MiFID II – what next ?

Michael Hufton looks ahead to the FCA's Thematic Review into MiFID II, including predictions, early results, and advice for IROs.

WHAT NEXT?

- **Results of the FCA MiFID II Thematic Review due in Q2.**
- **Strong support from the UK regulator for these reforms.**
- **Evidence shows significant cost savings delivered for investors.**
- **Growing internationalisation of MiFID II.**

Popular folklore has it that MiFID II contains some 1.7m paragraphs of text, coincidentally the same number of times IROs have heard the acronym over the past few years. It has become a turgid topic, and so it's with some trepidation that I approach MiFID II yet again.

2019 started with a focus on MiFID II one year on. But MiFID II 18 months on will be much more interesting. The Financial Conduct Authority announced its Thematic Review into MiFID II in July 2018 and is due to publish the final report in Q2. This has been a thorough body of work, pulling data from across the industry and conducting visits to buy-side, sell-side and independent firms. It should give us a comprehensive view of how the regulator thinks MiFID II is bedding in – and where the sensitivities lie.

From FCA CEO Andrew Bailey's speech on 25th February, and the FCA's presentation at AIRA's Annual Conference in Sydney in November, we have good visibility over what the high level conclusions of the review are likely to be:

- the FCA is strongly supportive of MiFID II;
- fundamental changes have occurred in the market;
- early results indicate a reduction in costs incurred by investors in equity portfolios managed in the UK of c£180m in 2018, an estimated £1bn saving over the next five years;
- the market is going through a period of price discovery and is yet to find an equilibrium; and
- internationalisation of, and growing international interest in, these reforms.

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What it means for IROs

From an IRO perspective, the extent of change isn't always obvious, especially for large cap corporates: most see more incoming meeting requests directly from investors; many see an evolving landscape at conferences; some perceive changes to sales and research coverage on the sell side. But the buy side has experienced profound change, with the entire industry moving to a model where the cost of research and corporate access is taken to P&L, not billed to the client, and several large firms building internal corporate access teams. The impact of these shifts is still percolating through.

Others have noted the growing international impact of MiFID II, for example the speech on 26th February by Commissioner John Price of the Australian Securities & Investments Commission (ASIC) to the Group of 100 Australian CFOs dinner: "…The impact of MiFID II may even be more far reaching than that. As recently noted in The Economist: 'As well as being a European rule, MiFID II may evolve into being an unofficial international standard.'"

We can be confident that the Thematic Review will strike an overall tone of positive-but-it's-early-days. However, the devil will be in the detail. Whilst the FCA is keen to stress it will be risk-based in its supervisory approach, it could well cite examples of both good and bad practice – with the possibility of referring cases for further investigation or enforcement. As such, it is likely to set de facto bounds of what is acceptable, and this will drive further change in market practice.

> ' Low pricing can be good, but not where it's so low it raises questions of effective competition '

Joining the dots gives clear indications where there could be issues. One is the importance of considering value, as well as quantity, in formulating pricing, with robust ex-ante as well as ex-post evaluation criteria and metrics. This applies equally to corporate access as it does to research – and is far from universal in market practice today. Expect uniform low-level pricing policies, especially where there is no obvious methodology behind the numbers, to come under scrutiny.

Low pricing can be good for the end consumer, but not where it's so low it raises questions of effective competition – one of the FCA's three operational objectives. Low cost 'all you can eat' packages and one-off events such as conferences priced substantially below cost are also likely to be a focus of attention. IROs frequently observe changes in conference attendance since the introduction of MiFID II, and I would expect to see further evolution in how conferences are attended, priced and paid for.

For IROs, the most likely outcome is a continuation of the trends that have become apparent over the past 12 months: a growing responsibility to do more within the team. ■