

Magni Client Commentary

Talking Points on International Governance Research and Investing

February 2016

Country Ranking Trends

- Magni Country Scores are unchanged for the month of February.
- Usually Magni is watching more countries for potential upgrades than for potential downgrades. Currently, the reverse is true with recent events in countries such as Poland, China, and Malaysia having the potential for negative consequences.

Poland Unchanged...so far

- A new asset-based tax on banks has taken effect. The immediate impact has been a government investigation into whether banks have attempted to offset the impact of the new tax by raising fees. The government outlawed such actions when it passed the legislation.
- A controversial plan to convert the currency of mortgages from Swiss francs to Polish zloty has been put on hold after the central bank warned that the draft legislation could push 70 percent of the banking sector into losses.
- Also impacting the investment climate is the replacement of members of the central bank's Monetary Policy Council. The Senate has elected three candidates out of the eight to be replaced. The new members have pledged to maintain the central bank's independence, however, concerns remain that bank autonomy could be weakened based on the allegiance of new members to the ruling party. At this point, there is not enough information to downgrade Poland, however Magni will continue to watch developments.

Italy's Market Integrity Unchanged

- Magni recently completed a review of Italy's Market Integrity. One of the main methods for measuring Market Integrity is to understand a country's adherence to international standards in preventing money laundering. Italy already has a strong and effective system for preventing money laundering done through financial institutions. The country's primary money laundering risks stem principally from illegal tax evasion and similar activities; often associated with organized crime (e.g., corruption, drug trafficking, and loan sharking). Previously-identified opportunities to address these risks remain unresolved. Following the review, Italy's score remains unchanged.

Will China Retrench?

- The head of the China Securities Regulatory Commission (CSRC) has been replaced. He had attempted to improve transparency both in markets and at the securities commission. However, he was later faulted for failing to rein in the use of margin loans that greatly exacerbated the fall of Chinese markets. His replacement, Liu Shiyu, has called for stricter supervision. Given the top-down nature of current decision making in Beijing, his push for market reforms will likely face many of the same challenges as his predecessor's planned reforms.
- China continues to earn low scores for the regulation of securities and transparency of policy. If successfully implemented, Shiyu's reforms would increase these scores. Magni will be watching to see if the new head is successful with reforms or if the country starts sliding backward on the progress it has made over recent years.

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What Direction is Malaysia Headed?

- Malaysia's long serving and widely respected central bank governor has confirmed that she will step down when her term soon expires. She is credited with achieving greater central bank independence and with aggressive pursuit of the corruption allegations around the state development fund 1MDB. The central bank last year recommended filing criminal charges in the case, but the recently-appointed attorney general declined to pursue the charges citing a lack of evidence. Her successor has not been named and it is expected that whoever is nominated will be under pressure from the government to tone down its scrutiny of 1MDB, so it will be important to see if whoever assumes the role can maintain the independence and integrity of the central bank.
- Magni considers Malaysia as having the potential to become one of the highest scoring countries in the emerging markets. The openness in discussing the 1MDB scandal and the initial pursuit of the scandal by the government reconfirmed Magni's scoring. Recent developments call into question the ability of Malaysia to sustain recent improvements and may indicate a change in direction which results in Malaysia sliding backward. Magni will be watching to determine what direction Malaysia chooses.