

Submission on Proposed Industry Funding Model for the Australian Securities and Investments Commission

Why is there no proposed AFSL sub-sector for independent equity research?

Ian Martin Advisory is a small independent research firm providing equity research to Australian and (as far as we are legally able to) international financial institutions. In general we avoid publishing financial recommendations and we do not advise on financial products nor deal in financial products.

We have had conflicting advice on whether we need to hold a financial licence given the nature and focus of our service. However, to be on the safe side, we are an authorised representative of an AFSL holder. Even with this however, we have received conflicting advice on the extent to which we are able to provide advice on Australian equities to financial institutions in overseas markets.

Our general comment on the proposed licensing model is that there is no specific licencing arrangement for independent equity research analysts. Possibly the General Advice Providers category may apply but this appears designed for providers of advice to retail investors rather than for independent equity research aimed at institutional investors.

There are many individuals and small organisations that provide such independent research or specific industry advice to financial institutions typically focussed on one or other sector of the listed securities market. Often these are people familiar with the sector and the advice offered does not extend to making financial forecasts but remains of a general nature.

At the same time there is an emerging group of independent financial research analysts (ie independent of brokers and investment banks) offering sector expertise with financial forecasts and valuations if not recommendations and price targets on listed securities. In the UK, Europe and the US the independent research sector is emerging rapidly with new regulation requiring investment banks to charge separately for such research.

“The EU rules, which still are being completed for implementation in 2017...are designed to address long-standing concerns about potential conflicts of interest and other problems associated with the way investors pay for research.” Wall Street Journal 9 Feb 2015 “*New Rules to Reshape Analyst Research*” available from <http://www.wsj.com/articles/new-rules-poised-to-reshape-analyst-research-sector-1423514292>

In the UK and Europe separate regulatory and licensing arrangements are being put in place to recognise and support independent equity research. There are similar developments underway in the US. These are specific to independent research rather than including them in a broader ‘general advice’ category.

We expect the demand for independent research will grow quickly in these more established financial markets after implementation in 2017, and we would like to position ourselves to contribute our insights on certain Australian equities to investors in these markets. We feel we are somewhat constrained from this contribution by the lack of a specific licencing regime for independent research. It is not clear, for instance, that the General Advice category would be sufficient to support such a service.

As well the lack of an AFSL sub-sector for independent research reflects a lack of work and preparation by ASIC for the emergence of independent research. If this grows rapidly in these other key financial markets by 2017 what will be the impact on Australian equity markets and the Australian financial system in comparison?

The Final Report of the Financial System Inquiry sets out a blueprint for Australia's financial system over the coming decades but neglects independent research as an important component of this despite the importance of equity research in capital market processes.

The Government wants to promote Australia as a financial centre (according to former Minister Josh Frydenberg, Speech to the Financial Service Council, 15 April 2015) and has a number of policies in place to promote this. A process to support Independent Research should be a part of such a policy process as it is in these other developed financial markets. As independent research emerges after 2017 it will improve the conduct and performance of financial analysis and performance in these markets and improve the reliability of such research for investment decision makers.

Regulation of the Australian financial sector should be on the same path or risk falling further behind these developed financial markets. At a minimum this should include a specific AFSL sub-sector for independent research. And with a specific licencing regime, ASIC should consider what specific arrangements should be put in place, bearing in mind similar developments in the UK, Europe and the USA, to support and promote independent equity research.

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