Compulsory seat-belts for investors?

1. Suitability tests for dog-owners

Everything's going to get better. If the Swiss government gets its way, which has been much approved by all the key opinion-makers, Switzerland will soon become one of the safest places in the world, as far as encounters with dogs is concerned. According to a proposed revision of animal welfare legislation, all dog-owners will be obliged to attend a one-day course and provide evidence of its successful completion. Pit bulls, poodles or pugs: all dogs and all dog-owners are equal before the law, and so we shall see, Saturday after Saturday, hordes of dogs and their masters and mistresses making their way to dog school, so that, after completing a top-quality canine education, they come into possession of the desired state certificate.

We shall not concern ourselves further in this Investment Commentary with the admittedly not earth-shattering topic of dog ownership. However, the regulatory process in this instance is typical enough to be worth some further attention. How did this really rather laughable proposal come about? It began, almost exactly a year ago, with a tragic accident, in which a six-year-old boy was mauled to death in a Zurich suburb by three pit bull terriers that had broken out of an obviously inadequately secure cage. Understandably enough, this event was a tremendous shock to public opinion, and occupied the headlines for several weeks. It became a political issue, with a petition signed by 170,00 citizens and 147 federal MPs, and it was obviously inconceivable, given this pressure from the street and the people's representatives, that the already-planned revision of animal welfare legislation should be addressed without due attention being paid to this issue.

The consensus that dog owners should be, so to speak, put on a leash by the state evidently continues, although as the Weltwoche (no. 48, p. 31) recently correctly pointed out, this individual tragedy was not followed by mass attacks by pit bulls run wild, and we are still way off any kind of national state of canine emergency. But once set in motion, the machinery of regulation is not so easy to stop. For in whose interest could it possibly be to put an end to this legislatory overkill? Not politicians' for sure. For the avoidance of concrete action – non-activism – is generally speaking not a promising approach in politics, and it might also rebound in real terms if another pit bull struck again. The government? Absolutely not. The prospect of creating a new Federal Institution for Dog Ownership (FIDO) to oversee the consistent implementation of the regulations across all the cantons, and to represent Switzerland on international canine ownership bodies is far too tempting. Dog-lovers' organizations? No way. For they glimpse an opportunity to have their social relevance carved in stone once for all time, and indeed to be compensated for the obligatory canine behavior courses. What could be more attractive for the chairperson of such an association than to be taken seriously for once, to be state-certified, as it were, with the chance to have all dog-owners as compulsory members of their guild? And what about poor Mrs Dog-owner and her dachshund? Not really, either, for the effort of defending her freedom would be disproportionate compared to the tiresome, but more or less acceptable trip to the dog school.

In economics such a situation is described as an "asymmetric incentive situation", and helps to explain the unstoppable drive to more and denser regulation. In our (democratically self-legitimating) system, there is no authority that can point out that the existing legislation is perfectly sufficient to correct recurring mishaps. How badly we need such an authority, and what good sense it would make to give it some political clout! Thus, the articles in the Swiss Criminal Code concerning involuntary manslaughter and bodily injury due to negligence (StGB Art. 117 and 122) contain exactly the right terms to enable the owner responsible for the three pit bulls to be appropriately punished. A degree of courage on the part of the judge might enable possible intent to be determined, and thus provide grounds for a very high sentence. The threat of such punish-

ment should be sufficient as a generally preventative measure, so that, while individual incidents might still occur, there would in future still be no threat of mass attacks by pit bulls. Instead, we have the administrative approach, and ultimately responsibilities (relevant in the prosecution of extreme cases) will become blurred, for in future the lack of responsibility of the dog-owner will be supplemented by the possible inadequacy of his canine behavior trainer, and inadequate supervision by the organs of the dog-owners association, not to mention inadequate higher-order supervision by FIDO. So then, after the next individual incident, it will become "unavoidable" to further tighten the animal welfare legislation and introduce specific penalties. This is known in the jargon as "down-scaling".

2. MiFID as a weapon against pit bulls

The blurring of responsibilities is the key problem that always arises when regulation becomes denser. The MiFID guidelines that come into force within the EU at the beginning of 2007 illustrate both this and also the equally serious indirect implications. MiFID stands for "Markets in Financial Instruments Directive" or "Guidelines of the European Parliament and Council concerning Markets for Financial Instruments". They were approved in 2004, still under the impact of the collapse in prices after the bursting of the technology bubble and the disaster on the (German) "Neue Markt". Their main aim is to protect investors from all possible dangers they might encounter, as might innocent children on their way to school.

It is true that the financial markets are places of both danger and crime. If we are right, there is indeed almost a certain regularity about the occurrence of financial scandals that damage the interests of investors. Over the last thirty years they have occurred every five to eight years. In the 1970s it was the splendiferous Bernie Cornfeld with his IOS fund, then later the inconspicuous Werner K. Rey, then the European Kings Club with its branches in Germany and Austria, and more recently Dieter Behring, the unusual laboratory assistant from Basle. All in all, they have blown away several billions of francs worth of funds entrusted to them.

This regularity allows some conclusions about the memory span of investors. It appears not particularly long, nor to be particularly effective. For, across the board, the schemes themselves and the characters involved exhibit recognizable similarities, which should make it possible to avoid falling for them next time round. They always promise returns that are well above-average and far too consistent. The funds invested always wind up in interlinked and ultimately completely intransparent legal constructs spread over multiple jurisdictions. Serious auditors are engaged infrequently, or only for more or less irrelevant subsidiaries. It is never clear from what source the above-average returns actually come. Either because the source does not actually exist, or exists only on an utterly inadequate scale, there are always holes that must be stuffed with money from ever-new investors – which is why marketing (and the high commissions required for this purpose) is of great importance. Ultimately most such schemes are revealed to be pure pyramid constructs based on a continual supply of new investors to satisfy the previous ones. This is the familiar chain letter principle, and it does not function ad infinitum. The devil takes the hindmost.

The people involved mostly have in common a lack of education and an inadequate professional background, but also a certain charisma that compensates for such defects. Bernard Cornfeld was a door-to-door salesman for an American stock fund before he built up his European empire. By 1968, that is, five years before the collapse of IOS, he was paying little attention to business but, as a member of the jet set, a good deal to attractive women. Damara Bertges, devoid of any financial knowledge whatsoever, is still celebrated today, despite a criminal sentence, as some sort of female Robin Hood fighting against "high finance". Behring in Basle attracted attention through his exorbitantly costly renovations of properties in the old town, while dressing aloofly in black. For a long while it seemed to occur to no-one that an apprenticeship as a laboratory assistant was hardly likely to be sufficient for managing hundreds of millions of francs, although the idea is about as absurd as a banker suddenly starting to deal in cyanide or polonium …

The fascination exercised by these miraculous multipliers of money regularly extends to a certain number of the pseudo-prominent. In the case of Werner K. Rey, this circle extended well into the world of Swiss banking, and an extraordinary number of personalities from politics and business also fell for Behring. The tragedy here is that their involvement often serves as a reference for "less professional" investors, and thus significantly increases the number of those affected.

No question: there always are pit bulls around the financial markets, and it is often the most innocent who get mauled. Nevertheless; are these more than isolated incidents? Is there really a

danger of mass attacks? Not according to the figures. To take the most recent case, Behring appears to have caused damage to the extent of perhaps 500 million francs. Set against the total Swiss investment volume of over 4,000 billion francs, this is about 1/10 per thousand, and if we assume that the next major incident will not occur for another five years, then we are somewhere in the nano-region of relevance for Switzerland as a financial center. The same applies for the bigger incidents within the EU. There is not, and never has been, any kind of epidemic or threat to the system.

That this is so does not affect the degree of culpability of the perpetrators, nor should the often not inconsiderable losses suffered by imprudent investors be trivialized. It is, though, disproportionate to derive a general need that goes beyond the already available regulatory and penal measures to protect investors from financial scandals caused by what are actually remarkably few financial pit bulls. But the EU's new MiFID guidelines are based precisely on the assumption that all the players on the financial markets are pit bulls, and none of them are spaniels, poodles or pugs.

3. What is MiFID trying to do?

According to Article 19, paragraphs 4 to 6 of the 44 pages of small print that make up the guidelines, providers of financial services are subject to the so-called "suitability doctrine". Specifically, this means two things. Firstly, a provider must check whether and to what extent a recipient is "suited" for this or that product or service. He must be aware of his client's knowledge and experience of the specific product or service; he must possess information about the financial feasibility of the enterprise; and he must ascertain (and, naturally, document – more on the problem of the burden of proof below) the personal goals of the client (investment horizon, risk appetite, risk profile, investment style). Should the financial service provider be unable to obtain this information, or obtain it only to an insufficient degree, he must abandon the enterprise, or possibly even the entire client relationship. Secondly, the financial service provider must know and communicate the risks of the financial instrument in question, ascertain the characteristics of the transaction, and be aware of the frequency of such transactions and the impact of the transaction on the client's (overall) portfolio (and, of course, document this too – see below). A relatively small number of exceptions are permitted with regard to so-called professional investors.

The MiFID implementation instructions set out in extensive detail how the suitability checks are to be carried out, both for investors and for products. Overall – and despite all skepticism, this must be unrestrainedly acknowledged – there is nothing basically wrong about them. On the contrary, one might almost think that parts of our instruction manual, which we, as an ISO-certified asset management bank, have been using since 1998, had been taken over more or less tel quel in the MiFID text and implementation instructions. Thus, we have long held the view that the risk components that are part of more or less complex structured products should be able to be presented to the client at any time in a disaggregated form. Accordingly, asset statements that show the effective exposure in asset classes such as fixed-interest, stocks, commodities, and such are part of our day-to-day advisory service, as is a dynamic presentation in terms of value-at-risk calculations. It is also a matter of course to use a client profile to identify the most appropriate investments. Or, to put it another way, if there is a bank that should have nothing against MiFID, because it has long based its systems on exactly these principles, then it would have to be our bank. We might therefore, for once at least, forego fundamental opposition, conclude this Investment Commentary at this point, and wish a Merry Christmas to all our readers.

The reason for our misgivings lies not in the feasibility, nor indeed in anxiety about expensive adaptations of the bank's software, should MiFID in some form be incorporated into the Swiss regulatory framework. Rather, we believe that MiFID represents a far more fundamental assault on the basic principles of a free capital market than many people realize. The consequences, as we shall see, will be, for the investor, a deterioration of his market position, and for the provider of financial instruments in search of capital, a measurable price increase for higher-risk projects.

There is a difference between the rules that our bank, for instance, has for years voluntarily adopted in its business dealings and the elevation of such rules to universally applicable legal standards, inasmuch as the latter state provides a cause of action when the rules cannot be complied with or appear to have been breached. In this way, a relative standard with at most internal sanctions is transformed into an absolute standard with all the penal consequences available under the law. The elevation of best-practice rules to legal standards, as stipulated by MiFID, contains within it an immense politico-legal problem. However appropriate their application seems in

our lengthy experience, the rules lack characteristics that are unambiguous and thus suitable as a basis for legislation. It is as if a handbook of etiquette were to be incorporated into marital law. Using it as a basis for legal action, with all its consequences, would have quite the wrong effect. No-one would any longer dare to marry, and people would have to find more offshore opportunities to satisfy their interpersonal requirements.

4. "Know your customer" vs. private sphere

There is no question that top-quality financial advice should take account of the client's personal situation. For any financial instrument, whether a "boring" bond, a highly interesting stock or an extremely complex hedge fund, is likely to have specific characteristics that either do or do not suit the overall situation. This "overall situation" includes all possible objectively determinable components and subjective states that make up the person of a client and business partner. In our ISO process handbook we deliberately use the term "case history" to describe the process of getting to know the client. We use a medical term, and we know that in medicine that any diagnosis will err if the case history is slovenly.

In our understanding of free business relationships it has always been the case that it is up to the client what he wishes to disclose. Many people have more than one banking relationship, and do not, for good reasons, necessarily wish that one bank knows of assets with another bank. But if MiFID Art. 19 is to be taken seriously, this will no longer be possible in the future. Every service provider will have to know everything, for if he does not, he runs the risk of drawing false conclusions on personal circumstances, and possibly giving wrong advice or selling the wrong ("unsuitable") products. Already here, we see how difficult in practice is legal compliance with ambiguous etiquette-like guidelines. How far should financial service providers' intelligence systems go with their clients, so as to avoid any (actionable) mistakes? Where does "know your customer" stop, and an intolerable surveillance system start?

Apart from this obvious intrusion by the new EU financial markets standard into the individual's private sphere and right to self-determination, the effective obligation on banks to categorize their clients contains another weak point. The standard already makes a – fairly discriminatory – distinction between "professional" and consequently other, unprofessional, clients. Within this latter category, banks will not be able to avoid further classification: "retail" as a euphemistic description of risk-incompetent have-nots, "risk-averse" for scaredy-cats, "risk-oriented" for speculators and the like. Apart from the already-mentioned problem of discrimination – and this in an age of racial discrimination legislation – such a classification does justice neither to the actual economic situation nor to the subjective state of the investor. Rather, it is the case that most people have both differing objective conditions and subjective feelings concerning different parts of their assets. It may be that the first 50 percent, for example, should under no circumstances be put at risk. The next 30 percent could if absolutely necessary be done without, but subjectively, rather not. The last 20 percent could well be regarded as something of a gambler's stake. In which category according to MiFID does such a client belong? Any categorization will be wrong! Even the retail have-not generally has some part of his assets that he can, and may wish to, put at stake. Why should he not be allowed to buy a couple of red-hot options?

Furthermore, the client situation is not stable, either subjectively or objectively, but rather dynamic, and sometimes capable of very rapid change. Who can forget how, between 2001 and 2002 bold big investors on the "Neue Markt" suddenly mutated into conservative lovers of absolutely safe (whatever that may mean) titles? And as bankers, how often have we heard that people had never really wanted those dangerous things from the "Neue Markt"?

Ultimately, the elevation of best-practice rules to legal standards blurs the responsibilities of advisers and clients. While in the past, the adviser had, within the relatively wide bandwidth permitted by the legal concept of "gross negligence", room for maneuver whose extensive exploitation could not provide cause of action, in future he will have to prove that he has not infringed any of the significantly more restrictive and supposedly unambiguous MiFID rules. To this extent, the burden of proof will be put upon the adviser in the case of losses.

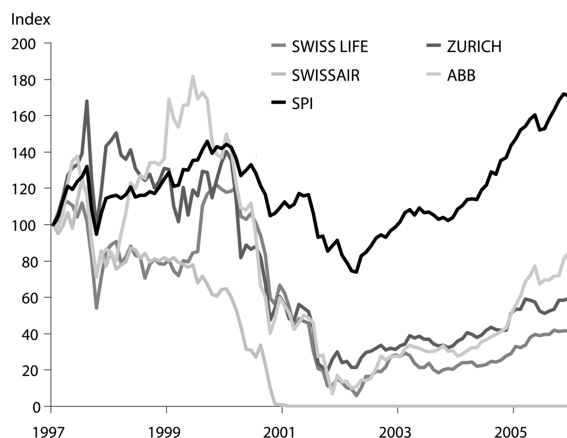
5. Problematic approach to probability

It is unquestionably correct that clients should be informed as far as possible about the characteristics of financial products. Not for nothing has our bank invested large sums, and far larger amounts of intellectual effort, in software that makes it possible to give due attention to the risk aspect of portfolios and their components. Nevertheless, it would be unwise to overestimate the possibilities of managing risk in this fashion.

For we obtain the information we use to classify financial instruments from past data series, and generally draw direct conclusions for the future from this previous behavior. Thus, we assume that a stock that has been trundling along on the stock exchange with a relatively low P/E ratio and relatively low volatility will behave similarly in the future. And we do not assume that a high-tech stock, whose price already discounts a ten-fold increase in profitability, and which bounces up and down daily within a bandwidth of several percentage points, will overnight transform itself into a moderate blue chip. The allocation of financial instruments to so-called risk categories makes sense to the extent that they normally remain within the defined bandwidth, so that the allocation remains relatively stable. MiFID is also based on this assumption.

The problem is simply that we are dealing merely with probability, and not with certainty. It is only probable to a certain degree that the allocation of a financial instrument to a risk category will also be correct in the future, and when the change comes, it is already too late. This can be demonstrated with a couple of at the time unquestioned Swiss blue chips. Who would not, prior to 2001, have reckoned the shares of ABB, Swiss Life und Zurich Financial Services as among the stable stocks, and who would not have said the same of Swissair, at least till about 1999? Almost overnight, these so-called quality stocks mutated into veritable high-volatility monsters, whose prices have in the meantime stabilized, but at a significantly lower level – in Swissair's case, at zero.

Roulette with blue chips



Source: Bloomberg; analysis

What would have been the benefit of an, at that time, entirely reasonable and correct allocation of these shares to the blue chips? If wrongly interpreted, not merely nothing, but less that that. For the wrong interpretation would have resulted in the erroneous assumption of a guaranteed normality. Herein lies the danger of the risk categorization required by MiFID: in the notion that the categorization itself involves no probability assumptions, and that the "normal" degree of fluctuation within the various risk categories can be relied on. Nothing could be more misguided or more disastrous.

For the real risks are to be found not in the expected volatilities and their confidence intervals, but in the surprise that things turn out quite differently from what one could have expected. Hands on hearts: what do we actually know at all? What justification have we for expecting "normal" developments? Can we in fact, on the basis of, statistically speaking, really rather short observation periods with not that many data points, really determine "normally" expected behavior? In his latest book, *Fraktale und Finanzen* (Piper-Verlag, 2005), the mathematician Benoit Mandelbrot shows that the frequency distribution of returns can by no means be correctly described by a normal Gauss distribution, and particularly that both negative and positive events occur far more frequently than might be expected. Furthermore, such extreme events seem to come together within relatively short periods of time ("clustering").

A risk categorization of financial instruments thus provides at best some indication of what might happen, but certainly no more than this, and nothing in any way unambiguous. Even when dealing with "low-risk" fixed-interest investments, caution is required when making statements. Who says, for example, that certain government bonds will ever be redeemed? What exactly is the difference between some European Kings Club's pyramid scheme and the debt mountain of a totally run-down state such as, let's say, Italy? Is it that Professor Prodi is less charismatic than Damara Bertges?

Another example: if measured by the volatility of their price development – that is, the risk determined by the standard deviation from the average return – certain hedge funds would have to go into the "fixed-interest investments" risk category. It is however universally recognized in economics that there is no such thing as a free lunch, or, with regard to hedge funds, that the excess returns (should they actually materialize) will have to be paid for with some other risk, not measurable in terms of volatility. For instance, with the risk that, because trading in the instrument is only sporadic, it may not be possible to get out in time, when danger threatens. How in the world can such unsystematic, unquantifiable

risks be classified? What sort of risk categorization could possibly be suitable?

Lastly, back to Mandelbrot: serious consideration needs to be given to revising and, where necessary, adapting the structure of risk/return categories in the light of his insights. In doing so, it might be that we would have to leave the path laid down by MiFID and its implementation instructions – current "best practice", that is. Internal instructions are easily adjusted; legislators are a good deal more sluggish. Detail-obsessed regulations are a hindrance to progress.

6. Undersupply and flight

We can see where the supposed investor/consumer protection laid down by MiFID will lead. Given the intrinsic ambiguity of the rules, firstly, responsibilities between the investor and his financial services provider – his broker, adviser or asset manager – will become blurred. When once again the stock exchanges reel under the impact of a serious slump, it will be very tempting to shift a part of the risk onto the financial service provider. Thus, we shall see the development of court practice that will be just as asymmetrically friendly to the "poor" investor as rent tribunals are towards tenants. The ambiguity of the rules provides more than enough room for asymmetry. In practice, MiFID is providing investors with a put option, a sort of insurance against extreme losses.

In the cold light of day, the cards dealt to financial service providers appear even less attractive than those held by landlords appearing before rent tribunals. For financial service provision is always based on a state of probability, whereas the plaintiff can always base himself on the security of historically demonstrable events and supposedly determinable causalities. Having witnessed, in recent years, the arrogant self-confidence with which commissions of historians and auditors have laid into a generation that was confronted with uncertainties that today's desk-pilots could not even dream of, we may have some idea of how unequal the balance will be. The put option is thus potentially of great and lasting value.

But is something like this available for free? This is the big mistake made by legislators, not only in the area of investor protection. Inevitably, and here we come to the second impact, financial service providers will seek to protect themselves against simply having to take over the risk of extreme losses tel quel. For one thing, they will exploit every possible and impossible bureaucratic opportunity to demonstrate that they have complied with every duty of care at every stage. They will have the client sign the investment profile as often as possible, they will send a warning of potential side-effects with every stock exchange settlement, and they will, as far as permitted by MiFID, try to waive their liability through their general terms and conditions and other contractual agreements. The result will be the further over-administration of the relationship between investor and financial service provider, and the definitive elimination of what used to be known as "trust". And for another thing, they will, more than before, seek compensation for the risk allocated to them by the legislators. As the regulations to be complied with are extremely complex, and the systems and control mechanisms required for compliance (compliance officers, auditors, etc.) are extremely expensive, the natural result will be the exclusion from the market of small, marginal providers. A providers' cartel will become established, that will use higher fees to compensate itself for the risks involved, the structures needed to manage them, and a good deal more besides.

The third impact will be a flight, once again, to the unregulated sector. Exactly the same will happen as we have already seen elsewhere. For why have hedge funds enjoyed such a boom in recent years? Primarily because offshore, asset managers can operate entirely unconstrained by the constricting corset applied until very recently by the highly regulatory investment fund legislation. Why have private equity firms shot up like mushrooms in recent years? Primarily in order to get round the ever more difficult to comply with take-over regulations on the stock exchanges, and the ever more difficult to interpret corporate governance regulations. The danger of making actionable mistakes on the open capital market, that could cost vast sums of money, is simply too great.

Capital is even more fluid than water. If an unfortunate regulatory regime generates added costs by transferring risks, and this causes a structural underprovision on the supply side due to the cartelization that results, then what the market seeks – unadulterated risks and unadulterated returns – will rapidly become available elsewhere and in previously unenvisaged forms.

7. Responsibility is indivisible

In its investor protection provisions, MiFID is clearly based on the thinking behind the welfare state, whose task is believed to be to provide its citizens with as painless an existence as possible from the cradle to the grave. This thinking is ut-

terly at variance with principles that are regarded as axiomatic in economics. Economies must develop, flourish, but also decay and disappear. The pain of failure – even of the failure of the national airline – is no less essential than success. We cannot simply dismiss Schumpeter: creative destruction hurts, and it is not some abstract concept of "business" that has to carry the cost. Rather it is flesh-and-blood risk-takers, whose ultimate personal responsibility cannot simply be dismissed.

Further, economic growth and decline are not subject to simple and easily determinable causalities, but rather characterized by chance, by good or bad luck. Only exceptionally, and then usually only after laborious analysis, do we know why something happened one way and not another. But how ready we are to allocate blame, in the belief that we understand the causalities! This is the unhappy stuff of which are made the Swissair trials that will soon commence, and it is also the stuff that has resulted in the MiFID standards. Chance, good luck, bad luck: these are not concepts with which legislators and courts feel comfortable. And so, how often the flight to pseudo-causality! In this context, it is again worth reminding ourselves how ridiculous are the stock exchange reports focused on supposed causalities that we daily consume. Who on earth can tell that the Dow Jones Index has fallen just because of a rise in the price of oil, or that the Dax Index has closed up just because of positive reports at last from Daimler-Chrysler? We see causalities where they do not exist, and by doing so, we create the impression of control through deliberate action. It would be much more correct, and more honest, if the Reuters report were to say that "for unknown reasons the Dow Jones closed yesterday evening 0.5% higher than the previous day", or that "Luckily, the Dax Index went positive at the end of the day's trading".

The combination of the will to create a pain-free society with the idea that business is essentially based on comprehensible, and thus largely plannable causalities results in the unfortunate concept that it is only a matter of finding the right legislative solution, both for the prevention of pit bull incidents à la Kings Club or Behring, and also to defuse the consequences of speculative follow-ups as on the "Neue Markt". Sadly, this will not happen: the laws of economics work differently. Mandelbrot also points out that stock exchange bubbles are always only identifiable as such in retrospect.

Chance, good and bad luck, success or failure based on identified causalities, entrepreneurial performance: these are all part of the package that financial service providers have to offer. It is a matter of risk and return, and these two interact. Those who attempt to reduce someone's responsibility for the risk he bears simultaneously remove his return. Compulsory seat-belts (may) make sense on the road, though for drivers, the ultimate protection from themselves would of course be to forbid them to drive at all. The attempt to relieve risk-takers from part of their risk is, by contrast, self-contradictory. Legislation can, indeed must, protect both investors/consumers and financial service providers from everything under the sun: from fraud, from preferential treatment, from theft, from confiscation. One thing, though, it may not do: protect the risk-taker from himself, for taking risk is precisely his intention, and his economic function. However good the intentions may be that lie behind MiFID: good intentions are seldom good enough. Those who wish to create a successful internal market for financial services, which is the universally proclaimed aspiration of the European authorities, must show greater trust in competition and its immense, prosperity-inducing efficiency.

8. Afterword for Switzerland as a financial center

As a non-member of the EU, Switzerland is fundamentally free as to whether, and to what extent, it will adopt the MiFID legislation. A working group was recently established to study this issue, consisting of representatives from the Ministry of Finance, the Federal Banking Commission, the Swiss Bankers Association, the Swiss Exchange (SWX) and the Investment Funds Association. This constellation is a priori unpromising. Which of these bodies could seriously be interested in retaining or indeed simplifying the current legal situation? The Federal Institution for Dog Ownership (FIDO) already exists, in the form of the powerful Banking Commission, and so does the Dog-owners' Association. And in the background, the audit companies are naturally rubbing their hands in glee, as the controlling of client profiles and the allocation of products to the "appropriate" risk categories would represent a further extension of their already excessive mandates. The Swiss Exchange alone, if it has done its strategic homework properly, could be interested in a solution that would be, compared to the rest of Europe, more capital-market-friendly (and thus ultimately also more investor-friendly).

If Switzerland as financial center wishes to continue to offer an increasingly successful global platform, then it needs to pay attention to its potential competitive advantages and, among other

things, to try to compensate for the diminishing significance of banking secrecy. This could be done, for instance, by not following others down a regulatory road characterized by a socio-economic welfare mentality. There is surely no need for harmonization hereabouts. Au contraire, it would be highly attractive if investors could in future choose between the supposedly investor-friendly world of MiFID and a significantly more capital-market-friendly Swiss solution. Then we'd see where the global funds would be inclined to flow. For once, we need to put aside our otherwise almost insatiable need for harmony with Europe, and rather make global competitiveness our benchmark.

KH, 11.12.2006