BAHAMAS FINANCIAL SERVICES BOARD

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THE BAHAMAS: A COMPLETE AND COMPELLING CHOICE

A *WealthBriefing* mini-series on The Bahamas financial services industry

EDITION 2

'Fund Administration and The Impact of the Pandemic' and *'Investments - the Search for a Safe Harbour'*

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INTRODUCTION

The Bahamas: from Challenge to Transformation

When it struck an ill-prepared world in 2020, the coronavirus did not stop The Bahamas' financial sector from innovating. Despite the fact that people could not travel and had to work remotely, the jurisdiction kept on diversifying its products and meeting the needs of its clients. The investing experience, far from declining, actually improved. During this time, it became clear that good corporate culture was now paramount.

In today's mini-report we see how professionals at financial firms have activated their business continuity plans successfully and adapted well to the new world of virtual meetings, thereby ensuring that their clients keep on receiving their bespoke services. We see how a new swarm of individual investors has arisen because of lockdown and how skittish investors all over the world are turning to the Bahamas for financial products and services to help them escape the inflationary trap that is closing around them. In many cases they are also, of course, drawn to live and work in The Bahamas because of the enviable quality of life on offer.

It is evident that crypto-funds as an asset class represent the future. With this in mind, the Government of The Bahamas has recently issued a White Paper on the future of digital assets.

Some of the largest players in the crypto-space have made The Bahamas their home - and not simply because Government policy grapples with the most important business issues of the day or because the regulatory regime is very stable. Service providers in The Bahamas are improving their game all the time, especially in the fiduciary area and in investment funds. Crypto-related ETFs are among the asset classes which investors exploit with the help of Bahamian brokers. The jurisdiction's 'SMART' and 'Professional' fund classes are helpful also in these difficult times.

One popular investment vehicle model this year is the exchange-traded fund or ETF, a fund of which at least one unit or share class is traded throughout the day on at least one trading venue. This type of pooled investment security resembles a mutual fund in the way that it works. It usually shadows a particular index, sector, commodity, or other asset, but unlike a mutual fund its investors can buy or sell it on a stock exchange in the same way that they can with normal stocks. The war between Russia and the Ukraine has sent commodity prices spiralling, so ETFs in commodities are very successful.

This communiqué is part of a larger report on financial services in The Bahamas which is coming out in stages during the course of the year.

ADVERTISING SUPPLEMENT

FUND ADMINISTRATION AND THE IMPACT OF THE PANDEMIC

*** By Antoine Bastian, the CEO of Genesis Fund Services Ltd**

The Coronavirus has caused immense disruption to business throughout the financial services industry, both in The Bahamas and abroad. Some fund administrators, however, have taken it in their stride. This is the story of one business that benefited from early updates to its practices in ways that it could not envisage before the virus struck.

During the past two years of this COVID pandemic, all business operations have had to deal with change on a large scale. Even the world of fund administration has changed and, at Genesis Fund Services, these changes have affected not only what we do but also the way we do it.

Before the pandemic, we all tended to view change as inevitable. However, the general pace of change in our industry was moderate until COVID arrived. That pace then accelerated enormously and catapulted us into an uncertain future. Change occurred more quickly than we might have liked or expected, but undoubtedly it has been for the better.

We have adapted to the 'new normal' of paperless processing

We now seem to be emerging from the worst of the pandemic and entering a new era. This is a 'new normal' for clients, for employees, for fund investors, for fund managers and for the jurisdiction. Technology, talent management and digitisation lie at the heart of this new normality.

THE PAPERLESS OFFICE

At Genesis, we took the fortuitous decision in early 2018 to create a paperless office. We did not have a crystal ball to help us foresee the events of 2020/21, which included the sudden and unfortunate COVID-19 lock-down mandate. We did, however, see that digital technology was evolving and pushing our processes – and the industry as a whole – towards more digitisation. We had to satisfy the demands of our clients and fund investors (especially institutional investors) for more advanced technological reporting, communication and management of their business data.

Fund administration's age-old reliance on manual processes and high volumes of paper was near death. Fortunately, before the pandemic struck, we reduced our paper processes and all remaining manual processes dramatically. COVID simply hastened and obliterated any vestiges of paper processes that were left because manual applications simply could not happen when everybody was working from home. The fund administration industry, and we here at Genesis, therefore adapted to the 'new normal' of paperless processing. We did this with subscriptions, redemptions, accounting and, most importantly, the review and collection of 'due diligence' data.

Without the advent of COVID, we would simply not have collected, vetted and processed 'due diligence' information from home as soon as we did. Before COVID, Genesis would never have permitted its employees, even its most capable and trusted employees, to have taken customers' passports, bank details and other information into their homes because of the need for privacy and accountability.

A STEEP LEARNING CURVE

However, to continue operations effectively and to satisfy regulatory responsibility while keeping up best practices, we had to work quickly to improve and monitor our cyber-security data-protection – fund administration's newest cost centre. We had never anticipated a time when 100% of the workforce had to work at home and the firm therefore had to take on the unbudgeted costs of buying everyone a new laptop, a second screen and an updated wifi device to speed up their work.

The advent of intense training in cyber-security and updates to controls that safeguard clients' information have led to major improvements and benefits at financial service providers. Now, employees who are not in the compliance department have to discharge responsibilities for 'due diligence' when they are at home and must be conscious of the need to safeguard clients' information and mitigate the risks involved in that work. This they now do very well.

The use of two- and three-factor authentication has become the norm. Firms are far more aware of their duty to safeguard clients' data and have overwhelmingly improved the ways in which they mitigate risks that pertain to individuals during the pandemic. Videos, memos and virtual meetings regarding privacy and risk have increased tenfold...or at least, it feels like tenfold!

At Genesis, we have observed that COVID has made all staff more conscious of the risks that cyber-maladies pose. It has also made them realise that it is their regulatory – and laborious – duty to safeguard clients' data.

BALANCING BETWEEN WORK AND LIFE

Many fund-administration staff have worked arduously and conscientiously at home. Buckling under the stress of working all hours in a domestic setting, logging on in the middle of the night and answering emails at ungodly hours, they want to take some time off and not be overwhelmed by their new virtual world. In short, they need help and the senior management team has to make it available to them. Because of this, the issue of everyone's work/life balance has become a key concern at every meeting with the senior management team.

During the past two years of dreadful lockdowns, isolation and the need to work from home have changed the way in which so many of our colleagues view the work experience. Some of them have seen their parents and other family members succumb to the vicious disease or suffer grave illness from it. Many have changed careers and residency or moved to different firms in the same sector. Human capital has moved around in an unpredictable and somewhat disruptive way.

The retention of talent is also a top agenda item for the leaders of fund administrators. I remember, years ago, working outrageously long hours in fund administration – Sundays included. My employers expected this of me, but it is impossible for today's firms to expect the same; people will not come in on Sundays. Firms must now be more flexible and competitive. They must hold onto well-trained, experienced and talented people. They must, moreover, be able to attract and recruit talented professionals.

Despite having experienced some staff attrition, fund administrators have had many opportunities recently to hire eager, talented professionals from all over the globe and from career paths outside the world of financial services. When considering human resources, fund administrators no longer want to employ mechanically-minded people to perform robotic functions. They would rather invest in versatile, problem-solving individuals who can work with various aspects of the business.

The general pace of change in our industry was moderate until COVID arrived

Although the cost of recruiting, retraining and developing professionals has increased, firms have now fast-tracked these elements of the work experience and are using creative means to do so. When COVID disappears, the result at every firm will be a well-trained staff, a greater capacity for work and a better experience for clients.

During this period of COVID, fund administrators have been working hard to improve their technology. A few years ago, any one of them would have been served adequately by one system that handled accounting and its relationships with investors, one for corporate and compliance matters and perhaps another for other aspects of the business. However, although fees have gone down for services over the past ten years, the cost of providing straight-through processing (STP) safely and efficiently has sky-rocketed along with the cost of both hardware and software.

Technology has become as essential as talented human capital

Investment managers and investors in funds, moreover, have been insisting that their fund administrators ought to improve their reporting, data delivery and cyber-security continuously. Smaller fund administrators have found the piecemeal nature of their technological solutions burdensome. COVID has hastened their need for software connectivity, the better to improve results for clients. Technology is not only crucial for the provision of excellent service; it has become as essential as talented human capital. The need for fund administrators to provide collaborative business data through the use of technology has become standard. Their further collaboration with investment managers and fund administrators through the use of technology – with regards to both the safeguarding of clients' data and the provision of seamless services – is another part of the 'new normal.'

Investment managers have had to face similar burdensome movements in human resources and changes in technology and regulatory rules. As such, they have had to reassess their service providers to ensure that their talent, the quality of their services and the technology that they require have improved beyond pre-pandemic norms.

Over the decade prior to the pandemic, 'due diligence' questionnaires for fund administrators were standard. The pandemic, however, caused a noticeable increase in questions to do with technology and 'due diligence' which covered, among other things, data protection, redundancy and cyber-security. Investment managers and institutional investors have also intentionally asked more questions about corporate governance, diversity, equity and inclusion. It is now normal for fund administrators to provide dynamic governance, diversity and technological platforms.

CORPORATE CULTURE

Although technology and human capital are of prime concern for a good fund services organisation, it must have a good corporate culture that can knit the two together. An intentional drive to formulate and implement plans to ensure that we have a cohesive team has been crucial for us during COVID. The demand for talks and seminars on communication, mental health and mindfulness, or other subjects to do with the development of the whole person, has outweighed the demand for more accounting or compliance training by far. People want to work with people whom they like or admire, or with people who can help their careers.

The creation of a new 'conscientious culture' during and after COVID has become as important as the development of efficient accounting or 'due diligence' processes. At the same time, the maintenance and progression of a vibrant corporate culture has been one of the most difficult aspects of business in this pandemic. Collaboration among leaders and coaching in the workplace will continue to be an important aspect of the future work environment.

All highly-functioning organisations have, or should have, continual plans to improve their corporate culture.

The Government has recently issued a White Paper on the future of digital assets

After the pandemic, The Bahamas will continue to be an important jurisdiction for investment funds. There is a high buzz about crypto-investing in our jurisdiction and the Government has recently issued a White Paper on the future of digital assets; it is evident that crypto-funds as an asset class represent the future. Globally, investment by institutional investors in the crypto-fund arena is relatively small but many fund managers are starting to consider some investment there, either directly in various crypto-currencies or through such other means as crypto-derivatives, crypto-firms or crypto-ETFs, i.e. exchange-traded funds.

The Bahamas' regulated 'SMART' and 'Professional' fund classes are primed for the exploration of these new and exciting, but very real, structures. Investment managers or institutions that are trying to figure it out can use the SMART fund model to gain crypto-exposure. Bahamian Professional Funds have no limitation on types of assets and can also be used as vehicles for crypto-asset exposure.

Whether in crypto-funds, private equity funds or hedge funds, the 'new normal' has positioned Genesis to be even more capable of providing fund-administration services of high quality in the world after COVID than it was before. Our base in the Bahamas has helped us retain and recruit highly talented staff. It has also been crucial for the creation of our fast and reliable technological platform.

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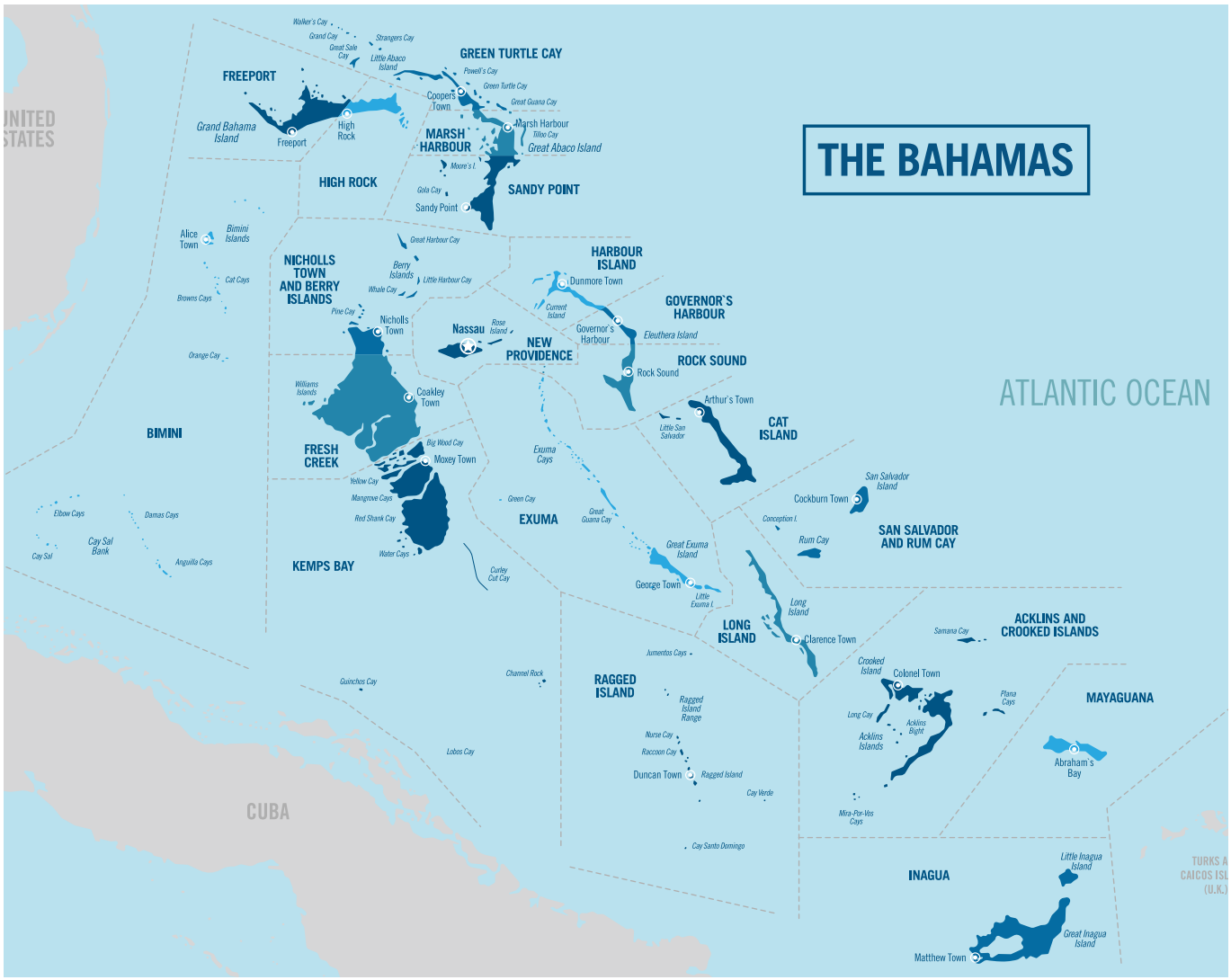

ADVERTISING SUPPLEMENT

INVESTMENTS – THE SEARCH FOR A SAFE HARBOUR

*by Chris Illing, the Business Developer at ActivTrades

The Russian president has brought decades of peace in Europe to an end. His war in Ukraine, combined with the Coronavirus pandemic which began today's cycle of high inflation in 2020, is causing a great deal of uncertainty in the financial markets. Investors in commodities, however, have done well.

2022 has been a challenging year for the international investor. During the height of the pandemic, the volume of mobile trading by retail traders grew enormously because people had plenty of surplus disposable income, more spare time in which to trade from the comfort of their homes and increasingly reliable internet connectivity.

Nowadays, anyone can easily trade in securities on the Internet. Online brokers make this possible, offering investors access to global trading venues through software and FinTech.

TRAPS FOR THE UNWARY

If someone wants to sit at home and invest on his computer or smartphone, he should compare the offers of the online brokers with each other. Although they offer their services at considerably lower prices than direct banks, i.e. banks with no branch networks, they are not completely free of charge. Sometimes the fee-free depots and trades are offset by return-reducing third-party flat rates, negative interest, exchange fees and trading commissions.

Stocks have struggled and bonds have done worse, but commodities are an isolated bright spot

In addition to the fees, the investor should pay attention to the asset classes in which he wants to invest when choosing his online broker. Not every service offers trading in crypto-currencies or contracts-for-difference, for example. It is also worth comparing the services with each other, because not every online broker has a multi-language-speaking customer service or can be reached by phone. The user interface should be clearly designed and easy to use. An online broker that offers a free demo-account for testing is recommended.

It is important for every investor in the stock market to have a balanced portfolio. Anyone who invests in stock listed all over the world and who relies on the large, well-known global stock indices is not going to feel the effects of volatility in the markets as badly as, for example, an investor who depends on Russian companies. One should not look at the next few weeks here, but at the next few years.

THE ASSET CLASS *DU JOUR*?

The inflation rate in the USA was recently 8.5% for the 12 months ending in March 2022. Crypto-assets are the most high-profile instruments that investors are using to protect their portfolios against inflation. They are, however, only one type of asset. Investors can look to real assets as well. Gold, for example, should continue to do well during the rest of 2022. The price of this precious metal rises when inflation is high but may dip if interest rates rise. The real interest rates, i.e. the interest rates after inflation, are therefore decisive and these are likely to remain negative globally. Even if the US Federal Reserve were to raise interest rates to 2% by the end of next year, which would be extremely high, real interest rates would still be well into the red given inflation of 4%. This should elevate the gold price.

In a year in which stocks have struggled and bonds have done worse, commodities are an isolated bright spot. It is important to note that investors in commodities have been able to gain this year from increases in the prices of raw materials. Investors obviously know that energy prices have surged this year, with the war between Russia and Ukraine interrupting the flow of oil and gas. The conflict has had its repercussions in many other commodity markets as well, since Russia and Ukraine export a whole host of commodities including wheat, corn nickel and palladium.

Along with exchange-traded products that target single commodities, several multi-commodity exchange-traded funds found themselves to be very popular.

ETF INVESTMENTS

Exchange-traded funds are popular with our investors as trading instruments. An ETF is a type of pooled investment security that

operates much like a mutual fund. The fund tracks a particular index, sector, commodity or other asset but, unlike a mutual fund, an ETF can be purchased or sold on our trading platforms in the same way that a regular stock can.

QQQQ trades on the Nasdaq exchange and is one of the more popular ETFs. This security offers broad exposure to the tech sector by tracking the Nasdaq 100 Index, which consists of the 100 largest and most actively-traded non-financial stocks on the Nasdaq.

An ETF is a type of pooled investment security that operates much like a mutual fund

Alternatively, the Direxion Daily S&P Biotech Bear (LABD) 3X Shares seek daily investment results, before fees and expenses of 300% of the performance of the S&P Biotechnology Select Industry Index.

The first US Bitcoin-linked ETF is the ProShares Bitcoin Strategy ETF (BITO.US), which offers investors a familiar way to gain returns but with the liquidity and transparency of an ETF. An investor can expose his portfolio to bitcoin easily with this. When BITO was launched back in October last year, it became the fastest ETF to reach $1 billion dollars in assets under management.

THE TRIALS AND TRIBULATIONS OF INVESTING

If a retail investor trades in an ETF, especially a crypto-related one, he will gain some advantages if he does so with the help of a regulated broker. In addition to various problems that beset the spot market itself, the unassisted investor faces some complex transactions if he wants to invest in bitcoin directly, even through an exchange. If he looks at the disclosures made by one of the exchanges that offers bitcoin, he might see a text in the small print that says "you could lose all your money in a fork." He must then spend some time on the Internet to find out what a fork is on the blockchain. Many people are comfortable with this process, but there are certainly some who are not amenable to the challenges of dealing in a new asset like that in its raw form.

Then, of course, there are the issues that surround custody and wallets. Once the investor is in an exchange, he has only just embarked on some tough decision-making. He must then determine whether the exchange ought to hold his wallet, whether he ought to hold his own wallet, whether he ought to hold his wallet and keep his code on a memory stick, or on a piece of paper in a vault, and so on. Many small investors are looking for simpler ways to take part in the crypto-market and brokers offer them one way of doing this.

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