

# **REGULATION – A BUSINESS PERSPECTIVE**

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# Background

- Economic downturn - 2008
- Deepest dip since Great Depression
- Question – Where to from here?
- Reflex action – more regulation
- Is that correct?

# Two Views on Regulation

Dr Hughes – Sunday Independent 3.4.11

## View 1

- “He who creates laws increases sorrow” (Old Proverb)
- Regulation
  - Causes cost and injustice
  - Limits economic activity
  - Stupid and arbitrary

# Two Views on Regulation

## Dr Hughes – Sunday Independent 3.4.11

### View 2

- We have the choice of
  - Anarchy or
  - “Freedom under law”
- Regulation prevents more harm than it causes.

# What does History Prove?

Dr Hughes – Sunday Independent 3.4.11

- **30 years after WWII**
  - High regulation of financial institutions
  - Based on memory of Great Depression
  - Seemed to work with few difficulties
- **No doubt brought**
  - Higher cost of capital
  - Lack of economic innovation

# What does History Prove?

Dr Hughes – Sunday Independent 3.4.11

- Ironic – 30 years after WWII
  - Years of good economic performance
  - Good growth and productivity
  - Closing of the wage gap

**Unintended consequences?**

# What does History Prove?

Dr Hughes – Sunday Independent 3.4.11

- Freer era to 2008
  - More misbehaviour
  - Destruction of companies – e.g. Lehman Bros
  - Cost a lot of money
  - Shook confidence in the whole system

# What does History Prove?

## Dr Hughes – Sunday Independent 3.4.11

- Post 2008
  - Public incensed
  - Executives seen as creating havoc and greedy
  - Bonuses seen as obscene
  - Call to regulate remuneration

# The Divide

- **At Davos 2011**

- Business view: excessive regulation will do more harm than good.
- Regulators' view: we must go further to prevent a recurrence of 2008.

# Conclusion Based on History

Dr Hughes – Sunday Independent 3.4.11

- Regulation seems attractive
- Only questions -
  - What sort?
  - How much?

**Do it properly!**

# Types of Regulation

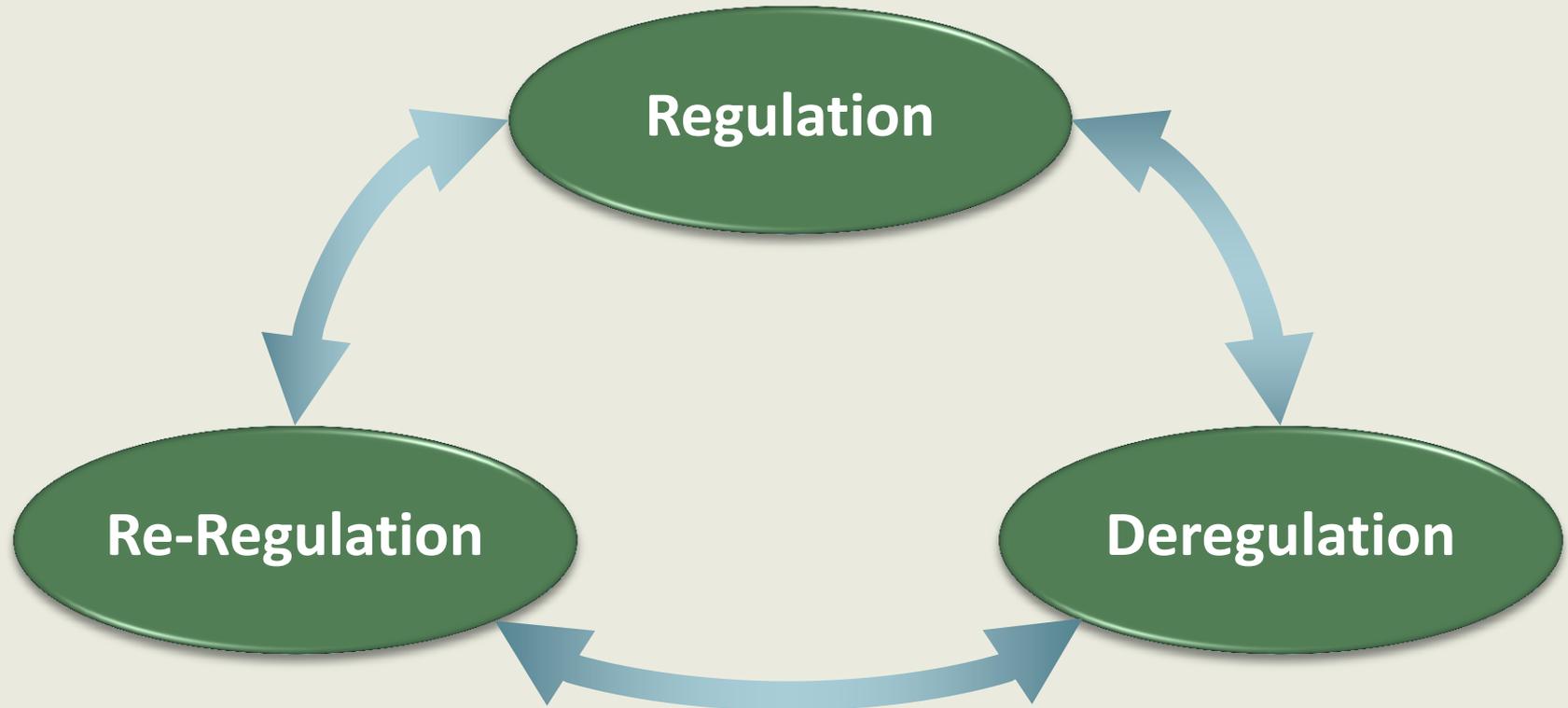
- Numbers
  - e.g. Margin or Reserve requirements
- Separation of roles, functions and services
  - e.g. Split simple banking services from high risk products and services.
- Transparency
  - Improved information
  - Better reporting and accounting standards

# Types of Regulation

- Good regulation requires the right balance of measures
- Too much regulation pushes people into opaque and un-regulated areas.

# Regulatory Cycle

Dr Hughes – Sunday Independent 3.4.11



Is this inevitable?

# The South African Experience

## Strengths

- World Class
  - Accounting (Early on IFRS)
  - Auditing
  - Corporate Governance (King III)
  - Regulation
  - Ombuds Process

## **BUT**

- Poor Competitiveness

# The South African Experience

## Why did we do well in 2008?

- Good regulation?
- Exchange control?
- Business judgement?
- Good management?

**All of the above!**

# The South African Experience

## Poor Competitiveness

- Over regulation stifling growth and job creation?
- Lack of scale?
- Skills shortage?
- Labour dispensation?
- Strong currency?

**Probably education!**

# The South African Experience

## The JSE 1994

- Closed floor
- Screen trading
- Dual capacity
- New capital requirements
- London listing requirements
- King I
- Opened to banks and foreign brokers
- Deregulation of commissions

**New legislation required**

# The South African Experience

## The JSE Today

- Market capitalisation Rbn6785
- World ranking 19
- Number of listed companies 405

# The South African Experience

Philip Matlokala – Financial Mail 25.2.11

## Financial Sector

- Had to contend with rapid and far reaching changes
- Third longest employer in private sector
- Two year's ago 14% of labour force
- Now 12% of labour force

# The South African Experience

## Flood of Legislation & Regulations

- Stock Exchanges Control Act
- Listings requirements
- King III Corporate Governance
- Financial Advisory & Intermediary Services Act
- Consumer Protection Act
- Companies Act (May 2011)
- Protection of Personal Information Bill

**Basel III**

# The South African Experience

## Legislation & Regulation

- High costs of compliance
- High barriers to entry (∴lack of transformation)
- Fear of examinations = retirements
- Intermediaries focussing on fewer products to clients' detriment

# The South African Experience

## Question by Peter Matlokala

“What is the cost of implementing first world legislation in a developing economy such as South Africa?” *(Adapted)*

Can we afford not to?

# Quo Vadis

## Areas to be Addressed in SA

- Transparency of bank charges
- Regulation of off market transactions (e.g. OTC derivatives)
- Regulation of credit rating agencies
- Shift to regulation based on principles, ethics and “treating the customer fairly”

# Quo Vadis

## Areas to be Addressed in SA

- Closing the cracks between regulation
- Deal with long term nature of financial service products (esp. insurance)
- Enhanced financial consumer education
- System to wind down large entities in times of need

# Conclusion

- No one believes financial services sector can regulate itself
- We have proof that poor conduct can lead to systemic risk
- Best codes in the world not better than people who implement them

**REGULATION IS CRITICAL  
BUT MUST BE WISE!**