ASIC Summer School 2012 – opening statement

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The Hilton Sydney

20 February 2012

Introduction

Good morning everyone and welcome to ASIC Summer School 2012: *Building resilience in turbulent times*.

Welcome to Country

Ladies and gentlemen, I would like to acknowledge that we meet today on the land of the Gadigal people, the first peoples of this Sydney region. ASIC pays its respect to the Gadigal people and we are pleased to ask Uncle Charles Madden, an Elder of Gadigal country, to formally welcome us to the land of the Gadigal today.

[Welcome to Country]

Thank you Uncle Chicka for your warm welcome to Gadigal Country.

Ladies and gentlemen, on behalf of my fellow commissioners, Belinda Gibson, Peter Kell and Greg Tanzer, and on behalf of all ASIC staff, I welcome and thank you for supporting this important event.

I think Summer School is an excellent opportunity to discuss what's going on in the markets as well as to meet people from around the world. For those who have travelled to Sydney for this event, I hope you get to enjoy the wonderful sights and experiences this city can offer.

Summer School is also a valuable learning opportunity for ASIC staff. Each session will be recorded and made available to ASIC staff, as well as, Summer School attendees via webcast.

We are fortunate to have some distinguished speakers lined up over the next two days.

I'd like to give particular thanks to our speakers who have travelled from overseas:

- Maureen Jensen, Executive Director and Chief Administrative Officer, Ontario Securities Commission, Canada
- Edouard Vieillefond, Managing Director, Regulatory Policy and International Affairs Division, Autorité des Marchés Financiers, France
- Dr Adrian Blundell-Wignall, Deputy Director, Directorate for Financial and Enterprise Affairs, OECD; and
- Ashley Alder, CEO, Securities and Futures Commission, Hong Kong

This is my first Summer School as Chairman of ASIC since taking over from Tony D'Aloisio last year.

I'd like to acknowledge the good work that Tony did in getting ASIC through the onset of the GFC. It was a challenging time with markets in turmoil and regulators under pressure to react, particularly on short selling.

- The ASIC restructure in 2008 made the organisation more stakeholder focused. It broke down the silo mentality and allowed ASIC teams to get closer to industry in terms of dialogue. It also allowed better scrutiny of participants through surveillances.
- Tony oversaw a major expansion of ASIC's role – the regulation of credit, transfer of market supervision and then competition in equity markets.
- An important legacy of Tony's is the MoneySmart website, which won the Australian Web Award for best Government Website for 2011. MoneySmart is fundamental to ASIC's strategic outcome of confident and informed investors and financial consumers.

Since the last Summer School, there have also been changes in ASIC's Commissioners. Shane Tregillis, Michael Dwyer and Peter Boxall have moved on to greener pastures.

Replacing them are Peter Kell and Greg Tanzer. Peter joined us from the ACCC and Greg has joined us from IOSCO. Both have previously worked for ASIC and they bring a wealth of experience to the organisation.

Overview of Summer School Agenda

The theme for this Summer School is 'Building resilience in turbulent times'.

Each day there will be a sub-theme.

- Today's sub-theme is 'Recession, risk and regulation – building resilience in markets'.
- Tomorrow will be 'Emerging and evolving markets – opportunities and threats'.

Tonight we have a special dinner event with a keynote presentation by Bernard Salt and a high-powered panel discussion moderated by Peter Thompson.

For lunch tomorrow, we will be joined by the Hon David Bradbury, Parliamentary Secretary to the Treasurer.

There will be many interesting presentations and panels over the next two days, but before we begin, I'd like to talk about the task currently facing ASIC.

Over the last six months, I have been speaking about ASIC's three strategic priorities. They are:

- Confident and informed investors and financial consumers;
- Fair and efficient financial markets; and
- Efficient registration and licensing.

You will find ASIC's strategic framework in your delegate packs and that framework contains more details on our priorities.

In order to achieve our three strategic priorities, ASIC needs to build resilience in the Australian financial system to prepare us for the next financial crisis.

Building resilience in the Australian financial system

There are three key challenges facing ASIC over the next decade to build resilience in the Australian financial system. These are:

- **1st challenge:** The growing regulatory perimeter, particularly with the exponential growth in superannuation – more products, more investors and greater investment funds increases risk in the financial system;
- **2nd challenge:** The increasing complexity of the financial system – products, information channels and financial markets are increasing in complexity which again increases risk in the system;
- **And most importantly, the 3rd challenge:** Leveraging ASIC's resources to be proactive because it is through proactive regulation that you build resilience. Stakeholder engagement, surveillance, education and guidance are central to maintaining confidence in Australia's financial system.

These three challenges need to be met in order to build resilience in Australia's financial system.

I will briefly expand on these three challenges.

1st challenge – growing regulatory perimeter

Superannuation is expected to grow to $3 trillion over the next decade. It will grow at twice the rate of the economy. This will increase ASIC's regulatory perimeter as more investors come into the system and money invested increases.

This is a shift of savings out of the banking system into the superannuation/funds management sector.

If you look at what the typical super fund invests in, it's equities, fixed income, property and cash.

- Growth in equities affects ASIC's market-facing teams that oversee mergers and acquisitions, capital raisings, brokers and the markets themselves.
- Growth in fixed income, property and cash impact debt issuance, managed investment schemes and mortgages. That is, activities regulated by ASIC.
- With self-managed super growing in size, they will be targeted with a range of products including structured products. Again, regulated by ASIC.
- On top of this, ASIC is responsible for disclosure by super funds.

This growth in super will also flow through to financial advisors, superannuation trustees, investment managers, custodians, research houses, credit rating agencies, auditors and accountants.

- They all play roles in supporting investors in superannuation funds and are all regulated by ASIC.
- There will also be a greater need for consumer education and financial advice due to changing demographics as baby boomers move to the retirement phase and switch to more conservative assets.

Also, a larger financial system will invariably generate more complaints and breaches.

As you can see, ASIC is significantly impacted from the growth in super. With more stakeholders and investment products, ASIC’s workload will increase. It will be a key challenge to ensure our regulation is sufficient and remains effective so that overall risk in the system is contained.

2nd challenge – increasing complexity in the financial system

While the regulatory perimeter is growing, the complexity of the financial system is increasing.

Investors

A super fund today has a wider range of investment products to choose from than ever before.

- In addition to the relatively 'plain vanilla' products such as equity or bonds, super funds and other investors can gain risk exposure through complex products.
- This includes cash or synthetic ETFs, CFDs, credit-enhanced asset-backed securities (including CDOs), credit default swaps and equity default swaps, as well as investments in hedge funds, private equity and others.

There is also more scope to invest overseas, including in emerging or 'frontier' markets. More complex products means greater risks and greater potential losses for Australian investors.

The increased risks in complex products are not just faced by retail investors. The GFC provided clear examples of non-retail investors – such as universities, councils endowment funds etc - that incurred severe losses from investing in structured credit instruments they did not understand.

Investors now have much more choice as to how to conduct their business.

- They can buy securities on exchange or through dark pools, they can choose to use automated or algorithmic forms of trading, or lend their securities to earn income.
- They can access a huge range of products, information and research on the internet and make investment decisions in a few mouse clicks.

The ever-growing range of products and investor operations means the regulator needs to be much more vigilant and proactive. This process of increased complexity is likely to continue in the future, especially while equity markets remain volatile and investors look elsewhere for yield.

Markets

In addition, the operations of markets themselves are increasingly technical and complex.

- Trades have moved from taking one or two seconds to milliseconds to microseconds. High frequency traders using this new technology have added to exponential increases in global order books.

- In the USA, this new type of trader is estimated to be responsible for 50% to 60% of market trading. The ability to undertake high speed transactions was a factor that led to the 'Flash Crash' in May 2011 where US$1 trillion of shareholder equity was wiped out in minutes.

ASIC needs to keep pace with these rapid changes in technology and prepare for their impact on the resilience of Australia's financial systems.

Increasing complexity in products, information channels and the financial markets will heighten risk and the potential for loss in the financial system. It will require a proactive regulator that is 'on the ball' and forward-looking. This leads me to my next point.

3rd challenge – Leveraging ASIC's resources to maintain proactive regulation

Following the GFC, the environment for regulation and has changed dramatically. Financial markets face heightened risk and regulators face increased expectations in their preparedness and diligence for major market failures.

This is a major challenge for ASIC, particularly with our limited resources.

A certain level of resources must be spent on reactive regulation – i.e. investigating breaches and potential misconduct, and fulfilling our statutory mandate such as registration and licensing.

While reactive regulation is mandatory, ASIC has discretion over how proactive it is. When I talk about proactive regulation, I mean being forward-looking, and identifying and addressing risks as they emerge.

- This can be done through engagement with stakeholders, surveillance (desk-based and onsite), investor education and regulatory guidance.

- These actions build resilience in the financial system as each actor in the system (investor, product manufacturer, distributer etc) meets a higher standard of conduct and understanding.

- The system then becomes more resilient to shocks, and when a market failure does occur, less money is lost.

To be proactive and forward-looking, you need to be able to identify which sectors pose the greatest risk. This requires a detailed understanding of the sector – understanding that is only gained through stakeholder engagement and surveillance.

This means ASIC needs to maintain its high level of engagement with industry and continue its risk-based surveillances.

This comes at a time when our regulatory perimeter is expanding and complexity in the system is increasing.

It is critical that ASIC leverages its resources to maintain its pro-active stance and continue building resilience in the Australian financial system.

These three challenges:

- the growing regulatory perimeter;
- increasing complexity in the financial system; and
- maintaining our pro-active regulation;

will be key to building resilience in Australia's financial system over the next decade.

Introducing Alan Kohler

Ladies and gentlemen, we have a busy schedule ahead of us over the next two days.

It should be a stimulating and entertaining program. I encourage you to participate and ask questions.

So without further ado, let's begin with the first plenary session.

It was with great pleasure that I asked Alan Kohler to be our first keynote presenter. Alan is an ABC News commentator, editor-in-chief of *Business Spectator*, founder of *Eureka Report*, and host of *Inside Business*. He's been a financial journalist for 41 years, including roles as editor of both the *Australian Financial Review* and *The Age*.

Alan will be setting the scene on which we'll base this two-day conference with his discussion of the economic landscape, the shadows that are falling across economies worldwide, and where we might be heading.

This presentation will then be followed by a panel discussion and there will be an opportunity for delegates to ask questions.

I would like to remind everyone that media are present and may ask questions in the Q&A session after they have identified themselves.

Please join me in welcoming Alan to the podium.

