EACB position paper on the technical advice of the Committee of European Securities Regulators (CESR) to the European Commission on non-equity markets transparency in the context of the review of the Markets in Financial Instruments Directive (MiFID)

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The **European Association of Co-operative Banks** (EACB) is the voice of the co-operative banks in Europe. It represents, promotes and defends the common interests of its 28 member institutions and of co-operative banks in general. Co-operative banks form decentralised networks which are subject to banking as well as co-operative legislation. Democracy, transparency and proximity are the three key characteristics of the co-operative banks' business model. With 4.200 locally operating banks and 63.000 outlets co-operative banks are widely represented throughout the enlarged European Union, playing a major role in the financial and economic system. They have a long tradition in serving 160 million customers, mainly consumers, retailers and communities. The co-operative banks in Europe represent 50 million members and 750.000 employees and have a total average market share of about 20%.

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Introduction

The European Association of Co-operative Banks (EACB) would like to thank the Committee of European Securities Regulators (CESR) for the opportunity to share its views on the important consultation on non-equity markets in the context of the review of the Markets in Financial Instruments Directive (MiFID).

In the following outlines EACB would like to point out responses to selected questions raised by CESR in its consultation document.

Question 1: On the basis of your experience, could you please describe the sources of pre- and post-trade information that you use in your regular activity for each of the instruments within the scope of this consultation paper:
a) corporate bonds
b) structured finance products (ABS and CDOs),
c) CDS,
d) interest rate derivatives,
e) equity derivatives,
f) foreign exchange derivatives,
e) commodity derivatives?

There are many sources used by our member institutions, e.g. exchanges, trading systems, brokers and information providers (e.g. Bloomberg and Reuters).

Question 2: Are there other particular instruments that should be considered as 'corporate bonds' for the purpose of future transparency requirements under MiFID?

No.

Question 3: In your view, would it be more appropriate, in certain circumstances, to consider certain covered bonds as structured finance products rather than corporate bonds for transparency purposes? Please explain your rationale.

From our perspective it would not be appropriate.

Question 4: On the basis of your experience, have you perceived a lack of pre-trade transparency either in terms of having access to pre-trade information on corporate bonds or in terms of the content of pre-trade transparency information available?

There are certainly substantial differences in pre-trade transparency between retail and wholesale investors. In the wholesale area transparency is already in place. For retail investors, however, the complex market information systems are too expensive. From our perspective the internet is the only way to procure the information in relation to retail investors. For this reason the obligation to provide pre- and post-trade information should be limited to regulated markets and multilateral trading facilities, because they already have established respective links to the relevant internet sites. It is not realistic to assume that every vendor is actually able to establish links to all relevant sites. From our perspective such a limitation of pre-trade transparency to regulated markets and multilateral trading facilities would also lead to more liquidity on these platforms for retail investors.

Question 5: In your view, do all potential market participants have access to pre-trade transparency information on corporate bonds on equal grounds (for example, retail investors)? Please provide supporting evidence.
Question 6: Is pre-trade transparency efficiently disseminated to market participants? Should pre-trade information be available on a consolidated basis?
Question 7: What are potential benefits and drawbacks of a pre-trade transparency regime for: a) the wholesale market; and b) the retail market? If you consider that there are drawbacks, please provide suggestions on how these might be mitigated.
Question 8: What key components should a pre-trade transparency framework for corporate bonds have? What pre-trade information should be disclosed?

We see one major problem with respect to any kind of pre-market transparency in the corporate bond market: it is very difficult to find firm quotes anywhere. The main drivers in this market are over the counter transactions (e.g. by phone and by Bloomberg). In this case, the quotes on Bloomberg or other systems are only indications and there are no market makers around. Especially in volatile markets, prices that are actually tradable are often far away from screen prices. Therefore, we consider the pre-trade transparency for corporate bonds misleading for retail investors.

Eventually, from our perspective exchange indications should provide the necessary pre-trade transparency for retail investors. Institutional investors and in general the wholesale market already have a sufficient pre-trade transparency by quotes via Bloomberg, Reuters and mail. They are also able to evaluate the quality and probability of their execution.

Question 9: Do you think that notional value would be a meaningful piece of information to be made accessible to market participants? Is there any other information that would be relevant to the market?

No, from our perspective there is no other information that would be relevant to the market.

Question 10: Do you agree with the initial proposal for the calibration of post-trade transparency for corporate bonds? If not, please provide a rationale and an alternative proposal (including supporting analysis).

Most over the counter trades are so called voice tickets. They are not traded through automatic trading systems. Therefore a close to real time publishing is not possible. In this respect we would like to point out once again our argument that only regulated markets and multilateral trading facilities should be obliged to post-trade transparency. The same applies to questions on asset backed securities and collateralized debt obligations.

Question 11: Should other criteria be considered for establishing appropriate post-trade transparency thresholds?

We strongly disagree with the proposal. Post-trade transparency in this form would significantly damage the markets rather than improving things. Post-trade transparency with information on price, volume and the exact time of trade will lead to less liquid markets. Many especially smaller market participants will lose the interest of providing the market and clients with quotes as the chance to recover the position with a margin that pays for the taken risk will be reduced. The situation of illiquid bonds will not be changed. Smaller banks and brokers are likely to step out of this field of business and this will lead to a concentration on some large players that will completely control these markets.

For the markets CESR is focusing on in this consultation, the more detailed the published information are the more illiquid these markets will get. From our perspective this will have a hugely negative impact on the refinancing situation for banks and corporates. We decidedly call for the publication of data on an aggregated basis only (prices, volumes and time ranges). In this way market participants are not able to see for what kind of conditions their competitors and counterparties were able to trade. The obligations for best-price execution and market conformity that are already in place ensure investor protection already today.

Question 12: Given the current structure of the corporate bond market and existing systems, what would be a sensible benchmark for interpreting "as close to real time as possible"?

The current system architecture in place enables our member institutions to report the information overnight. Any new kind of intraday reporting implementation would be a costly burden for small and medium sized banks like our members.

Question 13: On the basis of your experience, have you perceived a lack of pre-trade transparency in terms of access to and the content of pre-trade information available in the market for ABS?
Question 14: Is pre-trade transparency information readily available to all potential market participants?
Question 15: Is pre-trade information currently available in the ABS market consolidated and effectively disseminated to those market participants who make use of it?
Question 16: Which potential benefits and drawbacks of a pre-trade transparency regime do you see for the ABS market? If you see drawbacks, please explain how these might be mitigated.
Question 17: Which key components should a pre-trade transparency framework for ABS have? Which pre-trade information should be disclosed?
Question 18: On the basis of your experience, have you perceived a lack of pre-trade transparency in terms of access to and the content of pre-trade information available in the market for CDOs?
Question 19: Is pre-trade transparency information readily available to all potential market participants?
Question 20: Is pre-trade information currently available in the CDO markets consolidated and effectively disseminated to those market participants who make use of it?
Question 21: Which potential benefits and drawbacks of a pre-trade transparency regime do you see for the CDO market? If you see drawbacks, please explain how these might be mitigated.
Question 22: Which key components should a pre-trade transparency framework for CDOs, have? Which pre-trade information should be disclosed?
Question 23: Which of these criteria to determine the first phase of the phased approach do you consider most relevant? Are there other criteria which should be taken into account?
Question 24: Do you have specific ideas on which kind of ABS and which kind of CDOs should be covered by the first phase?

As already outlined in our answer to question 10, pre-trade transparency for asset backed securities (ABS) and collateralized debt obligations (CDOs) causes the same substantial problems as for corporate bonds. Both are traded exclusively bilaterally over the counter via phone and there are no things like market making or executable quotes in place. The necessary pre-trade information comes from non tradable Bloomberg quotes and Axes that are shown to the market per counterparty via mail or phone. Since these products should be traded by professionals that are able to evaluate value and pricing of such instruments knowing where markets are, there is no need for further protection for these investors. The obligations for best-price execution and market conformity that are already in place ensure investor protection already today.

Question 25: Do you consider that it would be appropriate to use the same framework for posttrade transparency for corporate bonds and structured finance products? Please elaborate.

As already outlined in our answer to question 10 for corporate bonds, also for ABS and CDOs the information should be published in an aggregated way only (prices, volumes and time ranges), so market participants are not able to see how the counterpart and competitor was able to trade.

Question 26: If so, do you agree that the same calibration parameters should be used for structured finance products as for corporate bonds? Or do you think different size and time thresholds should apply?

We do not see a difference.

Question 27: On the basis of your experience have you perceived a lack of pre-trade transparency both in terms of access to and the content of the information available in the CDS market?

The credit default swaps market is a market with a high degree of competition with professional participants. As long as there is no central clearing through a central counterparty (CCP) in the derivatives business, there is always a certain default risk regarding counterpart and underlying. This fact leads to differing prices for every single counterpart for the same underlying. In case such information would be party of any kind of pre- or post-trade transparency this would lead to unnecessary discussions in the market. Another factor influencing the quotes are package deals, e.g. relative value trades comprising two trades at the same time. Here bid-ask spreads are tighter and – without this information – the price alone would mislead other not involved parties.

From our perspective it would make send that only CCPs should be obliged to pre- and post-transparency. In addition credit default swaps are not traded through technical systems up to now as the limits for every counterpart have to be checked in advance. Therefore booking and documentation is handled manually in most cases and the time limit set for publication for bonds could never be met.

Question 28: Is pre-trade transparency information readily available to all potential market participants?

Yes, but it depends on definition of “potential market participants” and “pre-trade transparency information”.

Question 29: Is pre-trade information currently available in the CDS market consolidated and effectively disseminated to those market participants who make use of it?

Question 30: Which potential benefits and drawbacks of a pre-trade transparency regime for CDS do you see? If you see drawbacks, please explain how these might be mitigated.

Benefits:

- for trading and controlling purposes, ability to check, if you trade at the money

Drawbacks:

- arbitrage
- market-inefficiency
- the higher market transparency the higher costs the lower margins
- crowding out of small market participants.

Question 31: Which key components should a pre-trade transparency framework for CDS have? Which pre-trade information should be disclosed?
Question 32: In your view, would the post-trade transparency calibration parameters (i.e. transaction size thresholds, information to the published and timing of publication) proposed for corporate bonds in Section IV be appropriate for a) Single name CDS? and b) Index CDS? If not, please elaborate the reasons and propose alternative parameters (including justifications).

Due to the complexity of the products and the already existing data warehouse, please see our answers to question 10 and 11 for further developments in this regard.

Question 33: In your view, should sovereign CDS be included within the post-trade transparency framework for CDS? And if so, should the calibration parameters for single name and sovereign CDS be aligned? If not, please explain why they should be different and propose an alternative approach for sovereign CDS (including justifications).
Question 34: On the basis of your experience have you perceived a lack of pre-trade transparency in terms of access to pre-trade information on a) interest rate derivatives, b) equity derivatives, c) commodity derivatives and/or d) FOREX derivatives and the content of the information regarding these products available in the market?

a) IR derivatives

Information on prices for standard derivatives are easily obtainable through a number of sources, via the internet, banks, brokers, exchanges and market information systems (Bloomberg, Reuters). There are multiple providers of pricing and there is massive competition between banks for standard and tailor made products.

b) EQ derivatives

We have no comment on this matter.

c) Commodity derivatives

We have no comment on this matter.

d) FX derivatives

Information on prices for standard derivatives is easily obtainable through a number of sources, via the internet, banks, brokers, exchanges and market information systems (Bloomberg, Reuters). There are multiple providers of pricing as well as massive competition between banks for standard and tailor made products.

Question 35: Is pre-trade transparency readily available to all potential market participants?

IRD: Yes, FXD: No, but it depends on definition of "potential market participants" and "pre-trade transparency information".

Question 36: Is the pre-trade information currently available in these markets consolidated and effectively disseminated to those market participants who make use of it? If necessary, please specify your answer by product.

a) IR derivatives

Pre-trade information for standard derivatives is obtainable through banks and brokers. Exchanges and market information systems (Bloomberg, Reuters) provide efficient consolidated information on standard derivatives. Pre-trade information on tailor made products - by nature - is less easily consolidated but competition between market participants ensures access to multiple pricing and information sources.

b) EQ derivatives

We have no comment on this matter.

c) Commodity derivatives

We have no comment on this matter.

d) FX derivatives

Pre-trade information for standard derivatives is obtainable through banks and brokers. Exchanges and market information systems (Bloomberg, Reuters) provide efficient consolidated information on standard derivatives. Pre-trade information on tailor made products is of course less easily consolidated but competition between market participants ensures access to multiple pricing and information sources.

Question 37: Which potential benefits and drawbacks of a pre-trade transparency regime for a) interest rate derivatives, b) equity derivatives, c) commodity derivatives and/or d) FOREX derivatives do you see? If you see drawbacks, please explain how these might be mitigated.

a) IR derivatives

Prices of relevant standard derivatives are publicly available and would be appropriate for a pre-trade transparency regime for all kinds of IR derivatives. The information available to market participants ensures competition and as a result fair and tight pricing. Details beyond price information would not add to market transparency since more detailed information is closely linked to proprietary information of market participants such as internal evaluation of credit policies/strategies, modelling or statistical analysis. Aspects like volumes traded etc. are less relevant for IR derivatives since liquidity is by definition not limited.

b) EQ derivatives

We have no comment on this matter.

c) Commodity derivatives

We have no comment on this matter.

d) FX derivatives

Prices of relevant standard derivatives are publicly available and would be appropriate for a pre-trade transparency regime for all kinds of FX derivatives. The information available to market participants ensures competition and as a result fair and tight pricing. Details beyond price information would not add to market transparency since more detailed information is closely linked to proprietary information of market participants such as internal evaluation of credit policies/strategies, modelling or statistical analysis. Volumes traded etc. are less relevant for FX derivatives since liquidity is hardly limited.

Question 38: Do you believe that pre-trade transparency would be desirable for some or all types of OTC derivatives (i.e. equity, interest rate, forex and commodity derivatives)? Which key components should a pre-trade transparency framework for any of these above mentioned derivatives have? Which pre-trade information should be disclosed?

a) IR derivatives

Transparency is already an integral part of this market; all derivatives are priced on a common basis of standard derivatives whose prices are fully transparent and who are highly liquid in trading.

b) EQ derivatives

We have no comment on this matter.

c) Commodity derivatives

We have no comment on this matter.

d) FX derivatives

We have no comment on this matter.

Question 39: On the basis of your experience have you perceived a lack of post-trade transparency, both in terms of access to relevant information and the content of this information for any of the following markets: a) interest rate derivatives, b) equity derivatives, c) commodity derivatives and d) FOREX derivatives?

a) IR derivatives

No such lack has been observed in IR derivative products.

b) EQ derivatives

We have no comment on this matter.

c) Commodity derivatives

We have no comment on this matter.

d) FX derivatives

No such lack has been observed in FX derivatives.

Question 40: Do you believe that additional post-trade transparency would be desirable for all of the above instruments? If not, which ones would benefit from greater post-trade transparency?

a) IR derivatives

IR derivatives would not benefit from greater post-trade transparency.

b) EQ derivatives

We have no comment on this matter.

c) Commodity derivatives

We have no comment on this matter.

d) FX derivatives

FX derivatives would not benefit from greater post-trade transparency.

Question 41: Is post-trade transparency readily available to all potential market participants? Does this vary by asset class?

a) IR derivatives

Most IR derivatives are highly transparent, exceptions can be found among highly structured products and in particular among hybrid products linked to different asset classes like IR and commodities. Market information is disseminated more and more real-time or near real-time so that even non-frequent users of those products do not suffer from disadvantages compared to market professionals.

b) EQ derivatives

We have no comment on this matter.

c) Commodity derivatives

We have no comment on this matter.

d) FX derivatives

Most FX derivatives are highly transparent, exceptions can be found among highly structured products and in particular among hybrid products linked to different asset classes like IR and commodities. Market information is disseminated more and more real-time or near real-time so that even non-frequent users of those products do not suffer from disadvantages compared to market professionals.

Question 42: Which potential benefits and drawbacks of a post-trade transparency regime for a) interest rate derivatives, b) equity derivatives, c) commodity derivatives and d) FOREX derivatives do you see? If you see drawbacks, please explain how these might be mitigated.

a) IR derivatives

Benefit of a post-trade transparency regime might be a higher level of observed comfort for smaller and less market participants (market users). Those benefits would come in the form of further documentation obligations accompanied by increased costs adding to market concentration by favouring bigger market participants and thus decreasing competition.

b) EQ derivatives

We have no comment on this matter.

c) Commodity derivatives

We have no comment on this matter.

d) FX derivatives

The benefit of a post-trade transparency regime might be a higher level of observed comfort for smaller and less market participants (market users). Those benefits would come in the form of further documentation obligations accompanied by increased costs adding to market concentration by favouring bigger market participants and thus decreasing competition.

Question 43: Which are the key components (e.g. qualitative or quantitative criteria) which should be taken into consideration when designing such a post-trade transparency framework?

Key components should be prices of relevant reference rates, standard products, indices and futures. Other information than that is rather adding to obstructing transparency and can easily be detrimental to the goal of objective information.

Question 44: Do you think that a post-transparency regime could have some additional valuable externalities in terms of valuation, risk measurement and management, comparability and other uses in price discovering process on related underlying reference instruments?

This might well be the case in markets with currently not very transparent pricing in readily accessible asset classes. Also in markets with limited supply in products due to technical limitations, a post-trade transparency regime can add to quality of information, confidence of users and in consequence to higher market depth and price quality.

Contact:

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