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The President of the Republic
Palais de l'Élysée
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1 June 2004

Dear Mr President,

It is my distinct honour to submit this annual report to you for the first time in my capacity as Chairman of the Autorité des marchés financiers (AMF), created by the Financial Security Act of 1 August 2003. The report deals chiefly with the activities of the Commission des Opérations de Bourse (COB) and the Conseil des Marchés Financiers (CMF) for the period until 24 November 2003, when the AMF was inaugurated.

After a three-year slump triggered by the bursting of the "new economy" bubble and marked by international crises and a spate of scandals affecting large US and European companies, the markets regained some of their composure in 2003 and resumed a growth trend. The CAC 40 index of leading stocks, which started the year at 3063.91 points, down from the September 2000 record of 6922.33, closed at 3557.9 on 31 December. Volatility, an inherent feature of all markets, eased back from the extremes that had unsettled many market participants, especially in Europe, and returned to normal or relatively low levels.

However, uncertainties about the magnitude and duration of the economic recovery and the future pattern of exchange rates, combined with an entrenched and highly tense international situation, left markets in an ambiguous mood, most notably in Europe. Euronext Paris saw a decline both in trading volumes and in flotations, despite a wave of delistings that reduced the number of companies quoted on French regulated markets to 816 at 31 December 2003, compared with 873 one year earlier. Although equity issuance surged, it was concentrated on a handful of deals involving complex securities evidencing debt convertible to equity. France's derivatives markets remained stable.

Nevertheless, the COB and the CMF had a highly eventful year. Two major transactions took place on their watch, namely the Crédit Agricole - Crédit Lyonnais merger and Alcan's tender offer for Pechiney. In addition, the two regulators closely scrutinised a number of corporate restructurings, paying attention to the protection of minority shareholders and the fairness of the financial arrangements.

Furthermore, the crisis of confidence sparked by accounting scandals prompted heightened vigilance in the supervision of financial disclosures. The injunction procedure, set in motion when the president of the Paris regional court refers a case to the regulators, was used systematically to reprimand companies that had taken seriously liberties with their disclosure obligations.

The asset management industry – and in particular the collective investment sector, where France is a European leader – progressed further on the road to modernisation. It was driven by the implementation of new European and domestic rules and by the growth of alternative investment management. The regulator facilitated the marketing of these innovative and complex products, while laying down exacting requirements as regards asset managers' skills and informational transparency. Substantial progress was also made in the field of remuneration arrangements for asset management firms, with a view to clarifying procedures and forestalling possible conflicts of interest.

Market infrastructures have been revolutionised in recent years by globalisation, deregulation and steady technological progress. The CMF and the COB, together with the prudential regulator and their counterparts in the countries concerned, dealt with the regulatory aspects of the expansion of Euronext and the successful merger of Clearnet and London Clearing House.

More generally, the COB and the CMF were actively involved in regulatory harmonisation projects conducted at European level by the Committee of European Securities Regulators (CESR) – now headquartered in Paris following confirmation by the European Council – and at international level by the International Organisation of Securities Commissions (IOSCO) and the Financial Stability Forum.

The disciplinary activity of the two regulators and the Conseil de Discipline de la Gestion Financière (CDGF), focusing on investor protection and market integrity, proceeded at a sustained pace in 2003 in every area: supervision, inspections and investigations, and sanctions (more than 60 decisions were taken, some carrying substantial penalties of up to €1 million).

In sum, it is important to stress the remarkably steadfast way in which both the COB and the CMF continued to operate during the year. Not even the prospect of a radical institutional overhaul was able to dent their commitment.

The creation of the AMF is a landmark event for the entire French financial community. It was provided for in the Financial Security Act which, combined with several recent pieces of legislation, has raised the Paris markets to a very high level of regulatory quality.

The institutional hand-over was smooth and the continuity of operations was unaffected. The new departmental organisation became effective less than three months after the inauguration of the AMF by Francis Mer. The teams were merged according to a blueprint that distinguishes between the day-to-day task of regulation, conducted with issuers and intermediaries; regulatory policy, based on research and international cooperation; supervision and investigation; and the cross-cutting functions of technical and logistical support. The new board rapidly found its bearings and coalesced into a united entity. I wish to emphasise the advantages of its multi-disciplinary structure and its appointment methods, which endow it with exceptional powers and globally unrivalled independence. The Disciplinary Commission has been designed along the same principles, and its inception has put paid to arguments over the legitimacy of the system in place at the COB. It set to work immediately and issued several decisions. Five Consultative Commissions, each composed of industry experts and led by two AMF Board members, will help to improve forward thinking and lay the groundwork for regulatory developments, without impinging on the public consultations organised before new measures are adopted and while they are being implemented. The Consultative Commissions will invite industry practitioners and academics to take part in their activities.

These results could not have been achieved without the remarkable preparatory work done by the senior officers of the COB and the CMF throughout 2003. Without ever seeking to influence the choices the new authority would have to make, they were able to analyse and elucidate each option with relevance and foresight, and I would like once again to pay public tribute to their efforts.

Many tough challenges lie ahead for the new Authority. First, at the domestic level, it must contribute to the credibility of Paris as a financial centre, amid intensifying competition and heightened investor wariness of market shortcomings.

The first project will be to prepare a general rulebook. In addition to codifying the regulations of the COB and the CMF, the AMF will add new provisions arising, in particular, from the transposition of European directives. Moreover, this transposition process will keep the AMF busy in the coming months as it provides support for government departments. This is a major undertaking, particularly since the new directive on investment services will radically alter the way the market operator functions, for two reasons: the opportunities now available to "multilateral trading facilities" and the internalisation of stock market orders by major banking networks.

The AMF will also exercise the new or enhanced powers it has received under the Financial Security Act in areas such as financial promotion ("cold calling"), financial investment advice, and the regulation of investment research and credit ratings.

The process of restoring confidence in financial markets is still on shaky ground. The AMF, like its counterparts in major financial markets, must further improve transparency and integrity, while making sure that the more burdensome procedures do not impact negatively on market participants, who are experiencing intense competition. Its decisions should be guided by the need for efficiency and simplification, whether in financial disclosures, financial instrument transactions, asset management, distribution of financial products or infrastructure operating rules.

Here I must mention the effects of the accounting reforms ushered in by the European Union's decision to adopt International Financial Reporting Standards (IFRS) in 2005. This, too, is a revolutionary move that will affect the entire disclosure process. Responsibility for overseeing the enforcement of IFRS will lie firstly with the audit profession. Accordingly, the reform of the supervisory mechanism for auditors' standards and conduct via the formation of a new authority – the Haut Conseil du Commissariat aux Comptes (H3C) – is vitally important. The success of this reform will depend, inter alia, on the quantity and quality of the resources allotted to H3C to address a wide range of general and individual issues and to reinforce the international credibility of French statutory auditors.

Naturally, the AMF will have to fulfil its disciplinary mission both wisely and firmly. Already, in the space of some four months, it has ordered nearly 40 inspections and investigations. Its Disciplinary Commission has taken five sanction decisions, and nearly 40 sanction proceedings are in progress.

Financial market regulation now takes place in a totally international setting. The AMF will therefore have to play its part in the community of regulatory authorities, which are largely responsible for designing and enforcing rules. In particular, it will be closely involved in the work of CESR, now the official regulatory network for Europe's single financial market.

Among the issues of future importance are a huge standardisation project ("Level 3", to use the terminology of the Lamfalussy Process), closer operational cooperation in the field of supervision and inspection, and support for structural reforms made by exchange operators and "post-trade" infrastructures (i.e. those responsible for clearing, settlement and custody).

The AMF must also play an active role as part of IOSCO and the Financial Stability Forum. These bodies are in the process of promulgating worldwide standards. With increasing determination, they are organising a collective effort to implement those standards and to react to the misdoings of non-cooperative jurisdictions, which jeopardise the stability and integrity of world financial markets.

The AMF's mission is considerable. It consists in offsetting informational asymmetries, redressing the balance between the weak and the strong, preventing conflicts of interest, bolstering market mechanisms, and identifying and punishing those responsible for market abuse.

I welcome the legislature's decision to preserve the distinction between "microeconomic" regulation, on the one hand, and the remit of the prudential regulators responsible for banking and insurance, on the other. Like its predecessors, the AMF will maintain close links with these bodies.

To carry out these tasks, the AMF can rely on a staff of some 330 people, whose excellence and dedication deserves recognition here. In the coming months, the Authority's chief executive and his team will finalise their efforts to integrate and harmonise personnel regulations and working conditions. Once the policy and discussion seminars organised by the department and the Board are complete, it will also be necessary to gradually build up the resources of the AMF, whose workload has increased sharply compared with its two predecessor organisations.

In conclusion, I would stress that the purpose of regulation is to foster the development and prosperity of the financial community, of which it is an integral part. In this respect, the challenges facing France's finance industry are considerable and require concerted action by all participants. This means enabling more top-notch companies to come to market, pursuing efforts to channel domestic savings into equities, and building a robust and diversified intermediation process. These challenges are strategically important for our economy. Clearly, having a powerful finance industry guarantees independence and generates high added value. The remarkable progress that France has made since its Big Bang in the 1980s must not be derailed by doubts arising from the crisis in the "Net economy". Nor must it result in a slackening of efforts to adapt French society to a market economy, with which it is less familiar than some of its most advanced competitors.

Sincerely,

Michel Prada