

Strengthening the Capacity of Research Centers for Overseas Investments

한국경제매거진

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— **PARK Cheon Woong** Global expansion has emerged as a key agenda in the Korean financial service sector, due primarily to changes in demographic structure. After passing a peak in 2015, Korean working age population has been declining at a faster pace than those of other major economies such as Japan, China and the U.S. Korea's population is aging at an unprecedented rate globally, while average life expectancy is increasing. However, people generally do not have enough savings to sustain themselves as they live longer, which will inevitably lead to a greater demand for investments.

For Korean brokers and asset management companies, pursuing global businesses is not a matter of if, but when. The most efficient way to establish a business is following the flow of capital. As mentioned above, the demand for global investments is sharply increasing among retail and institutional investors such as the National Pension Fund. This customer demand provides a good incentive for market players to establish global businesses. The outflow of capital from Korea should not be considered as a threat to the Korean financial services market, but rather as an

opportunity for Korean brokers go global.

Building a global business model customized to Asia would be instrumental for Korean brokers or asset management companies. The global financial market is showing a keen interest in Asian emerging markets such as China and India, where Korean brokers have comparative advantages in terms of capital, capabilities and experience. Should China and India emerge as the center of the global business world, Korean brokers will be able to sharpen their competitive edge in the global market by building a solid presence in the Asian market alone.

Language has been an entry barrier for Korean financial service providers such as brokers to penetrate the overseas markets. However, the development of automated machine translation technologies such as PAPAGO is expected to remove this hurdle, allowing global asset management companies, investment banks and brokers to do more active business in Korea. Conversely, however, it also provides opportunities for Korean brokers and financial service providers to enhance their competitiveness as a global franchise.

Korea is in the early phase of the Fourth Industrial Revolution in all industries, let alone the financial industry. The financial and automotive industries, the two most protected sectors in Korea, might become among the first beneficiaries of innovation driven by big data and machine learning. The financial industry, which involves money transactions, has been subject to strict safety regulations. However, once the rise of new technologies such as blockchains or robo-advisors tear down high entry barriers, the financial sector will face a higher wave of innovation than other industries. Technologies such as big data, Artificial Intelligence(AI) and machine learning are widely used in the financial markets in Europe, the U.S. and Korea in areas such as investment banking, insurance and client services.

The key to the Fourth Industrial Revolution is co-operation, which is not limited to people-people but also people-machine relations. Korean brokers need to think outside the norm that they have to establish their own infrastructure and networks to drive the development of global businesses. Notably, small and medium-sized brokers with limited financial resources should work together in overseas markets which they cannot penetrate on their own. Building infrastructure overseas is a costly venture, but taking advantage of the established infrastructure will enable significant cost savings. Small to medium-sized brokers which face similar challenges abroad should network with each other by exchanging information in their areas of expertise and expanding cooperation.

— **KIM Yunsuk** The collapse of Lehman Brothers triggered a near meltdown in the global financial market in 2008-2009. The Korean financial market was not spared from the fallout, as seen in new terminology referring to loss-making overseas funds. Prior to the global financial crisis, overseas funds attracted many investors with the promise of high returns. However, the crash of the global financial market wiped out 50 to 80 percent of the value of investments.

The tax burden is one of the key considerations

for high net-worth individuals in deciding upon overseas investments. Under the current Korean taxation system, gains on overseas investments are subject to a capital gains tax or dividend income tax. For example, when an investor has reaped a ten percent gain on overseas investments, the after-tax real rate of return comes in at 5.6 percent. This is not attractive enough for investors to take the risk of making overseas investments. Asset allocation concentrated on a single market is also undesirable for retail investors. The market capitalization of the Korean equity market accounts for two percent of the global financial market, and thus Korean investors are missing out on the rest of the global financial market by investing only on the Korean market. An increase in overseas investments is inevitable; however, policy frameworks regarding such things as taxation should be in place to promote overseas investments. The biggest difference in the overseas investment boom of the past and the present is that Private Banks(PBs) have moved up the learning curve. Customers are showing great interest in financial products with medium-risk, medium-return. As overseas investment products are often inscrutable, inexperienced PBs may have difficulties in seeing through structural complexity. In this regard, training programs are being offered to address these problems.

— **CHO Yongjun** I believe Mr. Park's speech has inspired Korean research centers to turn challenges into opportunities. Korean brokers have already taken the necessary steps, enhancing global asset allocation and recruiting talent. It is reckless to make investments without accurate information or an analysis of investment targets. Investing without research is like gambling. Past examples show that overseas investments, not backed by research, led to huge losses. As was the case with Brazilian bonds, investors had rushed to bet on high-yield overseas investments without analyzing the markets or products and ended up with heavy losses. There is no argument that it is time for research centers to enhance their capability to meet growing interest in overseas

investments. Notably, research centers must examine in detail how they might address the growing importance of globalization and rapid market changes, such as the introduction of new technologies in the era of the Fourth Industrial Revolution.

— **KIM Jaehong** Despite strong interest in the analysis of global equity markets, the time difference and limited information available to Korean companies make it difficult to have a flexible response. It takes time for analysts to develop experience and provide reliable analyses that helps investors take a selective approach with a long-term perspective. As for Shinyoung Securities, the research center is seeking to enhance its talent development and global networking by forging partnerships with overseas asset management companies and sending employees abroad. This enables us to analyze the requirements of overseas markets. However, as overseas corporate analyses incur significant costs such as company visits, Investor Relations(IR) and networking, small to medium-sized companies should find ways to improve the quality of their analyses in a more cost efficient way. Notably, PBs have a critical role to play as overseas investments have a high-risk, high-return profile.

— **LEE Changmok** The Fourth Industrial Revolution is taking place at a breathtaking pace. It takes only 30 minutes for a single AI to process what it would take three hours for 30 analysts. This presents a serious threat, but also an opportunity if research centers work with these machines. One may mistakenly think that Korean investors pursue a medium-risk, medium-return profile. In fact, when investor seminars on overseas equities were held, it was high-risk, high-return products that attracted the largest crowd. Strictly speaking, there are no such products with a medium-risk, medium return profile. The term is intended to reassure investors who are seeking high-yielding, safe investments. The aging of the population is leading to a growing need for higher investment returns. Given that medium-risk, medium-return products involve high risk, this calls for a prudent approach.

Keywords

Graying population, internationalization of the Korean the financial industry, Asia-specific business models, quality and speed of good information, global businesses, the Fourth Industrial Revolution



Policy Implications

- Given Korea's demographic structure, it is inevitable that an increasing number of investors will look beyond Korea to global financial markets. Korean brokers should go global to match the need for overseas investments. Good information is the prerequisite for investments. Research centers have a critical role to play as investments should be backed by accurate analysis.
- The Fourth Industrial Revolution is one of the engines that drive overseas investments. Information analytics has seen rapid technological developments such as deep learning and machine learning, while accessibility to overseas investments has increased via MTS. As such, embracing changes accompanied by the Fourth Industrial Revolution and taking preemptive actions are the best way to enhance competitiveness.
- The key to the Fourth Industrial Revolution is cooperation. It is necessary for small to medium-sized financial service providers to take advantage of the established infrastructure in a cooperative way, rather than building infrastructure overseas on their own.
- Even though global networks provide instant access to information, it takes time to relay it to consumers or investors, which makes the information less relevant. It is necessary to devise ways to transmit good information to investors in a timely manner to promote overseas investments and highlight the positive aspects of overseas investments. The tax burden is one of the key considerations for high net-worth individuals in deciding upon overseas investments. The government should offer more attractive tax benefits to promote overseas investments.

Chapter THREE

SUSTAINABILITY