

**International Financial Services and Technology**

**ISSA Symposium**

June 12 - 14, 2002

UBS Wolfsberg Centre

**Starting Point for  
Clearing and Settlement Infrastructure for  
European Mutual Funds Market**

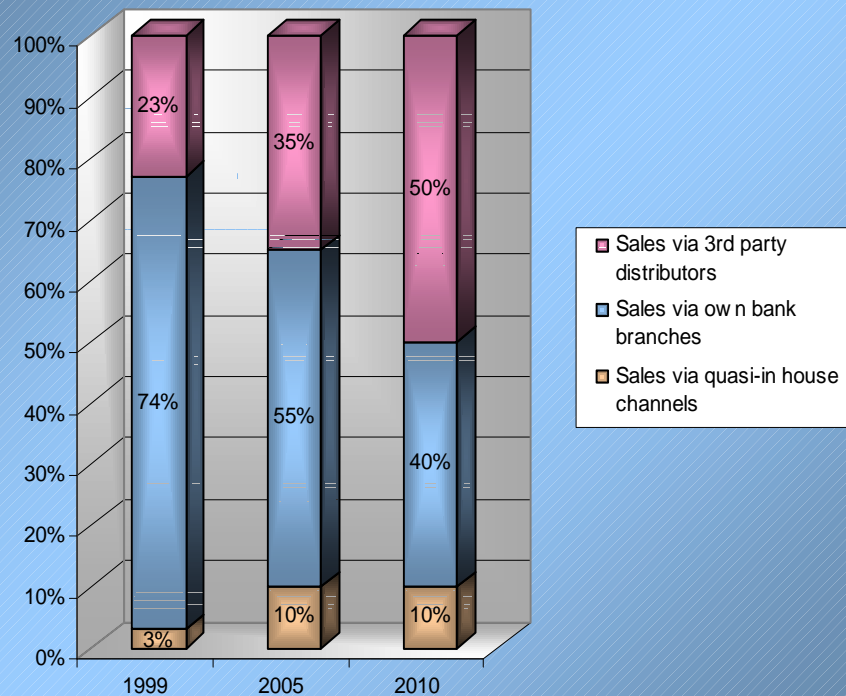
**Fayez N. Akhras**

## Basic Facts about Mutual Fund Market in Europe

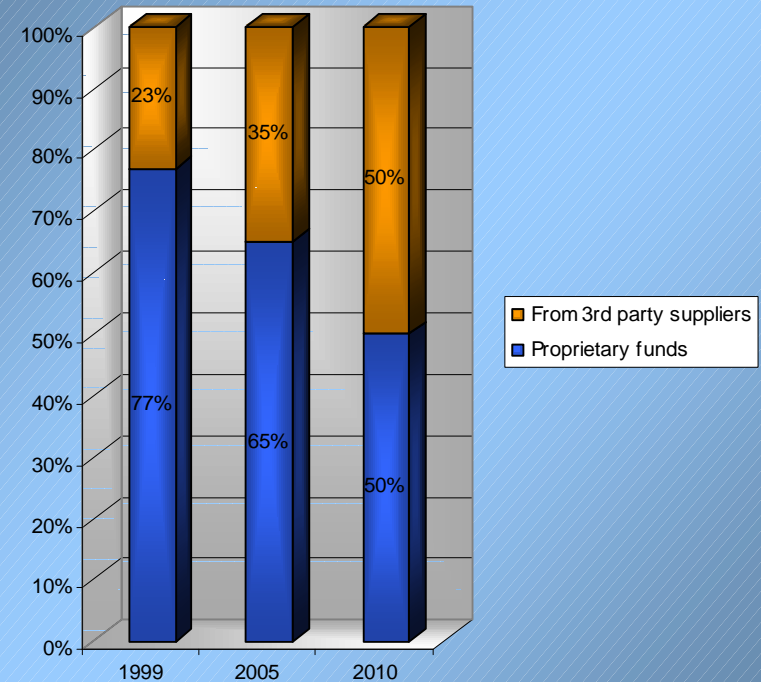
- ➔ Dynamic and fast growing investment fund market, presenting significant asset gathering opportunities for industry participants
- ➔ Movement towards open architecture for fund distribution - 3rd party distribution
- ➔ Changing landscape from Domestic Funds to Cross Border “International” Funds distribution
- ➔ Internet delivery and fund supermarkets are a critical driver of opening up distribution channels
- ➔ Investor culture and increased sophistication are redefining distribution in Europe
- ➔ Increased product complexity

# European Distribution Evolving to 3rd Party Distribution

Manufacturing perspective



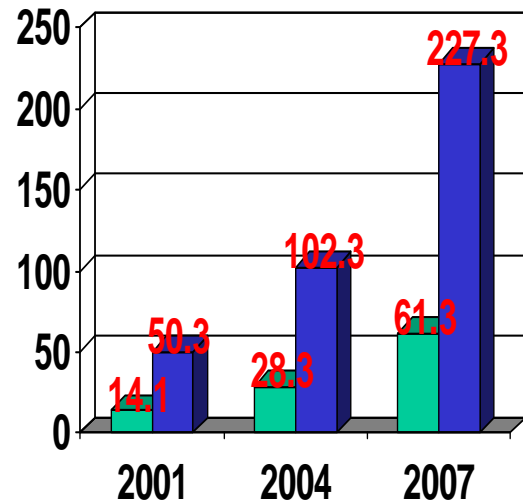
Distribution perspective



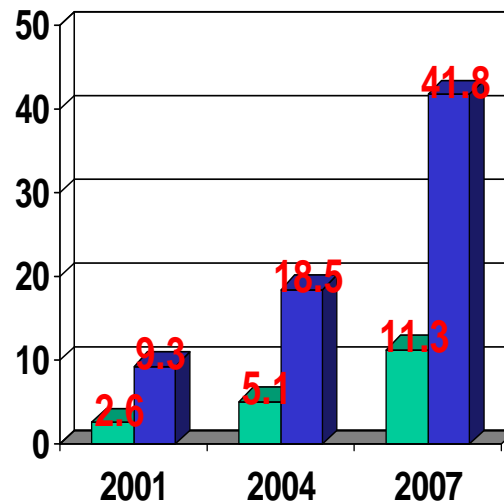
\* Based on Andersen Analysis

# Fast Growth Forecast in Mutual Fund Processing\*

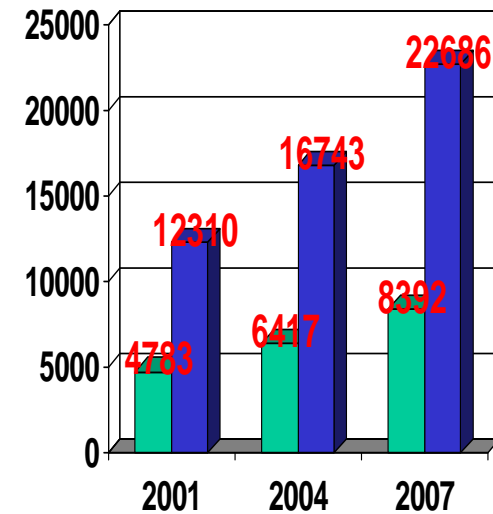
Transactions (M)



Accounts (M)



Funds

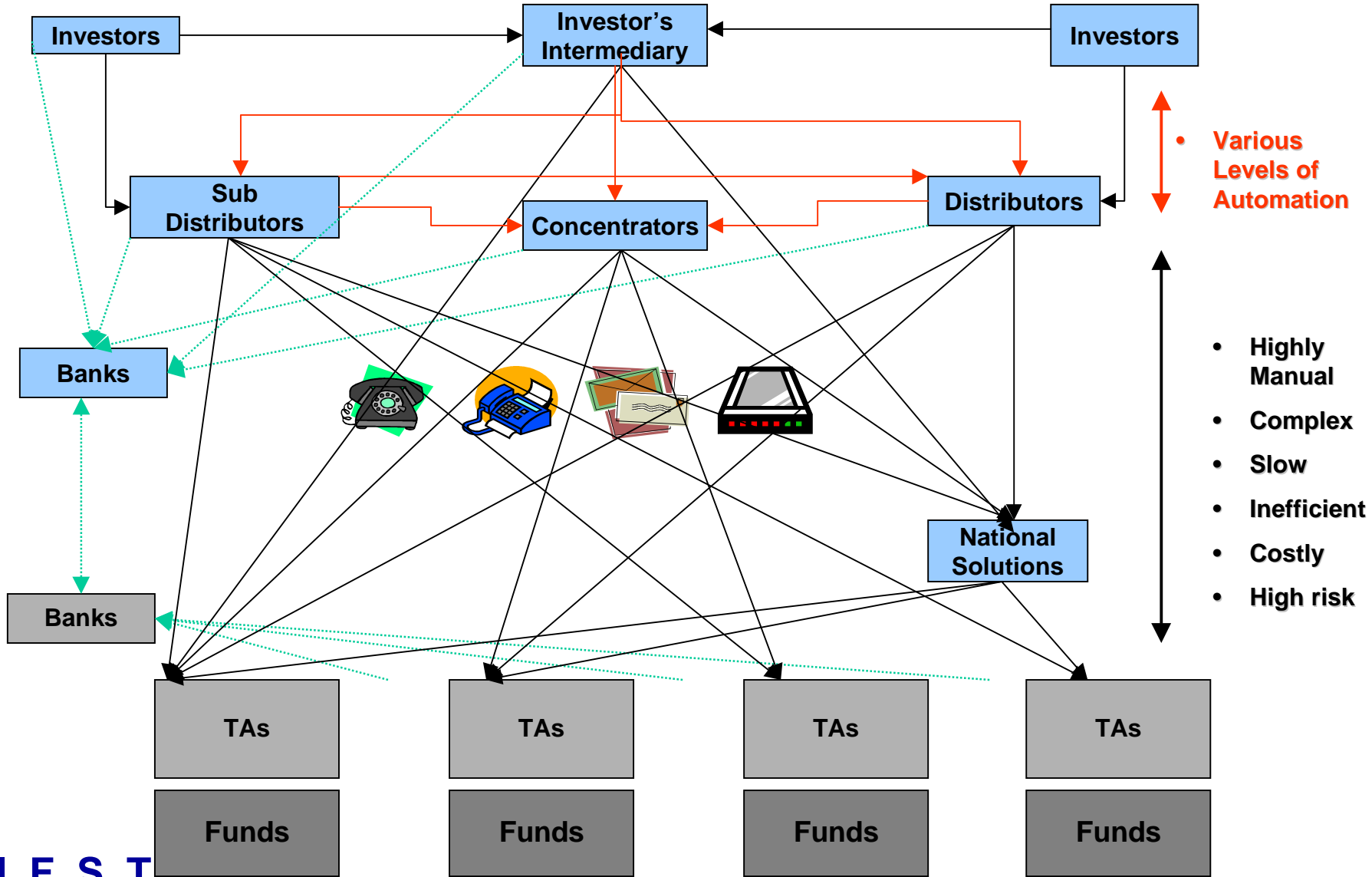


■ Luxembourg 
 ■ Europe (ex. Lux)

# Complexity of European Funds Market

- ➔ Two-tier structure, National funds & Cross-border funds (Lux/Dublin)
  
- ➔ Multiplicity of:
  - ➔ Domiciles
  - ➔ Distribution channels
  - ➔ Currencies
  - ➔ Languages
  - ➔ Tax systems
  - ➔ Clearing & settlement infrastructures
  - ➔ Regulatory requirements
  - ➔ Commission structures
  - ➔ Standards and business practices
  
- ➔ No industry standardization for:
  - ➔ Trade instructions (exception: SWIFT& EMX)
  - ➔ Settlement for offshore & cross-border markets
  - ➔ Connectivity between clearing platforms
  - ➔ Commission calculations or commission reporting
  - ➔ Trading and settlement business practices and process flows
  - ➔ Straight Through Processing (STP) or Straight Through Reporting (STR)

# Current State of Distribution Support in Europe



## The Result

### A Fund Clearing Environment that is:

- ➔ high in operational and settlement risk,
- ➔ highly inefficient and costly,
- ➔ heavily manual,
- ➔ non-scalable,
- ➔ very fragmented,
- ➔ incapable of supporting the continued evolution of business models of Distributors and Manufacturers

**Given the projected transactional and settlement growth of European mutual funds, the continuing reliance on existing environment is an avoidable risk today. If the industry takes no action, the risk will become unavoidable**

# Industry's Conclusion: A Critical Need for a Central & Standard STP & STR Solution

**Distributors**

**Front & Back  
Offices**

**Clearing  
Banks**

**Settlement  
Banks**

**Back Office**

**Funds**

**Valley of Communications**



# What is the Proper Vehicle for Building the Solution?

## ✓ While Industry agrees on:

- ✓ outlook for growth and distribution trends
- ✓ fragmentation of market and its infrastructure
- ✓ problem(s) with current infrastructure
- ✓ need for a solution

## ➔ Industry has not fully examined the design principles of an infrastructure:

- ⇒ Scope of infrastructure and services
- ⇒ Ownership structure and governance
- ⇒ Technical design and implementation
- ⇒ Financing and financial structure

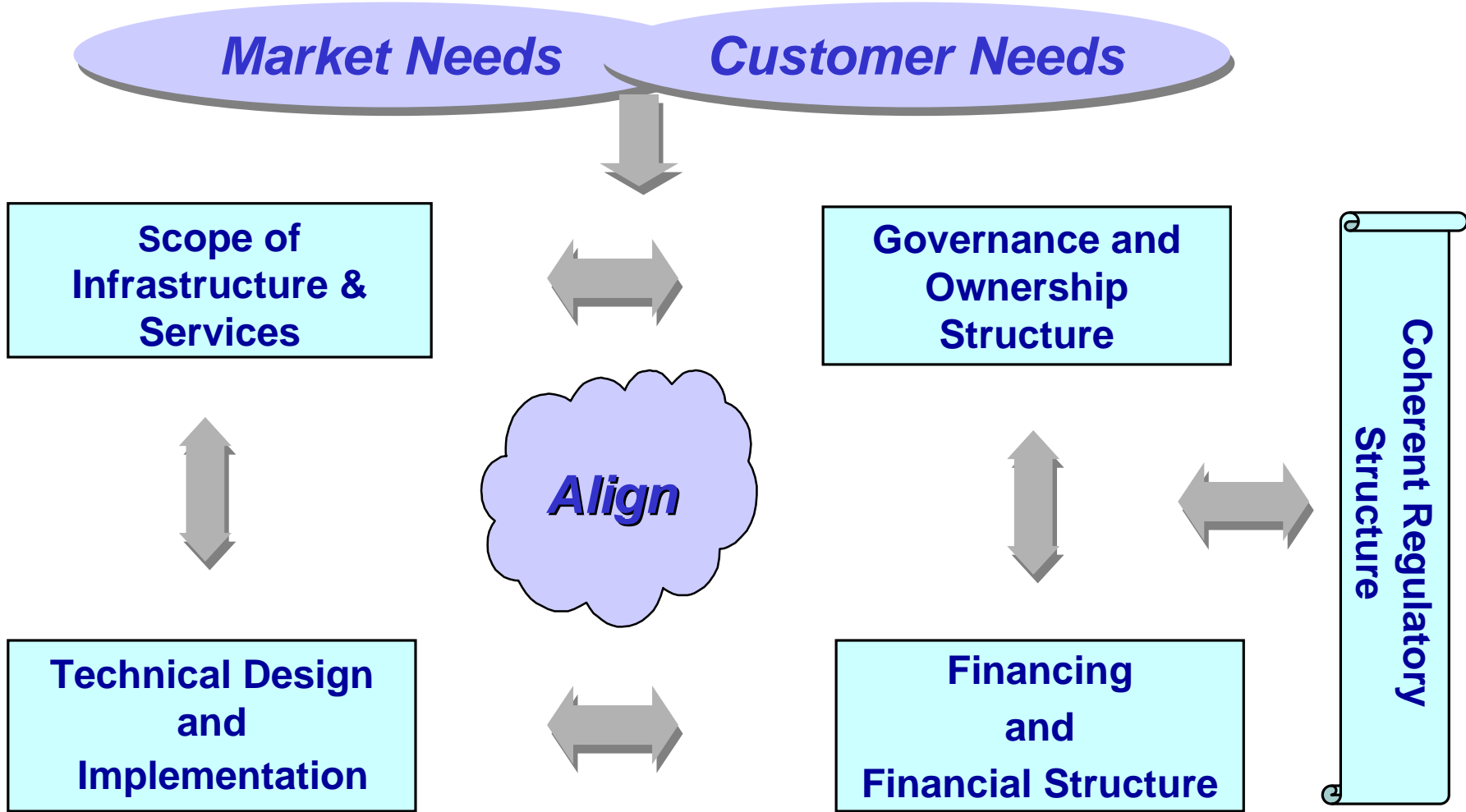
## ➔ Main and only focus should be on funds industry, not securities industry ... solution for clearing and settlement of funds cannot be directly imported from equities model

- ⇒ different market (e.g. price discovery, market making, trading, etc.)
- ⇒ different product (e.g. trade matching, share issuance, settlement, commissions, etc.)

## ➔ Some European initiatives have taken steps towards first generation solutions, however:

- ⇒ they entered the market too early, bypassing the market's agreement on design principles
- ⇒ some follow the securities industry model and are retrofits of its infrastructure

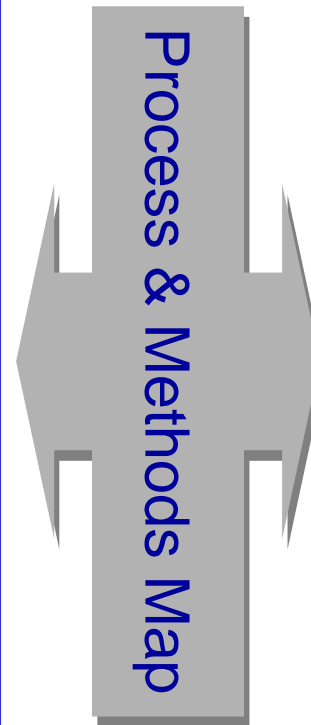
# Alignment with Market and Customer Needs



# ISSA's Methodology Maps to Design Principles of Mutual Funds Market

## ➔ ISSA's Recommendations 2000

- 1- Governance
- 2- Technology: Core Processing
- 3- Technology: Messages & Standards
- 4- Uniform Market Practices
- 5- Reduction of Settlement Risk
- 6- Market Linkages
- 7- Investor Protection
- 8- Legal Infrastructure



**Governance and  
Ownership  
Structure**

**Scope of  
Infrastructure &  
Services**

**Technical Design  
and  
Implementation**

**Financing  
and  
Financial Structure**

**Coherent  
Regulatory  
Structure**

# Need for a Forum Dedicated for Mutual Funds Market

- ➔ ISSA is the first and only neutral and objective forum to:
  - ✓ openly discuss the issue of mutual funds clearing and settlement in Europe
  - ✓ examine approach and process of building an infrastructure that meets the market and customer requirements
- ➔ As a first step, there is a critical need for a dedicated industry effort to
  - ✓ properly evaluate and recommend a set of design principles specifically tailored for the mutual funds market
  - ✓ seek a common sense of interest, vision and commitment from all mutual fund market participants in Europe
- ➔ Proposed agenda and objectives for mutual funds Working Group 1:
  - ⇒ validate the need to address the mutual funds market
  - ⇒ recommend action steps:
    - ⇒ how to address the needs
    - ⇒ organizational roles and responsibilities

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# Working Group: Evaluating Design Principles (Place Holder)

- Scope of infrastructure and services
  - ⇒ where in value chain should solution exist?
  - ⇒ national and/or cross border?
  - ⇒ relationship to existing market infrastructure for securities?
- Technical design and implementation - components of solution
  - ⇒ pre and post trade communication and reporting
  - ⇒ cash settlement and reporting
  - ⇒ standards and communication
  - ⇒ reporting
- Ownership structure and governance
  - ⇒ is it public, private or cooperative?
  - ⇒ how is the market represented in governance?
  - ⇒ who should drive the initiative?
- Financing and financial structure
  - ⇒ who should finance the design?
  - ⇒ who should finance the implementation?
  - ⇒ how to balance risk/reward?