Hermes Equity Ownership Services

# The Kay Review: what needs to change?

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Paul Lee
Director
p.lee@hermes.co.uk

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# Kay Review: process

- Established June 2011 by Business Secretary (Vince Cable) to consider short-termism at UK companies and in UK financial markets
- Interim Report published February 2012, Final Report July 2012
- http://www.bis.gov.uk/kayreview
- Department of Business published response November 2012
- Two key messages
  - Dominance of markets by intermediaries
  - Excessive focus on trading activity

# Kay Review: Implications for regulators

- Rethink regulation not to facilitate the markets themselves but to ensure that they deliver for the underlying users of the markets – the companies requiring capital and the ultimate providers of that capital

- Enforce fiduciary duty more effectively throughout the investment chain
  - duty to act in good faith in the best long-term interests of clients

- Drop support for any specific valuation or risk assessment models, favour informed judgement
  - Risk is not volatility or tracking error

- Uphold statements of good practice for market participants

# Kay Review: Implications for investors

- Instil fiduciary duty across all investors
  - Review of legal concept of fiduciary duty to clarify application in investment
  - Cannot be excluded by contract
  - Fund managers must be transparent on costs, including transaction costs and performance fees, must rebate returns from stocklending

- Active stewardship seen as natural part of investment activity
  - Investors forum to facilitate engagement

- Fund manager incentives to be made long-term, tied up within fund in question

# Kay Review: Implications for companies

- Reminder of directors' duties
- Discouragements to M&A focus
- Abandon quarterly reporting game
- Consult investors on board appointments
- Enhance and sharpen narrative reporting
- Incentives to be made long-term, tied up in shares held to retirement