



Consultation on Structured Products



leading on tax incentivised savings

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The Investment Bridge Limited

the investment bridge

connecting investment

UK Retail Structured Investments

'Raising the Industry Bar'

PREPARED FOR

TISA (Tax Incentivised Savings Association)
Structured Products (Investments) Debate

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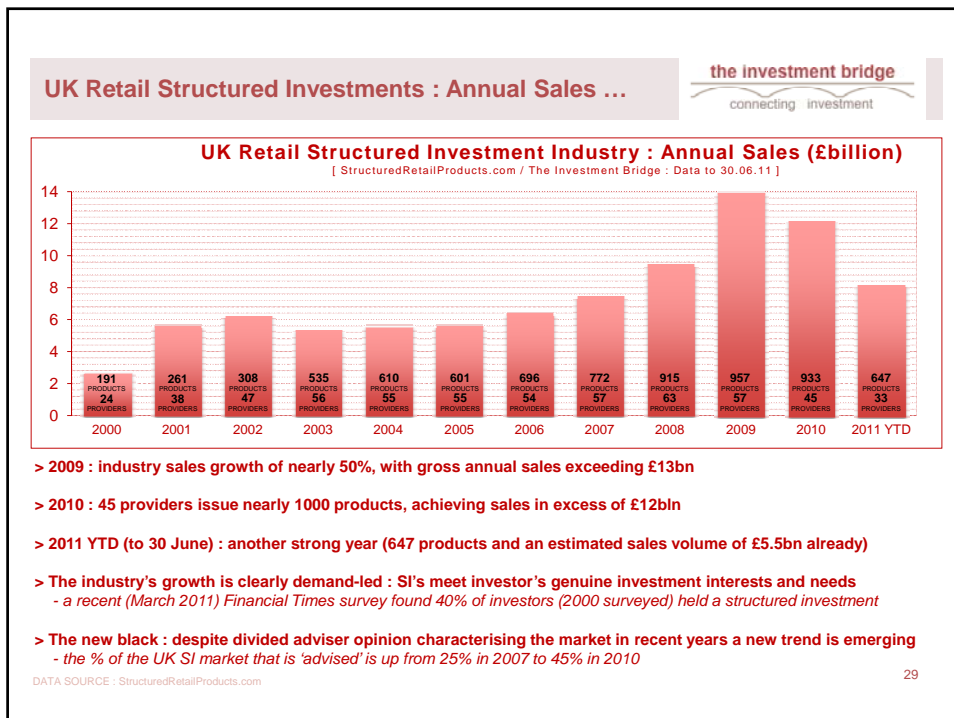
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TISA Structured Investments Debate

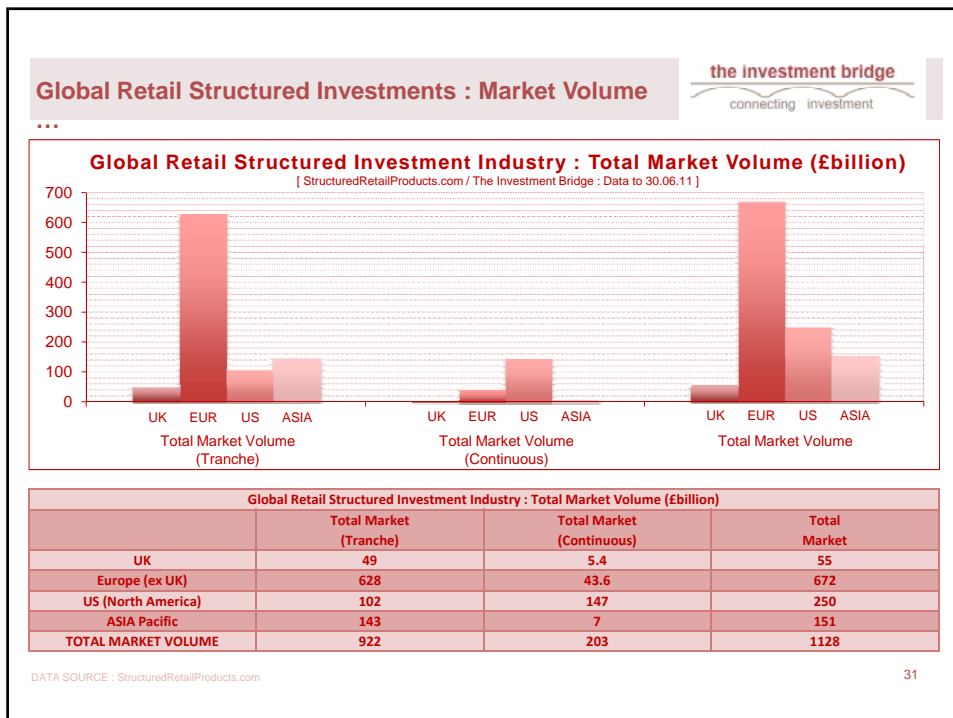
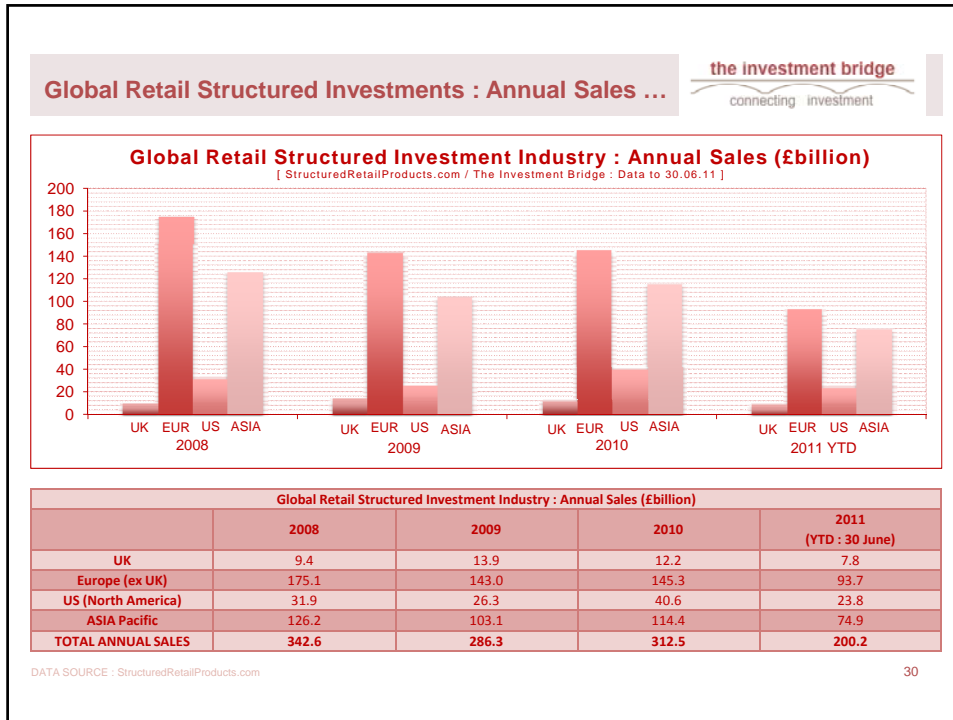


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The UK : significantly behind the curve ...



> The UK is significantly behind the curve in its use of structured investments

- primarily the result of distribution dynamics : 2/3 – 3/4 of investment advice and sales is through independent channels
- contrast this with many/most other markets globally being dominated by 2-4 major brand banking groups
- the UK independent advice channel is fragmented : 25,000 opinionated individual IFAs / R/Is
- past industry events (precipice and Lehman Brothers) have coloured adviser (and commentator) views
- culturally : more of an equity than a bond culture
- a powerful mutual funds industry : imagine where we would be if structured investments had come first

> The potential to fully embrace structured investments is clear : exponential growth opportunities

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Let's talk investment ...



> Who ...

- knows exactly how global economic growth is going to play out : and the level of markets in the next 5 years ?
- believes the FTSE 100 will fall below, say, 2800 - 3000 points in the next 5 years ?
- believes the FTSE 100 will be above, say, 9000 points in 5 years ?
- ... how many advisers / investors are actually positioning portfolios with these market views in mind ?

> If economic growth 'double dips' and we have a period of 'lost returns' : with low interest rates, rising tax, and uncertain/unpredictable returns ...

- investors will need / demand that their advisers break the relationship between market returns and their returns
- investors' portfolios will have to work harder : 'cleverer' investments will be needed

> STRUCTURED INVESTMENTS CAN 'BEND AND/OR BREAK' THE RELATIONSHIP BETWEEN MARKET RISK/RETURNS AND CLIENT RISK/RETURNS ...

AND DO SO WITH NO ACTIVE FUND MANAGEMENT RISK !

> We'll look at the direct BENEFITS of credit risk / counterparty exposure candidly shortly ...

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Let's talk investor interests ...



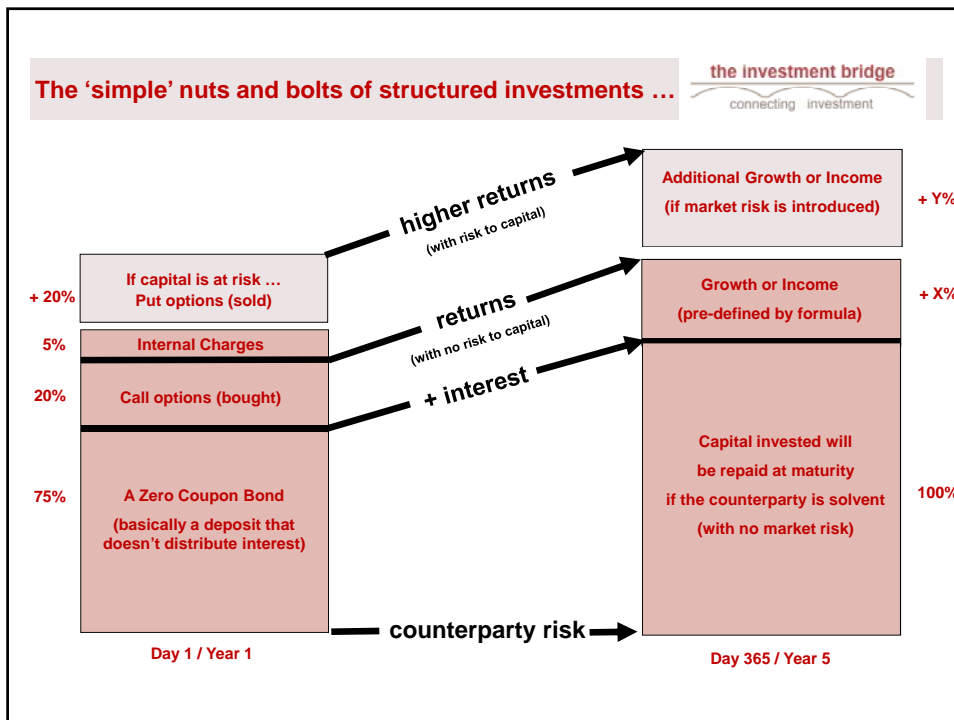
> Generally, and if not educated to believe, accept and tolerate something else, most investors would choose to :-

- 1. Pre-define investment risk : no-one takes investment risk 'for the sake of it'**
 - structured investments can remove, reduce or at least pre-define investment risk (levels and type)
 - this is achieved by formula/definition : and is not subject to the vagaries of active fund management

(though it is subject to counterparty risk)
- 2. Pre-define potential investment returns : commensurate with risk profiles**
 - structured investments can potentially define and optimise the parameters of investment returns
 - this is delivered by formula/definition : and is not subject to the vagaries of active fund management

(the risks are borne by the counterparty)
- 3. Remove direct charges : low or even no charges are obviously ideal**
 - structured investments state returns after charges : capital is invested without direct deductions

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Let's talk counterparty benefits ...



- > **No investment is perfect : but consider the benefits of credit risk / counterparty exposure**
- > **Counterparty risk is not hidden : by providers or advisers**
- > **Counterparty risk replaces a multitude of risks investors have been 'educated' to tolerate:-**
 - *market risk, ie downside, loss, risk*
 - *investment / market timing risk*
 - *active fund management process / performance risk*
- > **Counterparties take the market and performance risks that investors think they can't avoid**
- > **Counterparties CONTRACTUALLY AND LEGALLY define risk and return, via the terms of a bond**
- > **Some 'clever stuff' may be going on : removing market risk and pre-defining returns is challenging**
 - **but, counterparties carry the risks of the investment process : not investors**
(this is critical : contrast it, for example, with actively managed absolute return funds)
- > **If a counterparty remains solvent they are LEGALLY OBLIGATED to deliver the returns they stated**
 - many investors find it easier to consider whether a major financial institution is likely to be solvent in 5-6 years time than what may or may not happen to the stockmarket (and 'traditional' investment funds)
- > **Savers and investors can and do understand 'credit risk' : they know:-**
 - if they place their deposit with a big bank, that doesn't have major need or appetite for their funds, they get 0.5%
 - or, if they want or need a higher return, if they deposit with a smaller bank, that wants their funds more, they can get 3%
 - they remember Icelandic banks, Northern Rock, etc

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So, what have the issues been ...



- > **Removing, reducing or at least defining the levels and types of risk - and pre-defining returns - is compelling**
- > **There's nothing wrong with counterparty risk : it's a performance issue**
 - but client's tolerance for risk and appetite / need for returns must be identified and suitable investments selected
- > **It's therefore critical the Structured Investment industry meets / EXCEEDS guidance / expectations in respect of :-**
 - being clear about where investor's money is invested : in the bonds/securities issued by a single institution
 - clearly explaining relevant counterparty risk
 - prominently stating that capital is at risk
 - using language the target audience can understand
 - not describing products as 'protected' or 'guaranteed' if this is inaccurate or misleading
 - explaining the circumstances when FSCS coverage applies, and when it does not
 - the over-arching principle : fair, clear and not misleading
- > **It's not rocket science :-**
 - structured investments ALWAYS do precisely what they say on the tin
 - but the tins have to be labelled properly : and advisers and investors must read and understand the labels
- > **Too much product talk and not enough investment thinking and language**

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Divided opinions : perpetuated 'faction' ...



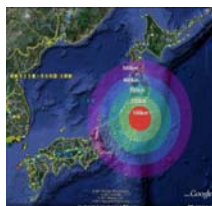
> Fragmented / divided opinions amongst UK independent advisers / commentators ...

- ... they're complex !
- ... the charges are too high !
- ... dividends are an important part of the total return !
- ... they cap the upside !
- ... there's no liquidity : investors are 'locked in' !
- ... we've educated our clients to understand that they can't 'have their cake and eat it too' !
- ... you can't have equity returns without equity risks !
- ... risk can be controlled through diversification and time !
- ... they (structured products and derivatives) are a zero sum game !
- ... the only people that win are the investment banks !
- ... okay, whatever ... but it's 'the wrong time in the cycle' to buy protection !
- ... oh, before we forget, if it looks too good to be true it probably is !

> FACTS, KNOWLEDGE AND UNDERSTANDING NEED TO REPLACE 'FACTION'

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Issues the industry must recognise and respond to ...



> Industry events echo loudly and for a long time : precipice bonds, Lehman Brothers (NDF, DRL, ARC : Keydata)

- high profile incidents : but actually isolated in terms of the providers involved and (certainly for Lehman Brothers) volume
- the lowest common denominators cast shadows over the best (shadows versus halos)

- the industry must collectively improve best practice : and restrict oxygen for the lowest common denominators

> The perception (reality?) that High Street value is poor : this will remain an industry whipping post

- in particular, structured deposits
- plus, the lack of (independent : any?!) advice is evident and will be under increasing scrutiny
- is the High Street trading on captivity, ignorance and opacity? Time to prove this is not the case

> The perception (reality?) of too much sales and marketing focus and not enough evidenced investment thinking

- investment thinking (research, asset allocation drivers, portfolio construction emphasis) simply not evident enough
- more transparency wanted regarding actual returns, to validate risk/return trade off : 'good news' proof

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Distribution dynamics : Structured deposits ...



> For institutions that own customers and advisers/sales forces (that are owned by shareholders):-

- the 'name of the game' is simple : profitably sell as much product as possible, as quickly as possible
- one size fits all sales, scale and volume is wanted : leading to standardised 'fast food' product strategy
- customers are offered what they're most likely to buy : which may not sound like such a bad thing ...

... but what uninformed/non-advised/ill advised customers are likely to buy may be a world apart from the best investment

> Easy Products' optimise sales opportunities for providers ... not investment propositions for investors

- plain vanilla FTSE 100 offerings are not necessarily poor value, per se
- or inexperienced investors plain vanilla can be a sensible 'stepping stone' towards equity investing
- and it's difficult to put a price on the value of 'reconciling hearts and minds', for cautious investors
- but low participation rates/low caps are not likely to be good value for more experienced investors

> 'Big brand' High Street providers rely upon their clients remaining ignorant of better propositions

- which are almost always available through independent advisers and specialist providers
- 25,000 free thinking and opinionated IFA's are not a volume game
- IFA's have no interest whatsoever in whether or not a provider maximises sales

> Distribution dynamics (not manufacturing capabilities) have shaped the perception of structured investments

- there is too much preference for simplistic headline rate driven product marketing
- there is not enough inclination towards investment thinking and objective advice
- the irony is that the firms that have the greatest resources do the least with them

> Better customer value will be good news for the High Street (and its shareholders)

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Regulatory and industry focus points for the future ...



> The FSA deserves recognition for its work so far, in its far reaching reviews : but has it achieved its aims?

- the aim in two words : **protecting investors**
- achieved through provider and adviser intervention : 3-4 providers removed from the industry
- but negated by individuals involved seamlessly resuming business elsewhere (plus ca change...)

> The FSA (and advisers / investors) must identify the cause of problems : not respond to the symptoms ...

- deposit wrapped 'investment linked' products remain 'light touch' regulated : an anomaly that should be addressed
- the risks of small independent providers are clear (and have been starkly exposed : lessons of the past must be learnt)

> The FSA must ensure its own guidance and prescriptions (Moneymadeclear, etc) are clear

> Finally, remember, the FSA's review of structured investments highlighted many generic issues

- the focus and reviews surpass any scrutiny seen in other investment areas
- and certain/many aspects of advisory failings (diversification, etc) were not specific to structured investments

> The Structured Investment industry must do more to self regulate and raise its own bar ...

- it can and should consider the credentials, capabilities, processes and approach of participants
- small independent providers, without scale and resource : prominent in both precipice and Lehman Brothers

> Oxygen for the lowest common denominators can be restricted :-

- **Supply** : Issuers / counterparties must be increasingly discerning about who they will trade with
- **Demand** : Advisers must (and are) increasingly voting with their feet in a 'flight to quality'
- **Regulation** : Increased scrutiny and intervention (of providers, individuals and products)

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The final word ...

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- > This is a £50billion industry in the UK and a £1trillion industry globally : that is in the ascendancy
- > Structured Investments offer something that neither active or passive funds are capable of offering
- > 'Best of breed' structured investments have a place in investor's portfolios
- > Differentiation is essential : clearly 100 providers issuing 1000 investments a year are not all the same
- > Knowledge and understanding is critical
- > *Particularly in the prevailing economic environment, surely all pragmatic, objective, client-centric advisers and commentators – including the professional and national press – need to recognise the obvious benefits of investors aligning 'best of breed' investment solutions from all available areas of the investment universe to achieve diversified, balanced, optimal investment portfolios ...*

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Thank you : any questions ...

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About The Investment Bridge ...



About The Investment Bridge

The Investment Bridge is an independent and privately owned consultancy firm, connecting specialist investment knowledge, expertise, resources, services and input across the investment community, including facilitating access to specific and potentially exclusive investment opportunities.

Bespoke Expert Services and Input to meet client needs

Services, support and input are developed on a bespoke basis for clients, potentially encompassing:-

Provider and Product Assessment and Strategy

Expert assessment of both 'top-down' and 'bottom-up' aspects of business plans at Provider and/or Product level. Advice on market, sector, positioning, distribution, including regulatory resource and input, service provider selection, costs, commissions and fees. Strategic thinking and business planning : all aspects critical to success.

Provider and Product Branding, Marketing, Distribution and Sales

Specialist advice on developing Provider and Product branding, including press and public relations, marketing, distribution and sales. Website, corporate collateral, effective CRM and marketing, including brochure-ware and presentations.

Bespoke/Exclusive Solutions, and Research and Due Diligence Input for Wealth Managers and Advisers

Guidance and access to major investment banks and specialist structured investment providers to develop bespoke and/or exclusive propositions. Expert independent input to Adviser due-diligence processes of Providers and Products.

Educational Masterclasses : White-Labelled Seminar Services

Educational Masterclass 'teach-ins' for Providers and Advisers, from basic to advanced level. White-labelled presentation services for Wealth Management and Advisory firms seeking to engage Professional Connections and/or clients (existing and/or prospective) in engaging investment seminars.

Industry Conferences and Events

Input to and involvement with industry conferences and events, as chair, key note presenter, speaker and panel participant .

Management Consultancy and Non Executive Director Services

The Investment Bridge provides input and services on a full management consultancy or project basis. Experience, professionalism, integrity and business acumen are key requirements for any Board. The Investment Bridge can contribute at Board and Senior Management level, including providing services as a Non-Executive Director.

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Founder and Managing Director : Chris Taylor ...



Prior to founding The Investment Bridge, Chris was Managing Director at Incapital Europe, the London-based affiliate of Incapital, a US-based investment banking firm and leading independent provider of structured investments and fixed income securities for professionally advised investors.

From 2007 to 2010, Chris was founder and Chief Executive of Blue Sky Asset Management, a multi-award winning boutique investment firm specialising in research backed structured investments for the intermediary business channel, with tailored offerings for discretionary managers, private client stockbrokers and institutions. The business of Blue Sky Asset Management was acquired by Incapital in July 2010.

Between 2006 and 2007, Chris was Managing Director of the Structured Investment Division of Dawnay Day Quantum, a subsidiary business within the Dawnay Day Group, a privately owned Private Equity, Property and Financial Services group.

From 1996 to 2006, Chris evolved his career in the investment industry whilst with HSBC Asset Management, the global investment business of HSBC Group. Chris was involved in the distribution of actively managed and passive index funds (and was responsible for setting up the UK's cheapest FTSE 100 tracker, with an AMC of just 0.25%, in the early days of passive fund management in the UK), actively asset allocated passive funds services, multi-manager and alternative funds and HSBC's structured products business, where he was Director of UK Structured Products Distribution, with multi-channel (internal and external) distribution responsibility.

Chris's financial services career dates back to 1987, and he has been actively involved with the structured investment industry since its earliest days in the UK, in the mid 1990's – playing a significant role in its creation and in many of its turning points over the years. He was awarded 'Highly Commended, Outstanding Industry Contribution' in both 2009 and 2010, and was also responsible for creating and delivering the most comprehensive, and award-winning, educational programme ever delivered by the UK structured product industry, in 2010.

Chris is a well known and highly regarded investment industry figure, with a prominent profile in both the trade and national press, regularly contributing to media and industry conferences and events to help raise the industry bar and promote the industry amongst advisers, investors and commentators.

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