

EQUITY RESEARCH, SALES & TRADING

Thomson Extel 2003 results reflect industry concerns, writes Sophie Brodie

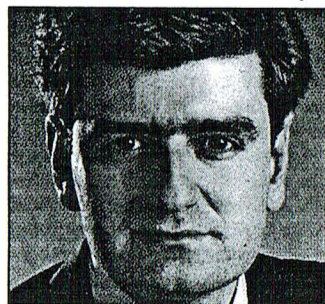
Soft commission 'set to disappear'

Fund managers have radically cut the proportion of commission they expect to be "softed" this year, according to the 2003 Thomson Extel survey.

The percentage of soft commission in managers' budgets has fallen from 10% in the 2002 survey to 1.5% in 2003. One analyst says: "The results reflect fund managers' belief that softing is dead following the Financial Services Authority (FSA) consultation paper."

The paper, which suggests abolishing soft commission and unbundling broker services, has met with hostile reaction. Smaller brokerages, such as the Eden Group, are up in arms, blaming the UK government for pressuring the FSA, the regulator, to issue proposals that they believe will force an exodus of investor commission from the UK.

Jamie Stewart, head of institutional research at Eden, says: "Political ideology is straining to neuter 'fat cats', who compromise social equality and embarrass the government. Legislators must understand that few fat cats ever dined off abuse in financial services and that for



Garcia-Cantera: need for aggregated analysis

every fat cat there are 10,000 lean and skinny cats who risk lingering deaths."

Stewart says soft commission is unlikely to be banned because London will have to tow the line of the US Securities and Exchange Commission, which is to ignore the issue. He believes that most financial services are paid for on the principle of underlying soft commission – without a detailed cost breakdown – and cannot be prohibited.

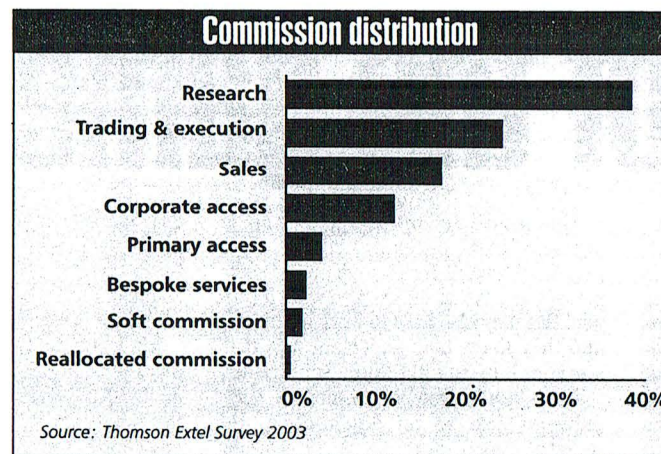
However, larger brokerages and fund managers are resigned to a gov-

ernment ban on softing, although they remain optimistic about not having to unbundle services as long as fund managers increase transparency on what they spend. Others say it is hard to see how managers can achieve greater transparency without unbundling.

According to the survey, more than 40% of buy-side managers agree that they will take unbundled services from the sell-side over the next year. Around 60% believe that paying directly for research will be important in 2004.

Other services paid for by commission have changed in importance over the year. The survey shows that fund managers expect to have less opportunity to access primary markets because of fewer initial public offerings and new regulations in the US are discouraging analysts from promoting primary stocks. This year, they attributed only 3.9% of commission to primary access, down from 5% last year.

The survey also showed that fund manager interest in top-down macro research had increased from 12% in 2002 to 16% this year. In spite of this



increased demand, several bulge-bracket houses, such as UBS and Citigroup, have recently reduced their strategy teams. Alex Ions left UBS within a day of his team winning the top Extel award for pan-European equity market strategy last week.

One analyst says: "At this point in the cycle, there is habitually more attention paid temporarily to top-down factors and more so this year, thanks to the huge growth in hedge funds, which are macro-driven." Opinions of maintenance research were divided in the survey with 31% thinking it remained important and 21% believing it to be quite unimportant.

Jose Garcia-Cantera, European head of research at Citigroup's Smith Barney, says: "What is generally referred to as 'maintenance' research may in fact be necessary. Analysts have to aggregate information such as quarterly results before they can offer clients value-added research."

The survey showed that 46% of fund managers expect to continue retrenching and consolidating in the depressed market. In an environment where there is less commission, research areas will have to compete with one another to attract clients and resources.

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