per annum in total income, with additional top-ups as and when required for some big holidays.

We then set about determining how they could meet their objectives, which included:

- clearing their mortgage debt
- providing some monies for house deposits for their children
- making some long-awaited improvements to both their UK and Italian homes.

We established that Pat and Jennifer could retire and stop work completely if they wanted to at age 55 by drawing Pat's pension, which would meet with most, if not all, of their objectives. They had sufficient resources to produce the £50,000 per annum they needed.

Pat gave notice to his employer, at which point they offered him a part-time consultancy position. He accepted, reducing his hours and increasing his daily rate to boot. Jennifer decided she did not wish to stop work completely, so she too reduced her working hours so they could spend more time together.

We began arranging for Pat to access his pension benefits at the age of 55. Once we had placed the pension onto a suitable platform, we structured the underlying investments, keeping a significant element in cash (we knew this would be required) and thereafter built a blended portfolio of both active and passive funds.

When Pat reached 55, we moved his pension into a flexi-access drawdown

arrangement, and he began crystallising some of his benefits in a phased manner. We did this by targeting pension commencement lump sum amounts. The blended portfolio we built for him has increased by just over 15% since inception (late 2016).

When Jennifer reached 55, we arranged for the phased encashment of her existing personal pension plans over a couple of tax years, her self-employed profits being at a level below the basic rate tax threshold. She was therefore able to access her personal pensions in a tax-efficient manner.

This enabled them to:

- gift significant sums to their children to enable them to buy their own properties
 - reduce, but not clear entirely, their own mortgage
 - make the required improvements to both of their properties
 - meet with their initial expenditure requirements in a tax-efficient way, taking account of their self-employed incomes.
- We were able to 'gap fill' their income with tax-free cash
- open some additional cash savings for them in individual savings accounts.

What happened next

Pat was able to keep his pension crystallisations below the £1m level, thereby avoiding any immediate Lifetime Allowance issue. Unfortunately, Pat did not engage with us early enough to be able to apply for any form of pension protection.

Following a review meeting just before Christmas 2019, Pat decided that he would not renew his consultancy contract after April 2020, and he will now retire completely at age 57. We are preparing for his pension to take higher levels of income withdrawal in the new tax year.

Pat and Jennifer are more relaxed and less stressed than when we first met with them. They are now looking forward to the next phase of their life together, and being able to live life with purpose. ●

// WE ALWAYS LIKE TO DEMONSTRATE THE IMPACT OF CASHFLOW MODELLING TO A POTENTIAL NEW CLIENT USING SOME OF THEIR OWN DATA //



IAN PAINTER CFP™ CHARTERED FCSI

Ian has been a financial planner for over 30 years, with his business specialising in true comprehensive lifestyle financial planning for those at or near retirement and their families.

He is a former committee member for both the Financial Planning Forum of the CISI and the South East branch of the CISI.

His firm is a CISI Accredited Financial Planning Firm.

Fighting for the right?

AN EXTINCTION REBELLION PROTEST TOOK PLACE OUTSIDE YOUR WORK, AND YOUR LINE REPORT, LORENA, A SENIOR INVESTMENT DIRECTOR, WAS FEATURED IN THE NEWS AND INTERVIEWED WITH OTHER PROTESTERS OUTSIDE THE COMPANY BUILDING



IMAGE: ADOBE STOCK

The global environmental movement, Extinction Rebellion, has been staging mass global peaceful protests to raise awareness and understanding of the climate crisis. The protests have included public marches, demonstrations, school walkouts and, since March 2020 – when the movement went indoors because of the Covid-19 pandemic – online rallies over videoconferencing platforms.

On your morning commute in February, while scrolling through the news on your phone, you were stunned to notice one of your senior investment directors, Lorena, a direct report, pictured in the thumbnail of an article about the protest. After clicking on the article, you saw the image taken over the weekend of Lorena outside the company building. The article features an interview with her.

You skimmed the article and clicked on the three-minute-long video interview.

The journalist starts the interview, recorded by the main entrance with the company logo in full view, by asking Lorena to identify herself and why she has decided to protest. She replies: “Hello all and welcome to the Extinction Rebellion protest today in our city. I’m a senior investment director and this is a cause that is extremely close to my heart...’ As the interview continues, Lorena is joined by other protesters who together explain the impact individual actions have on the climate crisis and encourage more people to join and exercise their right to protest.

After watching the video a few times and reading the article in full, you realised that it was number one on the news website and had been shared and retweeted on its Twitter page, and even included as a pinned Tweet. You arrived at work early and continued to search for where else the article had been featured. You saw that

2020 ANNUAL INTEGRITY DEBATE

This dilemma was discussed at the CISI 2020 Annual Integrity Debate, now on CISI TV. View it at cisi.org/integritydebate2020 to gain 1.5 hours’ CPD.



Extinction Rebellion had used all its social platforms to share the video, and it was quickly gaining viral traction, with over 100,000 views of the interview on its YouTube channel. It was also being shared by other news outlets.

Colleagues began arriving at the office, and you could overhear them talking about what they had seen on the news. They all gathered around a desk to watch the video interview and began questioning Lorena's actions. You could see that it had already caused a distraction in the office. As Lorena was your direct report and very well known within the sector, regularly speaking and participating at external events, representing the company on topics such as impact investing and environmental, social and governance, you began to consider the reputational impact, if any, her choice of action would have on the company.

Lorena was due to be in the office soon. As her line manager, you had to decide on the best course of action. You identified four options.

What would you do?

1. No formal action is required, but you decide to speak with Lorena privately to remind her of what is expected of a senior member of staff.
2. As the company has been indirectly associated with the Extinction Rebellion protests, and Lorena's involvement has the potential to bring the company into disrepute, a formal investigation will be opened that would most likely result in disciplinary action.
3. You give Lorena a verbal disciplinary warning as the company social media policy states "be careful discussing things where emotions run high (eg, politics and religion)".
4. Lorena's actions have brought the company into disrepute and interfered with her ability to do her job. The Board should be informed, and in order to mitigate any further potential risks, should speak with HR, advising that Lorena should be suspended on full pay pending the outcome of further investigation. ●



WHAT WOULD YOU DO?

Visit cisi.org/fightingfortheright to share your views. The survey results and CISI's opinion will appear in the August 2020 edition of *The Review*.

Most likely to: The verdict

This Grey Matter, published in the February 2020 print edition of *The Review*, presents a dilemma that arises when inappropriate workplace banter over social media is inadvertently uncovered by a team member who is the target of some of the comments. In this situation, the appropriate action of the individual and the manager involved is of the utmost importance.

Should you wish to suggest a dilemma or topic to be featured in a future Grey Matter, please contact us at ethics@cisi.org.

Suggested solutions and results are as follows:

1. On reflection, it's a bit of a laugh and saying something more will only make it worse. Also, Freddie is keen not to ruin his relationship with his line manager. (16%)
2. Freddie resolves to encourage Samantha to tell HR about the group, as it's clearly unacceptable. (47%)
3. Freddie should report the group to HR, using the photo he took on his own phone as evidence. (35%)
4. Freddie could encourage Dan to report the group to HR (either with Freddie, or on his own) - using the argument that it would be better to be the person that confesses rather than the person who gets caught. (2%)

Responses received: 377

This dilemma highlights some of the potential issues with the increasing use of social media in the workplace. A key principle to remember is that office gossip and banter about other colleagues in any form is unprofessional and can cause significant damage in the workplace. In this case, Freddie has been unfairly targeted and put in a difficult situation by his manager and others' poor behaviour. He does not want to potentially damage his relationship with his new manager, but he does want to stand up for what he thinks is the right thing to do.

This Grey Matter is also one of the scenarios discussed at the CISI's 2020 Annual Integrity Event on 12 February (view it on CISI TV). The audience voting at the event considered option 3 to be the favourite, with 42% of the vote, versus 35% for option 3 in the readers' online poll.

Our recommended solution is option 2, as this would enable Samantha, the manager, to do the right thing to rebuild Freddie's trust and to appreciate the importance of not allowing office banter and gossip to exist in the workplace by having an appropriate discussion with HR.

What is seen as office banter by some may seem very different to others and everyone has a responsibility to behave in a professional manner and to respect all their colleagues.

ROY ZIMMERHANSL, PRACTICE LEAD, PIERPOINT FINANCIAL CONSULTING, USES FIVE MARKERS TO EXPLAIN SECURITIES LENDING UNDER THREE HEADINGS

The state of securities lending told in fives

The securities lending business is on the cusp of the most impactful new regulation ever to affect the securities lending market – the EU’s Securities Financing Transactions Regulation (SFTR). In a series of five markers, we will explore the drivers of the business, the contribution it makes to markets and, finally, how environmental, social and governance (ESG) considerations are, or should be, driving investors’ securities lending behaviour.



SECURITIES LENDING

1. What: Securities lending involves the temporary transfer of stocks or bonds from an investor to a borrower in exchange for a fee. The transactions are typically governed by one of several standard sector agreements and almost always require the borrower to provide collateral to the lender as a risk mitigant against the potential for a borrower default (think Lehman Brothers).

2. Who: There are several participants in a conventional securities loan: an institutional investor that is the legal lender; an agent lender, usually but not always the investor’s custodian that acts on behalf of the investor; the borrower, usually a bank or securities firm; and the short seller that is the end user of the borrowed security. Recent figures from *Global Custodian* indicate the market has US\$25tn as securities available for loan daily, sourced from over 20,000 institutional investors. According to the International Securities Lending Association, the amount on loan has been hovering around US\$2tn for most of the past decade with an end-2019 split of 44% for equities and exchange-traded funds (ETFs), 47% for government bonds, 5% for corporate bonds and the remainder in other fixed income assets.

3. Where: Securities lending is now actively practised in more than 40 countries around the world. Several markets have introduced securities lending since the financial crisis, which included a ban on short selling in over 30 countries as one of its milestone events. Today, the allowance of securities lending and short selling has become a baseline expectation for consideration as a ‘developed’ market.

4. When: According to *Don’t blame the shorts* by Robert Sloan, the first recognised short sales occurred in 1609, but my guess is that people weren’t so concerned with lending securities to ensure delivery back then. For the first half of the 20th century, securities lending was less a business and more of a way to grease the wheels of settlement amongst market practitioners. The business aspect started to grow from the 1960s, and in 2019 was estimated to have generated around US\$10bn in fees for investors and their lending agents, according to IHS Markit’s Securities Lending 2019 snapshot.

5. Why: Institutional investors participate in lending to make money, whether using the proceeds as alpha capture or to offset expenses (as many ETFs do). End-borrowers need the securities to satisfy delivery obligations resulting from short sales. Short selling is part of multiple strategies that can be broadly categorised as directional (one-way bet that an asset price will drop), hedge (mitigating risk of loss from long positions), arbitrage (exploiting perceived price anomalies), and quantitative (algorithm-driven trend following).

Norges Bank Investment Management explains ‘The role of securities lending in well-functioning markets’ on its website. Let’s look at the benefits.



THE FIVE MARKET BENEFITS OF SECURITIES LENDING

1. Liquidity

Market making wouldn’t be possible without market makers having the option to borrow as well as buy securities they have sold to investors.

By allowing short sellers to participate in a market, there are more trades; both their short sales and their long purchases. For every share that is shorted there is a future purchase. Additionally, many proprietary traders operating market-neutral strategies avoid markets unless they can go both long and short.

More traders, able to trade in either direction, result in more liquidity, providing better conditions for all investors in a market.

2. Market efficiency

One of the original reasons for the development of securities lending was the need to borrow securities to avoid a failed settlement or to remedy a failing trade.



Roy Zimmerhansl is former global head of securities lending at HSBC. See him on CISI TV. roy@pierpoint.info

This is of increasing importance to regulators and the reduction in fails is a key goal for the Central Securities Depositories Regulation, which comes into effect in February 2021.

3. Constraint on short selling

One factor that also acts to restrict short selling volumes in most markets is the need for a would-be short seller to ensure there is a lender of the relevant security prior to executing a short. This 'locate' requirement effectively limits the number of shares and bonds available to be shorted.

4. Price discovery

This is the process whereby a current market price for an asset is set. Inevitably some traders will view an asset's price as expensive, others may consider it cheap, with the remainder having no view or accepting it as a reasonable representation of the value. Short sellers are one part of that community and securities lending represents a necessary part of the plumbing, enabling short sellers to contribute to price formulation.

5. Moderating peaks and troughs

Many people will be familiar with the phrase 'irrational exuberance' and short sellers play a role in regulating such excesses. When markets march uniformly in an unrelenting upward trend, short sellers assert themselves either as outright contrarians anticipating a market fall or as a hedge against a wider market fall. Amazon, for instance, is often shorted as a proxy to hedge against a wider market fall. It is a mega-cap stock, has huge daily trading volume and is widely available for loan (so cheap to borrow with low risk of an early close-out due to investor sales).

When market crashes occur, it involves investors of all types selling – long investors as well as short sellers. The difference is that short sellers need to repurchase the shorted stocks in order to book profits. Short sellers, therefore, help add buying substance to markets that might otherwise continue to have a selling bias and fall precipitously.



ENVIRONMENTAL, SOCIAL AND GOVERNANCE

Securities lending is part of the investment ecosystem, but at an individual investor level, is an optional activity. It is, therefore, a prerequisite that wherever relevant, securities lending reflects investor ESG principles. There are five key aspects to the intersection of ESG and securities lending.

1. Collateral

When securities are lent, the investor receives collateral – either cash or other securities. Cash is invested into money market instruments such as commercial paper, money market funds or reverse repo. If securities are used as collateral, the title transfers from the borrower to the lender. In both cases, the collateral assets form part of the fund property so the same exclusions that

apply to investments should be applied to the collateral. Not straightforward, but eminently doable.

2. Voting

Lending investors lose the ability to vote shares while on loan but can still exercise control over the process in several ways. First, they can exclude specific portfolios or assets from lending altogether. Second, they can exclude assets on an ad hoc basis if, for example, a contentious issue arises. Third, investors can put in place standing instructions requiring an agent to recall shares price to AGMs. Finally, on an ongoing basis, lenders retain the right to recall their assets from loan at any time and borrowers have a contractual obligation to return the shares within one normal settlement cycle. Accordingly, if an investor has not voted, it is a choice rather than a consequence of lending.

3. Tax

Clearly, prior to commencing lending, investors need to understand how various aspects of tax apply to securities lending. They also need to ensure they comply with their domestic taxation obligations while also satisfying the requirements in each lending jurisdiction where they are active. It is also critical that investors understand their agent's approach to loan distribution and policy with respect to managing collateral over dividend and interest payment dates for the collateral, as well as the securities on loan.

4. Governance

Lenders should have clear policy guidance on how they participate in lending, risk profiles, including counterparty selection and collateral acceptability, and approach to voting. They need to demonstrate how they deliver on those policies and test the management responsible for their securities lending activity.

5. Transparency

Investors should provide transparency to their own stakeholders on their securities lending activity. This starts with the formulation and communication of the topics identified under governance, but then deals with the communication of that information. SFTR reporting requires market participants to provide regulators with an enormous volume and granularity of data surrounding securities lending and repo transactions. The information made available will feed increased transparency. While there are some shining examples of transparency, much work is required here.

SUMMARY

Short selling and securities lending are the bedrock of the modern capital markets infrastructure. For a long time, it has been held out as a separate activity, exempt, immune or ignored when it comes to the process and thinking at the front end of investing. That needs to change – and it is.

As with all change, it will be uncomfortable for many and painful for some, but ultimately it will set the stage for a sustainable future for securities lending. ●

Quick quiz answers:
1.A, 2.C, 3.B



Ask the experts: CASS audit standards

Richard Andrews ACSI, financial services partner at KPMG, outlines the key elements of a CASS audit, how revisions to the standard will affect the firms that come under its scope and what these firms can do to ensure a smooth audit

Visit CISI TV for an insightful panel discussion on **Managing CASS in disruptive times**

The FCA's Client Assets Sourcebook (CASS) provides rules for firms to follow whenever the firm holds or controls client money or safe custody assets, helping to ensure the safety of client money and assets if the firm fails and/or leaves the market. There are two types of audit:

- 1) A reasonable assurance opinion on whether the firm has systems and controls to meet the requirements of the CASS rules.
- 2) A limited assurance opinion, which applies to firms that don't intend to (and claim not to) hold client assets and where the auditor will effectively provide an opinion that nothing to the contrary has come to their attention.

The assurance standard published in 2015 was the first consistent assurance standard for client assets. A revised standard for the audit of client assets, issued by the Financial Reporting Council, was published in November 2019 and came into effect on 1 January 2020.

Key developments include updates to reflect changes to regulation and the scope of the regime since it was first issued, and the strengthening of reporting requirements to those charged with governance. The revised audit standard also places more emphasis on firms being able to document how their IT and system controls comply with the CASS rules, expanding the scope of CASS audits. The increased scrutiny surrounding CASS audits means that many areas of a firm – several of which may not immediately spring to mind when considering the CASS rules – are now under the microscope.

What are some common challenges encountered with the 2015 CASS audit standard?

The rules are complex. The rulebook has developed over decades and is applied to companies from across the financial

services sector, so there is no one-size-fits-all approach. The 2015 CASS audit standard led to firms needing to develop detailed CASS risk and control assessments. This has been an increased burden on firms. However, in my opinion the additional focus has led to an increase in management-identified breaches or control deficiencies in the first years under the new standard.

“The zero materiality reporting threshold means that even the smallest error has to be reported”

It would be unusual for firms with a sizeable CASS business to have a completely clean opinion given the complexity of the rules. The zero materiality reporting threshold means that even the smallest error has to be reported, so a qualified opinion could be generated by an error of just a few pounds in a billion-pound business.

What constitutes a breach – and what approach should firms be taking to breaches?

In its simplest form, a breach is a failure to comply with a CASS rule. This could be a failure to undertake due diligence on a bank with which the firm has placed client money, although many errors arise from failures in record-keeping.

Firms should have preventative and detective systems and controls in place, and quality assurance processes are also vital. They also need to determine the severity of each breach, which needs to be logged along with details of its remediation plan, and assess whether they need to immediately notify the FCA.

How do the revisions address these issues?

One area in which the revisions will help is that it has been clarified that the auditor can use internal audit work as part of its planning and risk assessment.

The second area in which the audits could become more efficient is that the revisions are much more explicit around the use of service organisation reports. The challenge there is to ensure that these reports evolve so that they are sufficiently granular.

Is there a lack of knowledge and experience among audit staff with regard to CASS?

Client asset rules affect many different disciplines, so greater awareness across firms would help, as would specific training for reconciliations teams. This would help ensure that the auditor and the firm being audited are speaking the same language.

What can firms do to ensure a stress-free CASS audit, based on lessons learnt to date?

Best practice is to implement detailed rule-to-risk control frameworks that should be reviewed annually.

Firms need to look at the risks they are addressing, how frequently their controls are applied and whether they are detective or preventative to identify controls that might need to be tightened. It is also important to take account of changes to the business and regulations.

The level of documentation firms undertake around processes and controls has increased in recent years and the more straightforward the documentation, the easier it is for the auditor to see what is going on. It might also be useful to appoint someone to act as liaison between the auditor and the various teams within the firm. ●



“
The aim must be to return
to equilibrium a market that
has become dangerously and
obscenely skewed”

*Keith Robertson, Chartered FCSI,
The foundations of property, pp.60-63*

IMAGE: GETTY

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FROM THE EDITOR

THIS REPORT FOCUSES ON THE IMPACT OF **COVID-19 ON FINANCIAL SERVICES**.

THE COVID-19 CRISIS HAS HAD SHORT-TERM AND LONG-TERM CONSEQUENCES. SOME REGULATORY RULES HAVE BEEN RELAXED TEMPORARILY, AND LONGER TERM BOTH REGULATORS AND FIRMS HAVE ADOPTED NEW WORKING PATTERNS, EMBRACED NEW TECHNOLOGY FOR INTERNAL COMMUNICATIONS, TESTED FIRMS' AND MARKETS' OPERATIONAL AND LIQUIDITY RESILIENCE, AND ACCEPTED THE FLEXIBLE APPLICATION OF THE RULES FOCUSING ON OUTCOMES.

CHRISTOPHER BOND, CHARTERED MCSI, EDITOR, REGULATORY UPDATE, CHRISTOPHER.BOND@CISI.ORG

IMPACT ON REGULATORS

Regulators globally have been forced to react to firms using their business continuity plans and then, under the lockdown, most firms' staff working from home (WFH). They have also needed to support governments' strategies to limit redundancies and save firms and companies from insolvency. Both require adaption to the normal regulatory rules and their enforcement.

Here are some of the particular changes the UK's Prudential Regulation Authority and FCA have made:

- ▶ Extended the closing date for responses to open consultation papers and calls for input to 1 October 2020, such as the one on operational resilience, and rescheduled most other planned work.
- ▶ Scaled back the programme of routine business interactions, especially through meetings, so that they only contact firms on business-critical requests and responses to the current situation.
- ▶ Continued the expectation that firms act in the best interests of retail clients but with some flexibility, for example in money laundering checks for new clients, to ask clients to submit 'selfies' or videos, and to place reliance on due diligence carried out by others, such as the client's primary bank account provider, where appropriate agreements are in place to provide access to data.
- ▶ Accepted that sometimes it is not possible to record phone calls, but firms should inform the FCA and

explain what steps they are taking to mitigate the risk. This could include a retrospective review.

- ▶ Accepted that firms may not be able to submit their regulatory data, in which case the FCA expects them to maintain appropriate records and submit the data as soon as possible.
- ▶ Expected firms to take all steps to prevent market abuse risks, including enhanced monitoring, or retrospective reviews. The FCA will continue to monitor for market abuse and take any necessary action.
- ▶ Clarified that firms do not need to have a single senior manager responsible for their Covid-19 response. There are existing responsibilities specified in the Senior Managers Regime, for example SMF24 for operational resilience and SMF2 for financial resilience. The FCA has made a statement on key workers (someone who fulfils a role that is necessary for the firm to continue to provide essential daily financial services to consumers, or to ensure the continued functioning of the market). It recommends that SMF1, or the most relevant member of the senior management team, should be responsible for their approach to key workers. It accepts that senior managers' responsibilities may change temporarily without its notification, although there should be records. Equally, the '12-week' rule for temporary cover is extended to 36 weeks.
- ▶ Introduced flexibility over the requirement to notify the client if the value of the portfolio drops by 10%.
- ▶ Clarified that while government

schemes to help firms through this period can be used to help firms plan for how they will meet debts as they fall due and help companies remain solvent in the immediate period, they cannot be used to meet capital adequacy requirements, as they do not meet the definition of 'capital'.

- ▶ Warned firms and consumers to be aware of new types of scams.
- None of the above change the regulators' expectations of firms' conduct towards clients or ethical standards.

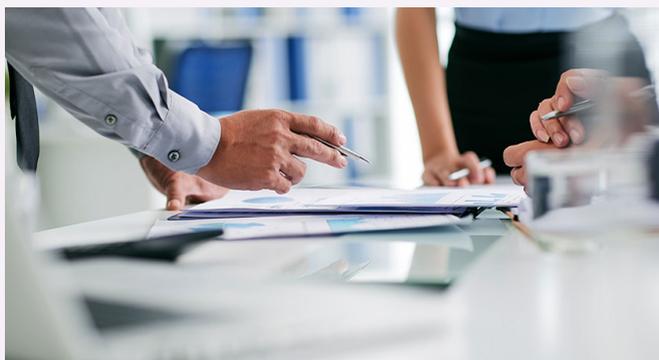
IMPACT OF HOME WORKING

Firms have had difficulties in continuing to work while transaction volumes have soared, as some clients have sold or reshuffled their portfolios and others have used market volatility as a selling or buying opportunity.

Firms have moved from using disaster recovery sites to most employees working from home. The FCA said on 27 March: "We expect the total number of roles requiring an ongoing physical presence in the office or business continuity site to be far smaller than the number of workers needed to ensure all of a firm's business activities continue to function on a business-as-usual basis."

WFH has thrown up many challenges for firms, including:

- ▶ illness of key staff
- ▶ deciding which staff to furlough or make redundant
- ▶ moving some remaining staff to new roles
- ▶ sourcing equipment (such as laptops and voice-recording devices) for home workers
- ▶ developing protocols for home workers
- ▶ managing communications with home workers
- ▶ enabling remote employees to execute trades – many firms had previously blocked this
- ▶ keeping adequate records of trades, investment decisions taken or advice given
- ▶ business communications with colleagues and central control
- ▶ loss of morale of isolated staff
- ▶ security of communications
- ▶ data protection issues from remote working, particularly on laptops and private computers
- ▶ timing of transaction reports



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- ▶ access to market and best-execution data
- ▶ increased authorisation to individual (sometimes junior) employees
- ▶ lack of senior management knowledge of what is happening, including positions taken and the liquidity position on a real-time basis
- ▶ reliance on outsourcing providers' business continuity plans and staff.

Reports from home workers have shown mixed reactions. Some responses include:

- ▶ slower broadband speeds
- ▶ working harder, since fewer breaks and no travel time
- ▶ frustration with new communications for meetings
- ▶ disorientation due to lack of landmarks during the day and no difference between home life and work
- ▶ loneliness as no face-to-face contact, and loss of self-esteem.

Office life will return for most staff. As one McKinsey commentator said in a *Financial Times* article from 30 March: "The social aspect of work and the sense of camaraderie is really important to a lot of people ... It makes what could be a grind quite fun. A lot of people are saying, 'I'm getting my work done but it's quite hard for it to feel meaningful!'"

TESTING OF MARKET INFRASTRUCTURE

Trading platforms, including exchanges for equities and bonds, have been stress testing their systems as required by the regulators since the 2008 global financial crisis. But none had expected a global lockdown. Consequently, there is

considerable relief and satisfaction that trading and clearing have continued so far with relatively few problems, without platforms having to shut down. In more detail:

- ▶ Executing trades and clearing them have proceeded smoothly to the relief of all, particularly given the market volatility and volumes.
- ▶ Automatic market supervision systems have continued to operate well.
- ▶ There are liquidity problems for some products, for example in money market funds and repo where some governments have stepped in.
- ▶ Fixed-interest bond exchange-traded

// THE SOCIAL ASPECT OF WORK AND THE SENSE OF CAMARADERIE IS REALLY IMPORTANT //

funds saw the extraordinary situation where secondary prices in some funds, such as BlackRock and Vanguard, were at a discount to net asset value,

despite daily dealing, until the Federal Reserve stepped in to act as a buyer of last resort, and some imposed a 2% redemption fee on frequent traders.

- ▶ Even before the pandemic, redemptions in some funds had been suspended, particularly in property funds where underlying assets take time to sell.
- ▶ Some unit trusts with illiquid, unquoted investments suffered sharp price falls in the market fall.
- ▶ Some exchanges' circuit breakers on transactions have been activated to ease the pressure on exchanges and prices.
- ▶ Major trade bodies are concerned about the rigour of exchanges in

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business continuity plans.

- ▶ There has been another blow to the few remaining physical markets, such as the London Metal Exchange and some US markets, since they could not operate with social distancing.
- ▶ Benchmark index updates, such as the S&P, have been delayed to avoid forcing index trackers to sell and buy large quantities of investments.

IMPACT ON PRIVATE WEALTH MANAGEMENT

This overlaps with the list of regulators' changes earlier. From the viewpoint of private wealth management (PWM) firms, here are a few of the sector-specific challenges they are facing:

- ▶ When and how to notify clients of the 10% drop in value of their portfolio. The FCA has said that firms may interpret this rule 'flexibly'. However, apart from the first notification, firms will still need to notify clients after the first drop in a standard three-month reporting period, and after any second drop after the start of the next reporting period. Many firms chose 1 April 2020 as the start date, so another notification was required if there were further 10% losses in April to June 2020.
- ▶ There have been discussions with the FCA on extending the supervision period before an adviser needs to achieve the required qualification.
- ▶ Firms such as larger asset managers that have made loans to clients against the value of their securities (so-called Lombard loans) have had to call in margin payments as the portfolio value has reduced. Failure to pay these can result in liquidation of the portfolio.

- ▶ Active investment managers hope their performance will compare favourably with passive products during the crisis because they are not obliged to buy investments automatically as passive product funds are.
- ▶ The UK government's loan scheme for SMEs could enable some PWMs to survive from a liquidity viewpoint. However, these government-backed loans will not add to prudential capital. The FCA has promised flexibility on capital adequacy for advisers; it is best to notify the FCA of any expected shortfall with the requirements.
- ▶ Trading volumes have increased dramatically under the crisis with very different views of clients. This has imposed an additional strain.

IMPACT ON INVESTMENT BANKING

This section covers a range of sell-side activities:

- ▶ A large increase in bond and equity trading by investment banks.
- ▶ An increasing use of banning short equity sales by regulators across Europe, as was imposed in the 2008 crisis by regulators including the Financial Services Authority (the predecessor to the FCA).
- ▶ The European Securities and Markets Authority made a statement on regulatory forbearance for the first period of reporting of securities financing transactions, such as repos, under the Securities Financing Transactions Regulation. FCA supervision of these will be delayed until at least 13 July 2020.

- ▶ Regulators are being asked to start the new rules on the capital to be allocated to derivatives transactions, particularly options, earlier than planned.
- ▶ The foreign exchange (FX) market has seen volatility. Some banks are finding it difficult to comply with the global code on FX while trading remotely or at home, or to monitor its compliance.
- ▶ There are stresses in the EU money market fund sector. One of the rating agencies (Fitch) has downgraded some funds to negative. This follows the problems with US money market funds where Goldman Sachs spent US\$1.9bn supporting its sponsored funds.
- ▶ The role of a prime broker to hedge funds has come under pressure. Many prime brokers have demanded collateral for their loans, or significantly increased the cost of funding, against their valuation of the hedge fund's underlying assets. This is critical since funds are often highly leveraged. Quant funds have suffered particularly since both equities and bonds dropped together.
- ▶ Hedge funds are used to look for opportunities to buy cheap assets in emergencies such as lockdown disruption. The German government has warned hedge funds against taking advantage of the market problems.
- ▶ Law firms are anticipating a wave of corporate insolvencies and gearing up those departments. One consequence of a default will be that non-bank lenders will lose their loans. Some hedge funds and investment banks are likely to suffer. If large enough, the government may be asked to help them. In this case, the regulators may finally decide to require non-bank lenders to have the same prudential requirements as banks (currently only deposit takers are treated as banks).
- ▶ The sharp decline in metals prices led to some huge margin calls by brokers on clients. It is too early to say what impact that may have on metals derivatives brokers.



Weathering the storm and mending the roof

The Covid-19 crisis has tested businesses' continuity planning to the limit. How well prepared have firms been for such an event, and how will their operations change in future as a result? cisi.org/weatherstorm

IMPACT ON COMMERCIAL AND RETAIL BANKS

Much of government and regulatory policy has been focused on helping SMEs survive with no or much reduced income. The high street banks are the natural channel for them to use. So, both have urged banks to fast track loans to,

and freeze repayments from, SMEs against an 80% government guarantee. The need is urgent, but the delivery is slow. This is caused by a variety of reasons, from the borrowers needing an investment-grade rating to banks demanding personal guarantees from directors through dislocation caused by home working of staff.

In parallel, the regulators have eased some prudential requirements on banks. These include:

- ▶ delaying or even scrapping the start of the new treatment of loan losses under International Financial Reporting Standard 9
- ▶ the same for the disclosure of climate-related risks due to start early in 2021
- ▶ relaxing the rules on monitoring trades so IT departments can focus on the smooth running of transactions
- ▶ cancelling the Bank of England (BoE) stress tests this year (granted)
- ▶ advising bank auditors to take a longer view of their accounts and to look through this crisis (granted)
- ▶ permitting banks to take a 'best efforts' approach to detecting money laundering and market abuse
- ▶ not penalising the lack of recording of phone calls from home-based traders and dealmakers
- ▶ more widely, Valdis Dombrovskis, the European Commission's vice-president for the euro and social dialogue, said the EU would delay the start of Basel III's requirements for which most EU banks will need to increase their equity (granted).

What is striking is that each country has made its own policy and regulations. The post-2008 global approach to regulatory changes under the Pittsburgh Agreement is disappearing fast.

IMPACT ON LISTED COMPANIES

The crisis has led to a sea change in regulation for listed companies. Here are some examples:

- ▶ The BoE has told UK banks and insurers that they should reduce or cut dividends and buybacks in order to protect the cash requirements of their business. This mood has flowed to other listed companies affected by the

economics of the lockdown. Research suggests that up to £52bn in dividends are at risk this year. The income of pension funds and insurance companies will be severely affected.

- ▶ The procedures for listed companies to raise new capital quickly by a placing rather than public offer are likely to be relaxed in the emergency to enable companies to survive.
- ▶ UK regulators have given companies and their auditors more time to provide information to investors on the effect

// RESEARCH SUGGESTS THAT UP TO £52BN IN DIVIDENDS ARE AT RISK THIS YEAR //

of the virus and lockdown on their businesses. This follows volatile markets from companies that made preliminary announcements. Companies have an

extra two months to publish their annual accounts – six rather than four. They need to take particular care in distinguishing between normal credit losses and ones caused by Covid-19.

- ▶ Some countries are tightening their takeover rules to prevent Covid-19-weakened companies, for example those in aviation, being taken over by foreign entities.

CONCLUSION

History will make its own judgement of the pandemic and the measures that governments and regulators took to manage it. History will also see some permanent changes resulting from it. Here is a personal list of some of them:

- ▶ Cash will disappear because of the contamination of notes and coins. Its use was reducing fast already – now it will never recover.
- ▶ The general arrival of the digital world, pushing recalcitrants to use it.
- ▶ The huge rise in government debt to help businesses and individuals survive

Ask the experts: Data protection while working from home

Iain Bourne, head of personal information and privacy at Grant Thornton UK, shares some insight on how to protect data while working from home.

cisi.org/data-wfh



the crisis will reduce the extent of the coming recession, but it will also saddle our children with a lower quality of life.

- ▶ The momentum behind the environmental lobby and change will decline as much borrowing capacity has gone.
- ▶ As governments print money, the public will lose confidence in government-controlled currencies and will increasingly turn to digital currencies outside government control.
- ▶ We have not seen the end of government borrowing. There is a lot of political pressure for more 'helicopter' money to finance a new European Marshall Plan.
- ▶ After the recession, inflation will eventually and inevitably return.
- ▶ A no-deal Brexit will become more likely as negotiating time shrinks.
- ▶ Some shops won't reopen after the switch to online buying.
- ▶ Aviation and foreign travel will take a long time to recover.
- ▶ Home working is here to stay, on a part-time basis.
- ▶ Supply chains will refocus and shorten within the same country given the national bans on imports put in place without consultation. Globalisation will slow for the same reason.
- ▶ A reverse in the trend of self-employment and zero-hours contracts (the gig economy) to the security of employment.

Views expressed in this update are those of the author alone and do not necessarily represent the views of the CISI.

BEYOND THE LOCKDOWN: BACK TO THE FUTURE

Time for reflection? Despite the bustling Microsoft Teaming and Zooming that has overtaken the corporate and financial – and many parliamentary – worlds during the virus crisis, there has been more time for reflection. ‘Reflective practice’, the process by which we analyse our continuing professional development activities, has become a cornerstone of the best-of-breed in lifelong learning. It is how you assess the benefit of the activities to your clients, your firm, and yourself, recognise strengths and weaknesses for self-improvement, and generate further ideas for personal and professional development.

The UK’s FCA set an important reflection ball rolling in 2018 when it began a programme on ‘purpose in finance’, to help firms identify their core reason for being, and how they can have a positive impact on society. The FCA’s Jonathan Davidson said then: “Consumer outcomes are driven by the purpose underlying a firm’s business model and culture. A firm with a good purpose will perform a stocktake of all their business activities and product lines and eliminate anything that is not consistent with their purpose, even activities that are profitable. Leadership is vital in ensuring a firm’s purpose is the right one and setting the tone for the rest of the organisation. Defining culture is much more than a box-ticking, compliance exercise.”

Now, in this time of the virus, the world is shifting on this front from the why to the how. In the 2019 Fortune 500 CEO survey – the apparent heartland of red-in-tooth-and-claw capitalism – only 7% believe their companies should “mainly focus on making profits and not be distracted by social goals”. While shareholder capitalism has delivered enormous progress, it also has struggled to address troubling issues such as climate change and income inequality. And round the corner come more challenges, notably the employment implications of artificial intelligence. (We cover key results from a recent survey of AI by Cambridge University’s Judge Business School and the World Economic Forum on the next page).

Professor Alex Edmans of London Business School has been at the forefront of thinking on purpose for many years, and his latest book, *Grow the pie*, assesses “how great companies deliver both purpose and profit”. In this issue of *Review of Financial Markets* (p.58), he outlines some of his key conclusions.

Andy Haldane, chief economist at the Bank of England, declared the book “superb ... it makes the case, compellingly and comprehensively, for a radical rethink of how companies operate and indeed why they exist. It is a tour de force.” Andrew Lo, professor of finance at the MIT Sloan School of Management, says of the book: “This is capitalism with a human face.”

Our distinguished Chartered Fellow Keith Robertson has thoughts nearer home in his masterly review of UK property prices, and their affordability, and what that means for family financial planning in the years to come (p.60). But a box-set of surprises arrived for me just before the virus set in, judging a competition amongst young financial professionals on what the future holds

// THE WORLD IS SHIFTING FROM THE ‘WHY’ OF PURPOSE TO THE ‘HOW’ //

for finance. The winning essay – on bonds for the ‘new normal’ – has turned out to be surprisingly

prescient as the world seeks clarity, energy and purpose in this dreadful corona year. Hats off to the two winners (p.64).

Resilience in these awful circumstances is important. But as a forthcoming series on CISI TV will demonstrate, longevity is vital. Resilience is getting through the day; longevity is getting through the decade. (Our poet-in-residence, Nigel Pantling, Chartered FCSI, takes an elegiac look a decade back on the next page at floor-based trading. Remember that?)

*George Littlejohn MCSI
Senior adviser, CISI
Editor, Review of Financial Markets
george.littlejohn@cisi.org*

ARTIFICIAL INTELLIGENCE TODAY: THE UPSIDES, THE RISKS

AI IS NOT THE FUTURE, BUT THE PRESENT DAY FOR MUCH OF FINANCIAL SERVICES. TWO FRESH SURVEYS PINPOINT THE OPPORTUNITIES – AND RISKS

According to *Transforming paradigms: a global AI in financial services survey* by the Cambridge Centre for Alternative Finance (CCAF) at Cambridge Judge Business School, and the World Economic Forum, AI is expected to become an essential business driver in the near term. Some 77% of respondents believe that AI will have high or very high overall importance to their businesses within two years and 85% of the surveyed financial firms have already implemented AI in some way. Nearly two-thirds (64%) of respondents expect to become AI mass adopters within two years, simultaneously using AI for revenue generation, process automation, risk management, customer service and client acquisition within two years, compared with a current figure of just 16%.

Some sectors will benefit more than others, at least in the short term. For example, it is expected to turn into a major driver of investment returns for asset managers. The technology gap between high and low spenders is widening as high spenders plan to further increase their research and development investments. These spending ambitions appear to be driven by more-than-linear increases in pay-offs from investing in AI, which are shown to come into effect once AI investment has reached a 'critical' mass of approximately 10% of R&D expenditure.

Fintechs appear to be using AI differently compared with incumbents. A higher share of fintechs tend to create AI-based products and services, employ autonomous decision-making systems, and rely on cloud-based offerings. Incumbents predominantly focus on harnessing AI to improve existing products. This might explain why AI appears to have a higher positive impact on fintech's profitability, with 30% indicating significant AI-induced increases in profitability compared with 7% of incumbents.



THE GROWING AI SKILLS GAP

A report in November 2019 by the Centre for the Study of Financial Innovation on the risks in AI identifies four specific skills gaps facing the purposeful deployment of AI, and at many different levels in organisations:

- **Talent gap:** There is an acute shortage of specialists who can design, develop, deploy, test and maintain AI systems – particularly of those who have knowledge of financial services.
- **Knowledge gap and unrealistic expectations:** AI systems could fail spectacularly if decision-makers who don't understand the technologies do not set appropriate expectations or give AI teams the right resources.
- **Over-reliance on AI:** Resources could be wasted on AI if it is implemented 'for its own sake', or if the people reliant upon it are unable to interpret or work with their outputs effectively.
- **Inadequate strategic alignment and governance:** Institutions that implement AI projects without restructuring their organisational hierarchy to reflect the new technologies expose themselves to risks from poor management and leadership.

CISI TV LINKUP

CISI members will find a programme on CISI TV featuring two of the lead authors of the Cambridge report, one of a series. Keith Bear, now a Fellow at the University of Cambridge, Cambridge Centre for Alternative Finance, was until recently immersed in the sector for two decades at IBM, where he was responsible for the strategy, business development, and large transaction development in the financial markets sector globally. His Cambridge colleague David Kruijff has over 20 years of global experience in the field of financial inclusion.

London Metal Exchange 2012

(i) The Trading Ring

Zinc is having its five minutes, dealers calling bids or offers for twenty five or fifty tonnes with settlement for tomorrow or two days' time. On their benches the dealers lean further forward, fingers jabbing prices, volumes across the ring. The clock's counting the seconds down as shouting peaks and the bell seals the session's end. Dealers laugh and settle contracts, the market moves to aluminium.

(ii) The Board Room

The walls are equatorial hardwood, hung with life-time achievement awards and trophies for consistent excellence. The management team sit like seers, debating the long-term implications of the expected incidence of contango, trends in kerb close-out for copper and the differing spreads to next December for nickel, cobalt and molybdenum.

Nigel Pantling, Chartered FCSI, our poet-in-residence, provides strategic advice to chief executives. nigelpantling.com

CAPITALISM IN CRISIS?

PROFESSOR ALEX EDMANS OF LONDON BUSINESS SCHOOL MAKES THE CASE FOR A RADICAL RETHINK OF HOW COMPANIES OPERATE AND WHY THEY EXIST



Alex Edmans is professor of finance at London Business School. His new book *Grow the pie: how great companies deliver both purpose and profit* is available at www.growthepie.net, from which these extracts are taken.

See Professor Edmans in action on CISI TV.

Alex Edmans
Professor of finance, London Business School
aedmans@london.edu

The consensus among politicians, citizens, and even executives themselves is that business just isn't working for ordinary people. It enriches the elites, paying scant attention to worker wages, customer welfare, or climate change.

Citizens, and the politicians that represent them, are fighting back. The precise reaction varies – Occupy movements, restriction of trade and immigration, and revolt against CEO pay. But the sentiment's the same. 'They', are benefiting at the expense of 'us'.

While radical calls to reform business drum up significant support, they risk throwing out the baby with the bathwater and ignore the crucial role that profits play in society. Profits are often portrayed as evil value extraction. But without profits, shareholders wouldn't finance companies, companies couldn't finance investments, and investments couldn't finance shareholders' needs. Shareholders aren't nameless, faceless capitalists, but include parents saving for their children's education, pension schemes investing for their retirees, or insurance companies funding future claims. Investors are not

'them', they are 'us'. So, any serious proposal to reform business must work for investors as well as society.

Viewing investors as 'them' and society as 'us' is an example of the pie-splitting mentality. It sees the value that a company creates as a fixed pie. Thus, any slice of the pie that goes to business reduces the slice enjoyed by society. Under this view, the best way to increase society's take is to straitjacket business so that it doesn't make too much profit.

The pie-splitting mentality is practised by many investors also. They think that the best way to increase profit is to reduce society's slice, by price-gouging customers or exploiting workers, and view a company that takes stakeholder welfare seriously as 'fluffy' and distracted from the bottom line. For example, Costco paid its employees almost double the national average (until its competitors recently increased wages). It also gives 90% of them healthcare – in part due to making part-time employees eligible after just six months of service. Costco is shut on all major US public holidays, even though they may be particularly profitable days for business, to allow its employees to be with their families. All these policies are expensive, and drive some stock analysts and investors crazy. An equity analyst, quoted in *Businessweek*,¹ lamented that "[Costco's] management is focused on ... employees to the detriment of shareholders. To me, why would I want to buy a stock like that?" Similarly, the title of a *Wall Street Journal*² article conveys the idea of a fixed pie: 'Costco's dilemma: be kind to its workers, or Wall Street?' The crucial word is 'or'.

But the pie is not fixed. The pie-growing mentality stresses that, by investing in stakeholders, a company doesn't reduce investors' slice of the pie. Instead, it grows the pie, ultimately benefiting investors. A company may improve working conditions out of genuine concern for its employees, yet these employees become more motivated and productive. A company may develop a new drug to solve a public health crisis, without considering whether

those affected are able to pay for it, yet end up successfully commercialising it. A company may reduce its emissions far beyond the level that would lead to a fine, due to its sense of responsibility to the environment, yet benefit because customers, employees, and investors are attracted to a firm with such values.

Under the pie-growing mentality, a company's primary goal is to serve society rather than generate profits. Surprisingly, this approach typically ends up more profitable than if profits were the end goal. That's because it enables many investments to be made that end up delivering substantial long-term payoffs. Now a profit-focused company will still invest in stakeholders – but only if it calculates that such an investment will increase profits by more than the cost of the investment. Comparing costs and benefits is how finance textbooks argue companies should decide whether to take an investment.

But real life isn't a finance textbook. In practice, it's difficult to calculate the future payoff of an investment. In the past, this was easier when investments were in tangible assets – if you build a new factory, you can estimate how many new widgets the factory will produce and how much you can sell them for. Most of the value of a 21st-century firm comes from intangible assets, such as brand and

// THE PIE-SPLITTING MENTALITY IS PRACTISED BY MANY INVESTORS, BUT THE PIE IS NOT FIXED //

corporate culture. If a company improves working conditions, it's impossible to estimate how much

more productive workers will be, and how much higher profit this greater productivity will translate into. The same is true for the reputational benefits of a superior environmental record. A company that's free from the shackles of having to justify every investment by a calculation will invest more and may ultimately become more profitable.

This new approach to business is the subject of my new book, *Grow the pie*:

¹ <https://hbr.org/2016/03/28-years-of-stock-market-data-shows-a-link-between-employee-satisfaction-and-long-term-value>

² <https://www.wsj.com/articles/SB108025917854365904>

how great companies deliver both purpose and profit. I wrote it out of concern for the polarisation between business and society that the world finds itself in. In the face of this conflict, this is a fundamentally optimistic book. This optimism is based on rigorous evidence that this approach to business works – for both investors and society – and an actionable framework to turn it into reality.

Let's turn to the evidence. The idea that both business and society can benefit might seem to be a too-good-to-be-true pipedream. However, rigorous evidence suggests that companies that treat their stakeholders well deliver superior long-term returns to investors. For example, one of my own studies (profiled in my TEDx talk, 'The social responsibility of business'), shows that companies with high employee satisfaction – measured by inclusion in the list of the 100 Best Companies to Work For in America – outperformed their peers by 2.3–3.8% per year over a 28-year period. That's 89–184% compounded. Further tests suggest that it's employee satisfaction that leads to good performance, rather than the reverse. Other studies find that customer satisfaction, environmental stewardship, and sustainability policies are also associated with higher stock returns.

Importantly, all of these measures of social responsibility are public information. So if the market were efficient, they'd already be incorporated in the stock price and investors couldn't make money by trading on them. But, because many investors have the pie-splitting mentality – believing that these measures are at the expense of shareholder value – they ignore them. I found that the 'Best Companies' – a list published by *Fortune* – quarterly profits systematically beat analyst expectations. This suggests that employee satisfaction improves productivity, but the market didn't previously take this into account and so underpredicted the Best Companies' earnings.

IMPLICATIONS FOR INVESTORS

I'll stress three points. The first is on the role of investors in business reform. As

mentioned previously, investors are often viewed as the enemy, extracting profits at the expense of society. One book claims that "Shareholder activists ... are more like terrorists who manage through fear and strip the company of its underlying crucial assets ... extracting cash out of everything that would otherwise generate long-term

// ALEX EDMANS' SUPERB BOOK MAKES THE CASE, COMPELLINGLY AND COMPREHENSIVELY, FOR A RADICAL RETHINK OF HOW COMPANIES OPERATE AND INDEED WHY THEY EXIST //

**ANDY HALDANE,
CHIEF ECONOMIST,
BANK OF ENGLAND**

value", and politicians in both the UK and US have made proposals to restrict investor rights. But such views aren't backed up by the evidence. Rigorous studies show that, while shareholder activism does indeed

increase profits, this doesn't arise from pie-splitting but pie-growing – improved productivity and innovation, which in turn benefits society. So any repurposing of capitalism should place investor engagement front and centre, as the new UK Stewardship Code is aiming to do.

The second is on the role of ESG (environmental, social, and governance) factors in investment decisions. ESG investing is often viewed as a niche area, only to be pursued by investors with an explicitly social mission, under the view that social performance is at the expense of profits. Instead, integrating these dimensions is good practice for all investors, including those with purely financial goals. Good companies aren't always good investments. If a company is good, and everybody knows it's good, then an investor pays for what they get. It makes no sense to buy Facebook because it's a leader in social media – everybody knows this, so its shares are expensive. A good investment is a company that's better than everyone else thinks. Stakeholder capital is a prime example of such hidden treasure: It ultimately leads to profits, but the market doesn't realise this, due to the pie-splitting mentality.

The third implication is more nuanced. While ESG investing isn't at the expense of profits, it's important not to go too far

the other way, like some ESG advocates who claim that ESG investing is a panacea. A *Financial Times*³ article argues that "The outperformance of ESG strategies is beyond doubt" and a leading UK broker recently claimed that "study after study has shown that businesses with positive ESG characteristics have outperformed their lower ranking peers". These claims are often accepted uncritically, given confirmation bias – the temptation to take 'evidence' at face value if it confirms what we'd like to be true. But only certain types of ESG factors are linked to superior financial performance. The ones that are founded on pie-growing. Some ESG investing is based on pie-splitting – the idea that a responsible company is one that doesn't give too much profit to investors (or executives) and instead redistributes it to stakeholders. Indeed, some ESG investors use CEO-worker pay ratios as a criterion, believing that too high a ratio suggests that the CEO is taking too much of the pie from workers.

But the evidence suggests that pay ratios are positively correlated with long-term stock returns. Instead, pay reform should be centred around holding the CEO accountable for growing the pie. This depends not on the level of pay but its structure. If the CEO holds a substantial chunk of equity, they're only rewarded if the pie grows; if it shrinks, so does their wealth. Research finds that companies with high CEO equity ownership outperform those with low CEO equity ownership by 4% to 10% per year. Further tests suggest that high CEO ownership causes firms to outperform.

Business needs to be reformed to regain the public's trust. But the reforms don't involve regulating companies to make them less profitable. Instead, CEOs and investors must take their responsibility to stakeholders seriously and seek to create profits only as a by-product of serving society, rather than through exploiting customers, employees, and the environment. Creating social value isn't simply 'worthy' – it's good business. The highest-quality evidence, not wishful thinking, reaches this conclusion: To reach the land of profit, follow the road of purpose.

³<https://www.ft.com/content/9254dfd2-8e4e-11e7-a352-e46f43c5825d>



Introduction to ‘The foundations of property’

Keith Robertson writes:

I set about writing ‘The foundations of property’ in autumn 2019, after leaving London and returning to my Borders roots in north Northumberland. It was intended to be the first in a series of essays reflecting my views and observations of our sector – in particular, investment, risk and retail markets and the people involved. This first article (opposite page) was prompted by the unavoidable realisation that the distortion in London property prices does not indicate that capitalism is working well but rather, that its name is used to justify personal greed at the expense, potentially, of a safe and stable society.

Within my working life there, from 1972 until 2019, buying a home went from being affordable for virtually anyone in stable employment to unaffordable for virtually everyone without a six-figure salary. Council and housing association rents, if you can find one or wait long enough to move up the list, are at levels that make long-term capital accumulation almost impossible. The Office for National Statistics (ONS) data bear this out. Mortgage lending criteria have varied a bit over the years, becoming criminally distorted by 2007, but broadly have remained at about three to five times earnings. This average 3x-5x earnings ratio has pretty much defined the average house price regionally since the 1920s; prices have always been higher in London and other hotspots, but so too have earnings there.

In the past 25 years, however, prices and affordability ratios in London have increased grotesquely for the reasons I describe in the article. The result has been that even moderately well-paid professionals like teachers, solicitors (outside the City’s ‘magic circle’), police, local administrators, let alone the masses of care workers, nurses, firemen, transport workers, and other essential workers that keep the city going, have been completely priced out of anywhere even half decent to live within

reasonable travelling distance of their workplace. I believe this has huge implications for the future working of London and any city that cannot house its key workers in decent accommodation reasonably close to their workplaces. My proposed solution is radical and intended to provoke readers in financial services into thinking critically about these issues. The chart shows not only how the price of property has increased over the decades, but that long-term affordability ratios have been blown out of the water, and the unaffordability of London continues to widen even as we demand key workers turn up to keep our hospitals running.

Between writing and publication, Covid-19 has hit the world and here the NHS has been responding as we have come to hope and expect. But London’s hospitals desperately need more trained staff at all levels, right down to the humble cleaner. This crisis will not be over by June, or by June 2021. We are in a new age of trans-species viral mutations, many originating in areas of intensive animal production and crowded markets, mutating from avian and porcine species and crossing readily to humans with poultry, pigs, even bats acting as vectors. SARS, MERS and Covid-19 are all from the coronavirus family. It is a racing certainty that as the human population approaches eight billion (it was about two billion when I was at school) these phenomena will also grow exponentially.

There are more fundamentally important things to think about than whether there will be a V-shaped recovery in the stock markets. Among the many economic, political and social lessons that will have to be learnt over the next few years will be the simple question of who and what matters to us in a crisis, and what needs to be made to happen to ensure that at least our doctors, nurses and other key workers can afford to live close enough to look after us all.

THE FOUNDATIONS OF PROPERTY

KEITH ROBERTSON, CHARTERED FCSI, CASTS HIS EAGLE EYE ON PROPERTY, AND WHAT IT MEANS FOR OUR SECTOR'S CLIENTS, FROM HIS EYRIE IN THE FAR NORTH



Keith Robertson, Chartered FCSI, is a highly qualified practitioner who has spent over 20 years as a practising fee-charging financial planner and investment manager. He continues to sit on the CISI level 7 exam panels and forum committees.

Keith Robertson
AF Consulting
keith@afconsulting.london

I've never thought myself a retiring sort of chap, yet here I am – retired, sort of. I now live as far away from London as is possible without technically emigrating. Things look different from here.

We live in a dead-end village. The road stops a couple of hundred metres past our house. Then the only options are to continue along a cliff path by bike or on foot, or swim. I walk. Our house is a source of joy and pride, but is also an embarrassment. It's joyful because it is wacky, built in the 1870s by the local monumental sculptor who took time off from carving gravestones, sarcophagi and guardian angels to do a bit of property development on the side. But once a stone carver always a carver: the wrist action becomes ingrained, one supposes. Built of the local sandstone, the entire visible exterior has been laboriously and deeply carved with a fish scales design and, at every corbelled floor level, busts of the good and the great of the era. So far we've identified an austere Victoria and Albert, pensive Dickens, lyrical Burns and Walter Scott (how did people manage to read him?) among others. There are pelicans rampant standing sentry at the corners, and we found a spare griffin (lizard in mouth) guarding the top of the garden as we trimmed back the brambles. Inside, the ornamental cornices and roses show just how awesome plasterers could be when plastering was a truly skilled trade.

The embarrassment comes because we discovered we paid the highest-ever price for a house in our village, not what we wanted to become known for. But the truth is that our 11-room semi, with high ceilings, phenomenal plasterwork, ornamental staircases and every window shuttered, cost palpably less than a one-bedroom flat where we lived in London.

Of course, house prices have always varied, across the UK and within each urban area. There have been obvious long-term trends of regional decline, as in old heavy industrial areas now semi-derelict. Improving infrastructure and transport (or the opposite) have changed where people live relative to their place of work, everywhere. However, in the past 30 years there has been one gigantic aberration: the explosion of prices in the south-east and London in particular. Something has gone askew. Since the growth of mass owner-occupied homes started after WWI, there has been a remarkably stable long-term relationship between the average price of houses and affordability, measured as a multiple of average income. Across the UK this has been more or less constant in the range of three to five times annual earnings, recognised forever by prudent mortgage lenders. OK, average earnings and multiples have always been higher in London, but not dramatically. Today an 'average' property sells for between 8 and 15 times 'average' London earnings. I'll return to this issue.

There are other ways of measuring what is, in effect, a fundamental valuation of residential property. One is the yield, or notional yield, one could get by letting property. This was another constant: roughly a premium of 5% over the benchmark ten-year gilt. This yield premium reflects the greater risks and overheads involved in letting residential property. Thus, in historically 'normal' times with gilt yields of say 4–6%, if you could buy property which would generate rental income of 10% gross,

you would be paying a fair price. If you bought at a higher expected yield, other things being equal, you were buying a bargain. Less, and you might be overpaying and would need to rely more on future capital gains for your return. With the benchmark gilt today offering round 0.5% one should, on this measure, be looking for a yield of 5–6%. Many London letting properties today sell at a half or even a third of that yield.

ASSESSING FAIR VALUE

My favourite fundamental valuation metric, Tobin's q ratio, can also be used to assess a fair value for property. Basically, q looks at the replacement value of an asset and compares how that relates to the open market price. This can be particularly helpful when applied to equity markets, the S&P 500 being the benchmark, but the principle can be applied to anything. In the US, when Tobin's q is applied to residential real estate on data since 1900, it shows a virtually flat line all the way till about 2006 when there is a marked blip upwards for a couple of years or so, reflecting the sub-prime scandal. It has now returned to flatline 'normal'.

Other things being equal, this pattern ought to be the same in the UK, but it decidedly is not. That is because other things are not

// TODAY AN
'AVERAGE' PROPERTY
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EARNINGS //

equal. The foundation of property pricing is the price of land, and the US has lots and lots of that; the UK does not. There are many good reasons for restricting where people may build houses in the UK, in parts a densely populated country – south-east England in particular. These are policy issues, and for 50 years and more, political will has been firmly for protecting green belts. London created a green belt before WWII and they became national planning policy in the 1950s. There is no doubt that green belt policy has resulted in inflation in urban land

prices so that land now accounts for more than 70% of the cost, compared with around 25% in the 1950s.

WHAT'S BEEN GOING ON?

But there have been other policy failures going on in London, particularly in the past 30 years. When I bought our four-bed London Georgian terrace house in 1977 in Stoke Newington, it cost £26,650, pretty much four times my earnings of £6,500 at the time: probably an 'average' graduate income after five years in the City. My then next-door neighbour, Andrew, had bought his for under £6,000 in the mid-1960s after coming over from Jamaica and working on the buses for ten years. The point is that London property was generally still affordable on long-term average multiples of earnings and some earnest saving. What's been going on?

In 1980, then housing minister Michael Heseltine introduced Right to Buy as part of the Conservative Party's radical Popper-inspired libertarian reforms. There was social purpose as well as political (tenants who could buy were more likely to vote Tory thereafter). There is something fundamental in owning one's own home, with all the connotations that go with that. It provides a place of stability to bring up a family, physical and financial security, and is the social and psychological bedrock of modern living. Originally, the objective was to recycle the social housing stock, with local

councils continually using receipts from sales to build new social housing, thereby providing a route for poorer people to have a stake in the economic growth of the country. Simultaneously, councils could upgrade their new builds. Politics intervened: a cabinet reshuffle allowed then prime minister Margaret Thatcher to move Heseltine out of the way to defence and reverse the reinvestment part of Right to Buy so that councils were expressly prohibited from using all the receipts. Instead of the stock of social housing expanding and modernising in a virtuous cycle, this resulted in a steady reduction in total numbers of available houses and flats, about two million dwellings by now, forcing up prices.

The Thatcher era also brought in Big Bang, creating a massive expansion of the City that continued until Brexit. Large central government subsidies enabled London's infrastructure and public transport systems to become world beaters and helped make London one of the most economically vibrant and attractive cities in the world.

Around this time and into the Blair decade, political philosophy changed and allowed the notion of the power of markets to infuse the Establishment's thinking. Under this way of thinking, governments would need only to provide the right conditions and

capitalism and competition would provide the most 'efficient' way to deliver solutions to anything. Accordingly, governments have put out the welcome banners, devalued sterling and opened the doors to anyone who wants to come here to do business. And have they come? Emphatically yes, at least until Brexit, but not exclusively to

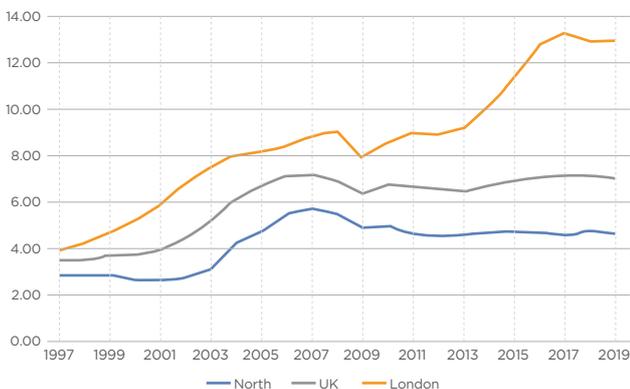
create economically productive new businesses. It seems irrefutable that a significant part of

// THE POLICY HAS PRICED OUT ALL MODESTLY PAID KEY WORKERS AND MANY RELATIVELY HIGHLY PAID PEOPLE //

London's (and the surrounding region's) old and new-build housing has been snapped up by overseas buyers, for whom sterling assets looked cheap. In my view this has been an incalculable public policy error.

The mistakes and their consequences are egregious and threefold. First, economically illiterate politicians have assumed any foreign money being invested in the UK is a good thing. Second, buying (and selling) property has no productive economic function. Third, and most important, the policy has priced out all modestly paid key workers and many relatively highly paid people. If a city-state with an economy the size of London cannot house its teachers,

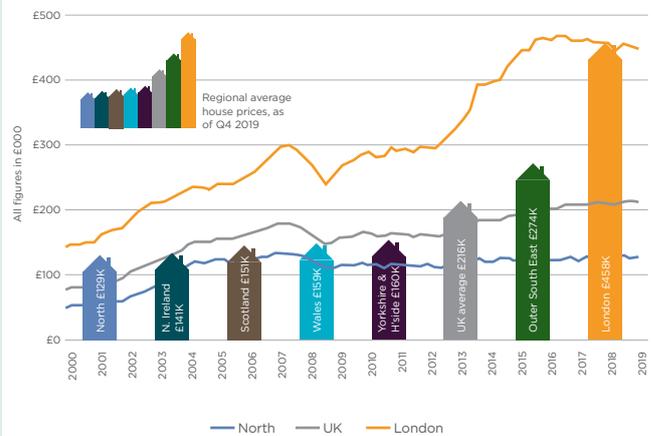
TABLE 1: UK LOWER-QUARTILE HOUSE PRICES VS LOWER-QUARTILE INCOME 1997-2019*



*Ratio of lower-quartile house prices to lower-quartile gross annual (where available) workplace-based earnings by country and region, England and Wales, 1997 to 2019.

Source: ONS

TABLE 2: UK REGIONAL PROPERTY PRICES



Source: Nationwide

nurses, street cleaners, bus drivers and emergency service workers because they've been priced out of renting, let alone buying, somewhere to live close enough to their jobs, sooner or later something catastrophic will happen.

Foreign inward investment is desirable if, and probably only if, the investment is directed to long-term economically productive ventures that boost UK growth. Those create profit and employment, adding to people's incomes and to the Treasury's tax receipts – a genuine virtuous cycle. To open our doors to anyone with money and sell them core capital assets, which are desperately needed to keep our cities and services running, is not helping anyone who lives here. All this policy has done is lead to massive inflation in residential property, pricing out of the market the very people needed to make the whole system work. This is unacceptable.

CLEAR THINKING REQUIRED

Capitalism is about applying capital for productive economic purposes for the greater benefit of the society we live in. Buying and selling property in itself has zero productive economic function, like collecting or dealing in art, wine or classic cars. Any personal profit is merely at the expense of someone else; nothing new has been created in the system. As Mayor of London, Boris Johnson used personal powers to override council planning decisions, and some 400 tower blocks are in the process of being built. Even if we don't care about what London actually looks like or whether it is pleasant and easy to work in, we already build the smallest dwellings in Europe (in square feet per occupant) even as the price for these rabbit hutches soars out of reach of any average earner.

We need to think clearly about what it is that makes a city work and be a provider of jobs. Above all, it is having people living there to fill the jobs and contribute to a growing economy. As council housing and housing association stocks are sold and not replaced, and as land is scarce without a blitzkrieg on the green belt, common sense dictates we need to ensure our key workers have somewhere suitable to live, and in priority to allowing just

anybody to buy up properties because they can make a fast buck – as has happened for the past 25 years or more. All this does is create a mega-class of rentiers whose sole purpose in buying is to push up capital prices and rents to enrich themselves. Such parasitism needs to be stopped in its tracks and replaced with rules that favour those who live and work in a city.

Taking New Zealand as a model, we should not allow anyone to buy property here unless they are resident in that property. New sales should be banned. Any individual or corporate entity that owns residential property that they do not personally occupy should be significantly taxed annually on its capital value, with a rider that rents cannot be increased to cover the cost. If offshore owners hide inside complex trust and corporate structures then, with notice and due process, laws should be enacted to allow legal sequestration.

Landlords who own historical portfolios of houses and flats can be tested against criteria including how long they have been in business and how fairly their tenants have been treated. New entrants to the letting market should be blocked for the time being. Formally controlling rents in the private sector appears to be counterproductive, so excess properties should for the time being be taken into public ownership to be let at fair rents. This is not anti-capitalist or xenophobic; it is a rational response to rich people and corporations taking advantage of a

// RETURN TO EQUILIBRIUM A MARKET THAT HAS BECOME DANGEROUSLY AND OBSCENELY SKEWED //

shortage of residential property and excluding those at the bottom of the ladder. Speculative buyers could be welcome to invest in any part of the productive capacity of the UK economy, but residential property must be considered a special case and ring-fenced until homes once more become affordable on historical multiples. In any area where there is a shortage of affordable property, there is no need for any person to own more than one home.

The aim must be radical, not to ban people from ever owning property in our cities or countryside for investment purposes, but to return to equilibrium a

market that has become dangerously and obscenely skewed. The outline suggested will gradually persuade rentiers that the game is not worth the candle and properties will come back on to the market. This will gradually lower property prices in real terms and one day they will return to levels where an average person can buy an average property at average multiples of average earnings near where they work. A second home might be possible in rural areas or towns, but this could be controlled by licence depending on local demand and vacancies until first-time buyer demand and supply is in equilibrium.

There would be some severe collateral consequences for this policy over the short to medium term. Recent purchasers (perhaps using the bank of mum and dad) would see the value of their home fall but, using Tokyo's experience in the late 1980s as a model, this phase might last a decade and half the value of property in real terms, but then a recovery towards long-term average valuations would rebalance each market towards normality. This would be painful, but a necessary lesson would be learnt: market cycles are normal and nothing keeps just going up forever.

VIEW FROM THE COUNTRY

If we want to live in a decent society with good services and security, then we must ensure that every member of that society can have the chance to own or rent a decent dwelling without prices being distorted by speculative predatory investors. Having somewhere affordable to live in order to work should be enshrined as a basic right. Imagine if such legislation were introduced in every country: no more than one residential property per person or family group until there is a clear surplus of dwellings over demand. Nobody would be worse off; nobody can live in more than one property at a time. Rich people can spend their money on other things, hopefully invested in economically productive instruments. One person's greed should not cause multiple others to be priced out of a fundamental necessity. If such legislation became universal, minds and money could be focused on genuinely useful and productive ventures, rather than fuelling the next bubble.

Things look different from upcountry.

POST-NORMAL BONDS: FINANCIAL INSTRUMENTS FOR A SUSTAINABLE ECONOMY

YELENA MUZYKINA AND YELENA NOVIKOVA CONSIDER THE DEVELOPMENT AND DEPLOYMENT OF NEW TYPES OF FINANCIAL INSTRUMENTS TO HELP PROMOTE A NEW WORLD ORDER IN FINANCE



Yelena Muzykina is an assistant director at the Qazaq Research Institute for Futures Studies.

yelena.muzykina@narxoz.kz



Yelena Novikova is an independent expert, contributor and public speaker.

yelena.novikova@hotmail.co.uk

1. INTRODUCTION

The need for a change in the current pattern of global economic development has been building for decades. By the end of the 20th century, several high-profile international organisations had voiced support for switching from single-indicator analytics that proved sustainability based only on economic growth data. In May 1990, the United Nations Economic Commission for Europe (ECE) raised the issue of the environment and its safety for future generations during the Bergen Conference on Sustainable Development, attended by environment ministers from 34 countries and the EC Commissioner for the Environment (United Nations Information Unit on Climate Change, 1993). Over time, it became increasingly apparent that the idea of sustainability should transcend material concerns and embrace a variety of factors, including quality of life and health, environmental efficiency, strength of communal relationships, fullness of participation in society, and others.

The need for broadening the variables for defining sustainability has become even more acute within recent years, a period that has been defined as 'post-normal times' (PNT) (Sardar,

2010). International society, including the global economy, has changed significantly, and it is necessary to establish new norms, conventions and rules.

This paper aims to discuss feasible contributions to this process in Kazakhstan, a country that lies at the centre of the Belt and Road initiative. With a belief that green finance and Islamic finance instruments can play a critical role in the post-normal Kazakhstani economy, the discussion focuses on financial instruments that we dub 'post-normal bonds', whenever we need to emphasise its relevance to post-normal times framework.

We feel obliged to clarify up front that, to this effect, post-normal bonds are bonds that can effectively address the complex and contradictory needs of post-normal times and economy. That said, the primary focus of this paper is a specific type of post-normal bond that can otherwise be called a 'green sukuk hybrid'. In fact, for the purposes of this discussion 'post-normal bonds' and 'green sukuk hybrids' are used interchangeably.

A green sukuk hybrid, in its turn, can be defined as a participatory proportional ownership instrument, a pledge against existing or future cash flow from the assets

used to finance and refinance projects when partners take risks, share profit and loss, and comply with the principles of the International Capital Market Association (ICMA) and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI).

We seek to show how this approach merges the best aspects of green bonds and sukuk, thus addressing the challenges of surviving and flourishing in a post-normal (PN) economy.

2. AMBIGUITY IN SUSTAINABILITY OF CONVENTIONAL BONDS

We first consider how different types of bonds fit into the PN context. Lord Mervyn King, a former governor of the

Bank of England, calls the world we are living in a "world of radical uncertainty" (King, 2017, p.136). This highlights that the risks being faced today cannot be defined precisely in the financial world. Expanding on King's idea, radical uncertainty is the key to understanding not only financial markets themselves (2017, p. 140), but also the overall character and dynamics of the PN and post-truth world that are mirrored by the economy.

Ziauddin Sardar, the founder of PNT theory, identifies three primary features of PNT (Sardar, 2019, pp.6-7). The first of these is the extreme interconnectedness of everything in the globalised and networked world. This feature can lead a local event to transform into a global-scale disaster. The rapidity with which this can happen constitutes the second characteristic of PNT. Arising from the elements of speed, scale and scope, the third trend highlighted by Sardar is simultaneity: "This is how we now have to see our world: as an interconnected, networked

system, where things accelerate quickly, often simultaneously, and become global in scale." (Sardar, 2019, p.6.)

In addition to

the '4Ss' mentioned above, other essential features of PNT include the '3Cs' (Sardar, 2019, p.9):

- C1 – *complexity* reflected in multiple ways and employed by interconnectedness, interdependency and networking;
- C2 – *contradiction* that peeps out around us in all sorts of inequality and a simplistic approach to problem-solving of complex issues; and
- C3 – *chaos* that springs up when "glaring contradictions and complexity come together".

The critical question for PNT is how to address the challenges arising in this global context. Sardar answers: "We

// A LOCAL EVENT CAN QUICKLY TRANSFORM INTO A GLOBAL-SCALE DISASTER //

must never lose hope and do our utmost to nurture positive, sustainable and life enhancing change” (2019, p.14). To achieve this, people must navigate PNT through the following means, summarised from Sardar’s discussion (2019, pp.15–18):

- Work on alternatives that can battle uncertainty.
- Consider multiplicity and inclusivism to cope with complexity.
- Encourage creativity as the best alternative to precise ‘mathematical’ methods.
- Uplift ethical values (modesty, accountability, humility and community) that connect with knowledge and question technological advancements.
- Promote polylogues to create spaces for multiple perspectives, logics, voices and existences, in order to achieve a new synthesis.

Overall, it is suggested that only new syntheses and knowledge can help humanity to address the wave of uncertainty and build a sustainable life in PNT. Therefore, the PN economy requires new instruments that comply with the prerequisites mentioned above.

It is clear that conventional bonds are losing their position in the PN economy and are not necessarily sustainable. This is due to a number of factors:

- Bonds are debt instruments that generate income primarily for the bond issuer, thus promoting financial (and social) inequality.
- They emerged in times when Western culture and morality were predominant; therefore, their role is increasingly being questioned and contested.
- They prioritise interest payments within a ‘get-it-at-any-cost’ ethical framework.

While traditional bonds still serve some purpose as instruments within the global economy, the current situation requires stronger complementary alternatives. Among the potential options are green bonds and sukuk, both of which are designed to contribute towards sustainability. The key characteristics of both include:

- Combination of tangible and intangible values to move from a greed-based to a PN economy.
- Focus on specific projects.
- Assets-based nature.

TIMELINE 1: BRIEF HISTORY OF SUKUK

1988	Fiqh Academy of the Organization of Islamic Cooperation legitimised the use of sukuk
1990	Malaysia Shell MDS Sdn Bhd issues the first modern sukuk
1991	Establishment of Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)
2003	AAOIFI publishes a standard on ‘investment sukuk’
2005	World Bank issues its first Islamic bond amounting to US\$200m
2014	The International Finance Facility for Immunisation issues the largest supranational entity debit sukuk
2017	Malaysia launches the world’s first non-sovereign green sukuk
2018	Indonesia sells the world’s first sovereign green sukuk

- Third-party verification.
- The credibility of a borrower as the key to success.
- Increased focus on social and environmental responsibility and performance.
- Facilitation of multi-faceted financial inclusivism.
- Reliance on universal human values rooted in spiritual traditions (such as those presented in the Bible for Christianity, or the Qur’an for Islam).

These are the characteristics of green bonds and sukuk that align with environmental, social and governance (ESG) factors that are applied to set standards for socially conscious investors in order to create a positive net sustainability impact.

We will now discuss how the global situation is reflected in the context of Kazakhstan.

3. NEW TYPES OF BONDS IN THE KAZAKHSTANI ECONOMY

Green sukuk hybrids establish a middle ground between the green bond definition offered by Astana International Exchange (AIX) in its regulations (2019, p.129) and the definition of sukuk given by the AAOIFI (Afshar, 2013, p.47).

3.1. ‘Embryonic’ development of green bonds and Islamic bonds

According to Thomson Reuters’ *Islamic finance development report 2018* (Mohamed, Goni and Hasan, 2018), the Islamic finance sector is growing at an impressive rate: while the total value of Shariah-compliant assets in 2003 was US\$200bn, it had reached US\$2.44tn by 2017. The banking sector is gradually responding to the demand of Islamic lenders: during the decade 2003 to 2013, sukuk bond

TIMELINE 2: BRIEF HISTORY OF GREEN BONDS

2007	The European Investment Bank issues the first green bond
2008	The World Bank issues its first green bond
2010	Climate Bond Initiative creates the first Green Bond Standard
2012	African Development Bank issues green bonds to finance climate change solutions in Africa
2013	Credit Agricole becomes the first issuer of corporate green bonds
2014	Green Bond principles released and endorsed by the ICMA
2015	Agricultural Bank of China becomes the first Chinese entity to release green bonds
2018	Poland becomes the first sovereign issuer of green bonds
2019	Green bond issuance surpasses the symbolic benchmark of US\$200bn

TIMELINE 3: BRIEF HISTORY OF SUKUK IN KAZAKHSTAN

1992	Al Baraka Bank (Pakistan) opens its branch in Kazakhstan
2011	Kazakhstani government develops legal framework for Islamic bonds
2012	Kazakhstan develops 41-step 'Roadmap for development of Islamic Finance by 2020'. The development Bank of Kazakhstan issues its first sukuk at Malaysian stock market
2015	Kazakhstan introduces amendments to address Islamic insurance, leasing, sukuk and Islamic banking system
2016	Kazakhstan launches its first sovereign sukuk
2017	AIFC launches its Islamic Finance Rules
2019	Astana International Exchange adopts AIX Business rules that include Islamic finance section

issuances rose twentyfold to reach a value of US\$120bn (World Finance, 2019). A brief history of modern sukuk can be visualised as presented in Timeline 1, p.65.

Green bonds were launched as a niche product just a decade ago by multilateral institutions such as the World Bank and the European Investment Bank. In November of 2019, the green bonds market reached the milestone value of US\$200bn (Climate Bonds Initiative, 2019).

A brief history of green bonds is presented in Timeline 2, p.65.

3.2. Synergy between green bonds and Islamic bonds in Kazakhstan

In Kazakhstan, the history of Islamic bonds began in the 1990s and overlapped with the green bonds' launch in the 2010s, including the significant events outlined in timelines 3 and 4 on this page.

As the graphics on this page demonstrate, the development processes of sukuk and green bonds in Kazakhstan have moved in parallel, with some effort required to synergise them. Astana International Finance Centre (AIFC) and AIX are examples of financial market players taking such steps.

4. WHEN TWO BECOME ONE

4.1. AIFC develops rules for taxonomy of post-normal bonds

Both green and Islamic finance are so crucial for the development of the AIFC that president Nursultan Nazarbayev's foreword to the 2019 Annual Report of the AIFC highlights them as two

strategic pillars (AIFC, 2019, p.9).

However, the development and distribution of Islamic finance have been more noticeable in contrast to green finance to date, both across Kazakhstan in general and at the AIFC in particular. This is also indicated by the floor plans of AIFC properties. Nevertheless, overall, these financial innovations seem to follow similar patterns, albeit with some element of delay.

The first mention of Islamic finance within the context of the AIFC dates back to the Islamic Finance News Forum hosted by the AIFC in 2017. Kairat Kelimbetov took on the office of governor of the Islamic Development Bank (IsDB) Group for Kazakhstan in March 2017. In contrast, the AIFC did not adopt its green finance concept and strategy until November that same year.

Due to a mix of logistical, historical and developmental reasons, a similar pattern applies to the speed with which

// THE GREEN BONDS MARKET REACHED US\$200BN IN NOVEMBER 2019 //

the AIFC was able to secure Islamic finance talent, as opposed to the acquisition of green finance talent.

The AIFC's Bureau for Continuing Professional Development (BCPD) is currently offering a wide variety of Islamic finance qualifications:

- The Islamic Finance Qualification from the Chartered Institute for Securities & Investment
- The Bahrain Institute of Banking & Finance Advanced Diploma in Islamic Finance
- Professional Certificate in Islamic Finance
- Certified Islamic Professional Accountant - flagship qualification of AAOIFI.

Since 2019, the BCPD has also offered the only Chartered Banker Institute's Green Finance Certificate (distributed by the CISI).

Similarly, a justifiable asymmetry exists in terms of the advisory infrastructure at the AIFC. While the AIFC does have an Advisory Council on Green Finance, consisting of four

high-profile members including the governor, there are multiple advisory councils available for

Islamic finance. Among these are:

- AIFC Advisory Council on Islamic Finance (ten members)
- AIFC Central Shariah Advisory Board (five members).

As one might expect, the AIFC's goal of achieving a higher level of symmetry between the development of green

TIMELINE 4: BRIEF HISTORY OF GREEN BONDS IN KAZAKHSTAN

2013	Kazakhstan adopts national concept policy on green economy
2015	KASE signs agreement with Sustainable Stock Exchanges Initiative
2016	Voluntary methodology for ESG reporting is released at KASE
2017	AIFC develops the national concept policy on 'Transition to Green Financial System'
2018	Kazakhstan-2025 strategy to align with nationally defined contributions
2019	Astana International Exchange adopts AIX business rules that include green finance section; KazPV announces its intent to issue Kazakhstani first green bond

and Islamic finance approaches is particularly noticeable upon examination of its relationships with various international networks and institutions.

The AIFC's membership in Islamic finance networks and institutions includes:

- Member of the Islamic Finance Services Board
- Member of AAOIFI
- Member of the General Council for Islamic Banks and Institutions
- IsDB Governorship in Kazakhstan.

Meanwhile, the AIFC's membership in green finance networks and institutions includes:

- Member of the International Network of Financial Centres for Sustainability
- Member of the Green Finance Committee of the Asian Financial Cooperation Association
- Formal partner of the Climate Bonds Initiative
- Formal Partner of the Centre for the Fourth Industrial Revolution of the World Economic Forum
- Member of the Green Principles of the Belt and Road Initiative.

Overall, while asymmetry does exist in the AIFC's readiness for scalable green and Islamic finance innovation, this does not mean that green finance does not play a critical role in the brand positioning of the AIFC as an international/regional financial hub. The AIFC has already developed a framework for the 'Green Financial System for Kazakhstan', including multiple project components that focus specifically on green bonds.

Although the AIX has already developed a set of rules for green bonds issuance (AIX, 2019), based on the ICMA's Green Bonds Principles, the central role of the AIFC's Green Finance Centre is consulting with the Kazakhstani government and the National Bank of Kazakhstan on the overall transition to the green financial system.

4.2. AIFC to create demand and supply sides

As chief strategic officer of the AIFC, Professor Alexander Van de Putte stated in a recent interview that there is no shortage of ideas in Kazakhstan

(Van de Putte, 2019). To date, however, the available ways for obtaining financing to implement those ideas have been limited.

There are several directions the AIFC is exploring in relation to introducing bankable projects to investors and vice versa:

1. Global and local private equity, hedge funds and real estate funds.
2. Family offices and high-net-worth individuals (AIFC, 2019, p.68).
3. Eventually developing a small- and medium-sized enterprises market, so that venture capital firms have an exit option at the end of the cycle (Waverley, 2019).
4. The planned establishment of the Green Finance Fund that is to be modelled after the Green Climate Fund, with a mandate to provide guarantees for green bonds and equity injections in companies implementing green projects, among other purposes (AIFC, 2019, p.98).
5. Capital market development with potential inclusion in Morgan Stanley Capital International emerging market indices (including bond indices) for greater exposure to international investors (Kelimbetov et al., 2019).
6. Public-private financing for risk incentivisation of bankable infrastructure projects (Van de Putte, 2019).

4.3. AIFC and post-normal bonds

The AIX has developed its rules for green bond issuance following the ICMA Green Bonds Principles and CBI systematics (AIX, 2019, p.129; AIFC, 2019, p.71).

Further, to encourage more widespread issuance of new bonds, the AIFC Green Finance Centre guarantees to cover the issuer's expenses upon a mandatory external review of the first five green bonds (AIFC, 2019, p.82).

This incentivisation seems to have worked at an unprecedented speed, as KazPV announced the upcoming issuance of its Green Bond at AIX in 2019, followed by mentions of the potential for green-sukuk hybrid issuance (InBusiness, 2019).

CONCLUSION

Due to a unique combination of historical and cultural factors and the multi-vector positioning of the AIFC as a financial institution, there is great potential for a new hybrid type of bond to be issued at AIX. However, this process requires diligent development of the theoretical and legal framework. Moreover, enough time needs to pass to generate

trust and confidence around this financial instrument. That being said, green sukuk hybrid

// THERE IS GREAT POTENTIAL FOR A NEW HYBRID TYPE OF BOND //

bonds possess apparent advantages:

- Doubling impact potential
- Generating interest among a distinctly different pool of investors
- Creating a source of financing for distinctly different projects
- Successfully balancing the profit-conscience dilemma
- Releasing creative potential to survive in the shifting contemporary economy.

As discussed, the AIFC has accumulated sufficient talent and a suitable advisory infrastructure to deliver a green-sukuk hybrid bond. However, in order for this to take place successfully, asymmetries between the development of the green and Islamic tracks at the AIFC need to be addressed.

THE WORLD OF PECHA KUCHA

The competition of which this was the winner involved a variant of 'Pecha Kucha'. What? Well, the entry system required normal essays, judged by a panel of experts. But finalists then presented their results to a conference of their peers using a variant of Pecha Kucha, a storytelling format where presenters show 20 slides with 20 seconds of commentary each. Audience votes tipped the balance of results. For those of us inured to death by PowerPoint, this was a revelation.



Andrew Davis

🐦 @andy_davis01

LAST WORD

Viral forces

THE BANKING AND ENERGY SECTORS
FACE A NEW AND VOLATILE THREAT AT
THE DAWN OF THE DECADE

“ Covid-19 has left our immediate future wrapped in more uncertainty than most of us have ever experienced. But this much is sure: the 2020s will be a very different decade to the one we were anticipating as 2019 came to an end. Of course, we now know that even in the final days of the old decade, the first cases of this new disease were surfacing in China. But we had no clue then what extraordinary times lay just around the corner.

Ironically, as the new decade beckoned, two long-awaited landmarks were approaching that seemed to signal the end of one era and the beginning of the next. In both cases, the changes pointed to a ‘new normal’ that looked set to last for years. In reality, it was over within a few weeks.

At the end of August 2019, the final deadline arrived for claims for misselling of payment protection insurance (PPI) policies that went on from 1990 to 2010. With most claims being settled within eight weeks, the flood of compensation paid to UK consumers by the nation’s banks had slowed to a trickle by the end of October 2019, soon to dry up entirely.

A watershed moment

And what a flood it was: between January 2011 and August 2019, banks handed at least £36.8bn to British households; the peak coming in 2012 when almost £6.3bn was paid out. Even as recently as 2018, more than £4.4bn found its way into consumers’ bank accounts. Some of these windfalls were saved, but many were pumped back into the economy to fund new cars, holidays and home improvements.

The end of almost ten years of multibillion-pound handouts to British

households was a keenly anticipated moment of release for the UK’s banks. PPI payouts, and the cost of processing them in their millions, had been a drain on their profits for almost a decade. The end of this nightmare seemed to mark the final closing of the post-crisis story for the banks, heralding a return to better times.

Within three months, they were plunged into a new world of pain as the economic shutdown raised the prospect of a wave of defaults that are likely to weaken their balance sheets and slice into their profits. Share prices have tumbled and dividends, of course, have been suspended once again under pressure from the regulators, as they were after the 2008 to 2009 financial crisis. So much for the new normal.

“ The world we emerge into will be very different from the one we thought we were living in ”

Just as the final PPI claims were being processed, another watershed moment arrived – in September 2019, for the first time since records began 70 years ago, the US exported more oil than it imported. Securing supplies of energy to fuel the world’s biggest economy had been an abiding concern of US administrations for decades. Now, finally, that job was done. Rising production of shale oil – up three million barrels a day over the past three years – meant that US output had overtaken that of Russia and Saudi Arabia and brought the US the energy independence it had craved.

Progress over the past few years towards this moment was critical in allowing

the US to adopt a much more assertive attitude towards its enemies and allies alike. If it no longer had to rely on others for its energy, it was therefore much less likely to risk its armed forces in regions such as the Middle East. This effectively reset the US’s relationship with everyone else and left China in the position the US used to occupy – a major economy heavily dependent on imported energy. As such, it was a critical plank on which the Trump administration built its ‘America first’ policy.

Energy issues

But the US scarcely had time to savour its landmark achievement before Covid-19 rendered it largely irrelevant. Amid an unprecedented collapse in demand for oil caused by the global lockdown, the price of US crude crashed – it is now so low that most US producers are operating at a loss and many oil sector businesses are expected to go bankrupt. The major problem facing the US today is where to store all the unwanted oil being pumped from its wells – so much so that in late April 2020, for the first time ever, the benchmark price for US crude briefly turned negative. It remains at severely depressed levels that spell continuing pain for the US oil sector.

Although no one can say how long it will take, we will eventually emerge from the Covid-19 crisis. But the world we emerge into will be very different from the one we thought we were living in just a few months ago. And like everyone else, the banking and energy sectors have been taught a painful lesson about the power of events and how they can overwhelm seemingly sensible assumptions about our direction of travel. ●

ILLUSTRATION: PADDY MILLS/SYNERGY



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Popular 90 mins

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Gain an overview of insider dealing, market abuse, money laundering, terrorist finance and financial sanctions.



Refreshed 90 minutes

Financial planning

Gain an overview of the financial planning process, key terms and the regulatory framework that governs it.



New 90 minutes

Green bonds and asset-backed securities

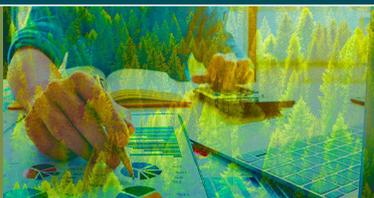
Explore the various types of bonds and securities available, as well as their benefits and risks.



New 90 mins

Impact investing

Aim to take ethical and sustainable investment principles a step further through intentional investment.



Popular 75 mins

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Understand ethics in finance, the importance of trust and trustworthiness, and compliance versus ethics.



Popular 60 mins

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