

## **1. Opening Remarks**

Mr Eui Dong Chung, KSD Chairman & CEO, welcomed around 75 delegates from ISSA member firms and select guests. 13 countries were represented.

Mr Chung referred to the 21st century as "the age of no right answers". Looking back on the past few years, many economic sectors - the capital market industry in particular - lived through far reaching and ever faster changes. Major industry players disappeared or changed shape by way of merger, and new ones emerged. Boundaries between areas that once used to be clearly segmented, have become increasingly blurry or were torn down altogether.

KSD joined ISSA in 1988 and has always been an interested, active and supportive member. KSD sees value in an ISSA membership in that the association can help its members to better understand these changes. They are thus in a better position to ride the waves, rather than run the risk of being swept away in the currents.

KSD has always endeavored to be at the forefront of trends, to keep abreast of changes and to serve the Korean capital market to the best of its abilities.

Hosting today's meeting is a tangible expression of the value KSD puts into international partner-ships to obtain and to share relevant industry knowledge.

## **2. ISSA Information Items**

The full text and the slides used in Josef Landolt's address are available separately. Main points included:

- An update on ISSA's involvement with the G30 process and an assessment of that process. Progress has been slower than generally anticipated, but there have been positive developments in the area of G30 Recommendations 2, 3 and 8. The key to achieve implementation of Recommendation 2 is in Europe, where the European Commission pushes for the definition of a common IT communication protocol linking the capital markets of all 25 European Union member countries. SWIFT was mandated to draft a blueprint and published a proposal for industry feedback earlier this year. A special task force, representative of the European securities industry, was then convened to resolve issues where the public consultation process had failed to provide clear guidance, or had produced contradicting responses. ISSA participated actively in that working group. The final version will be available by March 2006. A five year implementation period for Europe must be expected. A communication protocol fit to accommodate the needs of 25 diverse European member states, should be suitable for other markets as well, and it is hoped that the European solution can be extended to meet G30 Recommendation 2 on a global scale.
- Of special note is a discussion paper for a streamlined withholding tax model, prepared by tax specialists of JPMorgan. ISSA endorses the model although some amendments will be necessary. All ISSA members and interested parties are invited to review the proposal and submit comments to the ISSA Secretariat or to its authors directly. Feedback from the Asia/Pacific region is still missing and would be particularly welcome. The paper is available from the ISSA website or through the secretariat.
- ISSA's involvement with cross-border mutual funds processing: In April this year, ISSA convened a roundtable meeting with European key players to explore areas where cross-border mutual funds processing could be made more efficient. Two schools of thought became apparent:
  - In one camp those who would like to automate today's business processes which are rather fragmented *on a cross-border basis*;
  - In the other camp, those who question today's retail-investor oriented processes and would prefer aligning funds processing to the well established and efficient procedures of the equity market.

ISSA made contact with EFAMA (European Fund and Asset Management Association) which recently published a set of best proposals to realize efficiency gains in the existing funds order placement and settlement process. Research and discussion will continue and funds processing will be a key topic in next year's ISSA Symposium (6-9 June 2006, as always at Wolfsberg, Switzerland). See the ISSA website for more information on this subject.

- ISSA's active participation in the General Assembly of the Americas' CSD Association (ACSDA) in March, in lieu of conducting its own regional meeting in the Americas: Through the joint venture with ACSDA, ISSA can reach 24 markets on the American continent, well beyond its own membership in the region.
- Change in the ISSA executive board: Dresdner Kleinwort Wasserstein decided to withdraw from the board. In its place, Schroder Investment Management accepted an invitation to join the circle of sponsor firms. Schroders is represented on the ISSA board by Mr Markus Ruetimann, Chief Operating Officer. The ISSA board is pleased to have a leading asset manager among its members. The newly composed board will meet for the first time on 7 November 2005.

### 3. Infrastructure Reforms and Market Updates

#### Japan

Japan is in the midst of a massive capital market reform program scheduled to end in 2009, affecting the market's legal framework, all relevant market institutions and all classes of financial instruments. Mr Onuma (JASDEC) and Mr Nishimukai (JSCC) presented the cornerstones of the reform and an update on the major recent and ongoing projects. There are numerous industry-wide initiatives and projects driven in parallel, coordinated through the "Reform Promotion Center For Securities Clearing and Settlement System" ([www.kessaicenter.com](http://www.kessaicenter.com)). A selection of key elements of the reform includes the following:

- Extensive revisions to the legal framework
- Improvement of industry-wide straight-through processing (STP)
- Paperless trading of Japanese Government Bonds (in place since 2003)
- Paperless trading of non-government bonds to start in January 2006
- Voluntary conversion of investment trust funds from physical bearer shares to book-entry shares from 2007
- Full dematerialization of the equity market by 2009
- Implementation of central counterparty services for all major instruments
- Enhancement of a pre-settlement matching system for all instruments (note: 99% of all trades already match on T+0)
- DVP for all instruments, including off-exchange trades of listed instruments
- Facilitation of cross-border trades

Please refer to the slide presentations for further details and sources of additional information.

#### Korea

Mr Ahn (KSD) introduced FundNet, the central investment funds processing platform developed and operated by KSD for the Korean market. Introduced in 2004, FundNet is designed to be the core infrastructure system of the asset management industry in Korea. It supports the handling of investors' orders to buy and sell investment fund shares on one hand, and the proper settlement and custody of each fund's underlying investments on the other hand, assuring full compliance with Korea's new Asset Management Business Act (AMBA). Links to similar foreign systems are planned. Please refer to the slide presentation for further details.

**China**

Mr Shen (SD&C) gave an overview of the reforms and developments in the Chinese markets over the last few years. The legal and regulatory frameworks were strengthened, the market infrastructure built or modernized, and the range of financial instruments expanded. Compared with other markets, all of these changes were realized at record speed. Further reforms and improvements are planned, notably in the areas of risk management, further efficiency gains, and to proactively exploit new business opportunities. The market is still dominated by individual investors (currently around 70 million). However, domestic and overseas institutional investors play an increasingly important role.

Please refer to the slide presentation for further details.

**Indonesia**

Mr Akbar (KSEI) presented a status update on the Indonesian capital market with regard to the ISSA Recommendations 2000.

Please refer to the slide presentation which is fully self-explanatory.

**Taiwan**

Mr Lin (TSCD) provided an update on recent market developments in Taiwan. A major reform was the establishment of the Financial Supervisory Commission (FSC) in 2004. FSC acts as the single supervisor and regulator for the banking, securities and insurance sectors.

2005 saw a large number of market changes, many of them in response to discussions with local custodians serving overseas investors, and with foreign investors directly. Significant market changes include measures to facilitate market access for foreign investors, the relaxation of certain trading regulations (among them, permission of short selling of the Taiwan 50 index stocks), the relaxation of rules relating to account transfers without change of beneficial ownership, the relaxation of rules on securities lending and borrowing, and the development of a central processing platform supporting the offshore fund market. TSCD absorbed DICD (Debt Instruments Depository and Clearing Co.), bringing clearing, settlement and custody for all financial instruments in the market under the same roof.

Please refer to the slide presentation for further details.

**Thailand**

Ms Piamduaytham (TSD) reported on the establishment of a central depository and clearing house, under the roof of TSD, for the Thai bond market, expected to be launched in December 2005. The Thai government drafted a ten year development plan (2005-2014) to exploit the bond market's growth opportunities, and to support it with an infrastructure that can match the best systems currently in place anywhere around the world. An efficient and liquid bond market will be the third pillar of the Thai capital market, alongside the existing money and equity market segments.

Please refer to the slide presentation for further details.

## 4. Clearstream/Deutsche Börse Group Initiatives in the Region

### Deutsche Börse Group's View

Mr Metoudi introduced the Deutsche Börse Group (DBG) as the only fully integrated exchange organization worldwide, i.e. providing IT services, financial information, trading platforms, clearing, settlement and custody facilities out of one hand.

With regard to the Asia/Pacific region, Deutsche Börse Group follows a three-pronged approach to business development:

1. Improve the distribution of its own products in Asia/Pacific: Today, Deutsche Börse Group already services more than 800 clients in 17 Asian countries. Facilitating access to its trading platforms and ICSD services from Asia, and technology transfer through the sale of system licenses, are among the means to reach the goal.
2. Improve the distribution of Asia/Pacific based products in Europe: Currently, more than 1'000 equity issues domiciled in 14 Asian countries can be traded on XETRA (the German market platform for cash trading). Indices and ETFs (Exchange Traded Funds) with Asian underlying instruments are listed on DBG's trading platforms. DBG actively promotes Frankfurt as an IPO location for Asian issues.
3. Take part in the set-up and development of the Asia/Pacific market infrastructure: DBG maintains partnerships and MOUs (Memorandum of Understanding) with the Shanghai Stock Exchange, Chinaclear and with the Osaka Stock Exchange. If and when "AsiaClear" or "AsiaSettle" ever becomes a reality, DBG wants to be closely involved in its creation.

### China Securities Depository & Clearing Co.'s View

Mr Shen expected SD&C to profit from the cooperation agreement with Deutsche Börse Group by gaining access to know-how in the following areas:

- Financial market integration and market expansion
- Integration of backoffice functions across different market segments
- Development and operation of state-of-the-art risk management systems
- Development of margin trading and securities lending and borrowing operations: Short selling is currently prohibited, but it is expected that the Chinese market will eventually open up to these instruments.
- Development and operation of a derivatives market
- Further development of the investment funds market: Currently, 49 fund management companies operate in China. There are some 200 investment funds and between 60 and 70 million individual investors. The market's potential for growth is considered huge.

SD&C also entered into cooperation agreements with a number of other infrastructure operators including KSD (Korea), OMX Group (Northern European markets), Hong Kong Exchanges and Clearing Ltd., JSCC and JASDEC (Japan). These alliances will allow SD&C to move faster into the future by adopting best practices from other markets right from the start, and by avoiding pitfalls others experienced in their early stages of development.

### Thoughts on "AsiaClear" - An international CSD for the Asia/Pacific region?

The idea of creating an Asia/Pacific equivalent to Clearstream or Euroclear has been around for many years. Bilateral links between CSDs have not taken off in the region so far (nor in Europe on a significant scale, for that matter). There is, however, a clear indication that cross-border investing within the region will gain significance. To date, Asian investors typically favored the US market if they decided to invest abroad at all. More cross-border trading will increase the need for efficient and safe infrastructure platforms to support such transactions. Eventually, there will be demand for an ICSD-type structure. It is, however, still too early to speculate on its shape and on the time horizon for its creation.

## 5. Securities Lending and Borrowing

On behalf of PASLA, Mr Daswani and Mr Falco presented an overview on the state of securities lending and borrowing across twelve markets of the region, focusing on issues where changes or improvements would be desirable so as to achieve maximum market liquidity and efficiency. Typically, obstacles fall into one of two broad categories:

- onerous reporting and disclosure duties imposed on counterparties,
- unequal treatment/restrictions imposed on foreign market participants.

A common element of all market reviews was the observation that today's causes of inefficiency are no longer on the operational side, but on the side of legal, regulatory and tax requirements.

## 6. The Asset Manager's Perspective: How Can The Region Attract More Foreign Investment?

The panel included Mr K.S. Jeon (Schroders Korea Ltd), Mr D.J. Jang (Shinhan BNP Paribas ITMC), and Mr Hank Morris (GAM Hong Kong Ltd).

Most Asian markets are growing, some even show very impressive growth rates. However, most markets have now "only" recaptured the levels they were at in 1999.

Throughout the region, the state of securities clearing and settlement systems are no impediment to the growth of the asset management markets. There are public reports by the Asian Development Bank confirming this observation.

The discussion focused on the Korean market, which is relatively small but rapidly growing. There is a fast growing demand for investment products. The market is extremely short-term oriented, with investment horizons typically ranging from 6 to 12 months only. Even more so than in other markets, a spectacular investment performance in one accounting period is no indication for success in the next one.

Some of the insights gained from the Korean market reality apply to other parts of the region as well. A selection of issues, observations and recommendations includes the following:

### Regulatory Environment

- Markets should deregulate to the extent possible. Local regulation should be brought in line with global regulatory standards, or at least not create conflicts with global norms.
- Local market operators servicing offshore clients should maintain an active dialogue with their regulators to highlight problem areas and to resolve them. Regulators may not always be aware of particular information needs of foreign market participants. Similarly, they may not be aware that certain regulation might cause (unnecessary) obstacles for foreign investors. An example: A central bank may require asset managers to secure approval prior to investing in OTC derivatives. In order to obtain approval, all terms of the transaction including information on the selling broker involved, must be disclosed. If the transaction is to be executed in a market that uses a central counterparty, the asset manager will be unable to fully comply with the disclosure requirement since the selling broker remains hidden behind the central counterparty.
- Financial markets tend to be innovative and flexible. Many regulatory frameworks could be simplified greatly – and the introduction of new products expedited – by dropping the requirement to obtain the regulators' permission for every new type of financial instrument, service or transaction. A simpler set of rules defining "off limit" business areas would serve the same purpose. (The speaker referred to this as moving from a "positive" to a "negative" regulatory system.)
- Generally, the regulatory environment in the Asian markets does not favor small, boutique-type investment advisory firms, due to high minimal capital requirements and burdensome restrictions and obligations imposed on firms wishing to obtain or renew an investment advisory license. In addition, small firms typically suffer from the very high legal fees associated with maintaining or

renewing a business license. A large number of small, innovative and flexible investment managers would, however, attract more attention from offshore investors.

- Double taxation schemes tend to be complex, particularly where equity investments are concerned.
- All relevant rules and regulations, including all amendments, should be publicly available in an official English version.

**Business Environment**

- A stable business environment and reasonably predictable economic development helps to attract foreign investment. The political leaders should do their utmost to create an investor-friendly climate.
- Market infrastructure solutions, such as for instance FundNet described in one of today's earlier sessions, are important to make transaction processing more efficient and cheaper. However, asset managers often experience that the cost of joining and maintaining a membership in such industry solutions, is too high to make their use worthwhile.
- Taking the example of Korea, there is no shortage of investors with significant savings to invest in the financial market. It is, however, very difficult for offshore fund managers to sell their products into the Korean market. Competition is fierce, profit margins for both domestic and foreign fund managers are thin and are eroding further.

**Human Resources**

- A flexible labor market adds attraction to an economy as an investment target.
- A well educated, well qualified work force is an important asset.
- English language skills are indispensable to bridge the language barrier.

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