



# Transparency, Best Execution & Emerging Market Structure Trends

Ben Pott, 4 July 2017

# Agenda

- > MiFID II – timeline and introduction
- > Market Structure under MiFID II
- > Transparency Regime
- > Reporting Requirements and Best Execution
- > Outstanding Issues

## MiFID II timeline and introduction

- > MiFID II is scheduled by the EC to take effect 3 January 2018
- > Extends MiFID I obligations to all financial instruments, and implements G20 objective of trading OTC derivatives on electronic venues, where appropriate, and aims at aligning with Dodd-Frank
- > For fixed income products, intermediated business will take place on OTF, MTF or RM. Bilateral business will be conducted OTC or on an SI (depending on a bank's total client business).
- > For all trading venues and SIs, both pre- and post-trade transparency rules apply as well as onerous reporting requirements. SI's have to make quotes 'available' to their clients, whilst venues are required to make the information available to the public.
- > There are waivers from transparency requirements where orders/transactions exceed certain threshold or where illiquid instruments traded.

## Market Structure under MiFID II

- Non-discriminatory access to trading venues and fair and transparent fee schedules
- Enabling 'open' access to clearing houses to introduce competition in European futures markets
- Introduction of OTF and SI regime provides level playing field for multilateral and bilateral trading

	<b>Regulated Market</b>	<b>MTF</b>	<b>OTF</b>	<b>Systematic Internaliser (SI)</b>
<b>Financial instruments</b>	Equity and non-equity	Equity and non-equity	Non-equity only	Equity and non-equity
<b>Execution of transactions</b>	Non-discretionary	Non-discretionary	Discretionary	Discretionary
<b>Proprietary capital</b>	Prohibited	Prohibited	Prohibited, with exceptions	Expected
<b>Matched principal trading</b>	Prohibited	Prohibited	Permitted in some cases with client consent	Only in exceptional circumstances

## Transparency Regime

- **Pre-trade requirements**: extended to non-equities (including bonds, structured finance products, emission allowances and derivatives) which means RMs, MTF and OTFs are required to publish current bid and offer prices and depth of trading interest at those prices in electronic form (at least above SSTI – i.e. block size) and to the public
- **Pre-trade transparency** waivers available for (i) large in scale (LIS) orders; (ii) actionable indications of interest in RFQ and voice systems above size-specific to instrument threshold; and (iii) illiquid instruments. All to be set by ESMA.
- **Post-trade reporting requirements** near-real time (within 15mins) to the public by venue or via APA.

# Transparency regime for fixed income markets

## Level 1 requirement ESMA proposal Level 2 Documents

<b>SI Threshold</b>  Frequent & substantial basis per ISIN	Quarterly assessment (6 months data)	Bank-specific thresholds	EU wide thresholds			
	Frequent	∅ once a week	2.5 % trades (for liquid instruments)			
	Substantial basis	25% OTC volume	1% volume			
<b>Liquidity</b>  Quarterly assessment including transactions of preceding calendar year	Liquid market if all criteria met on a cumulative basis			Newly issued instruments are assessed via issue size for a phase in period until ESMA calculations are available		
	Average daily notional amount	Average daily number of trades	Percentage of days traded in period			
	EUR 100,000	15	80%			
<b>Pre &amp; Post Trade Thresholds</b>  Quarterly calculation of thresholds excluding trades smaller than 100k  Direct implications of thresholds on required transparency	Calculation		SSTI pre-trade	LIS pre-trade	SSTI post-trade	LIS post-trade
	Trade-percentile (excl. trade tickets smaller than 100k)		30	70	80	90
		Up to pre-trade SSTI	Up-to post trade SSTI	Up-to post trade LIS		
	Liquid Bond	Pre trade transparency	Real time post trade		Possible delays (price T+2; volume up to 4 weeks)	
	Illiquid Bond	No pre trade transparency	Possible delays (price T+2; volume up to 4 weeks)		Possible delays (price T+2; volume up to 4 weeks)	

## Implications

- Difficulty of setting thresholds neither too high nor low
- Unknown source for denominator
- IBIA approach agreed, liquidity assessed for each ISIN
- Liquidity criteria are very low
- Revisions to SSTI threshold level over time
- Delays at NCA discretion, might result in national inconsistencies

## Reporting Requirements and Best Execution

- Transaction reporting for participants and venues (in the case of non-MiFID firms).
- Reference data reporting obligations for all venues and SIs.
- Order data record keeping obligations (for submission to regulators on request).
- Best execution data reporting requirements for SIs / venue operators.

## Outstanding Challenges

- > Scope of instruments subject to MiFID II depends on definition of which instruments are considered to be 'Traded on a Trading Venue'
  - > Will determine how 'attractive' off-venue trading is compared to trading on venue
  
- > Liquidity and size thresholds?
  - > Will determine the extent of pre-trade transparency for fixed income products
  
- > Market size and SI determinations?
  - > May drive on-venue trading and will determine market structure and buy-side impact
  
- > Transaction reporting for trading venues?
  - > Extraterritorial requirement for venues to transaction report for third country firms including personal data
    - could mean split liquidity if customers unhappy about trading on EU venue



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