Wholesale Markets Brokers' Association and London Energy Brokers' Association Reply to the ESMA Call for Evidence – The Evaluation of Regulation (EU) 236/129 (SSR)

The Wholesale Markets Brokers' Association and London Energy Brokers' Association

The Wholesale Markets Brokers' Association (WMBA) and the London Energy Brokers' Association (LEBA) (*jointly referred to in this document as the '**WMBA**'*) are the European industry associations for the wholesale intermediation of Over-the-Counter (OTC) markets in financial, energy, commodity and emissions markets and their traded derivatives. Our members are Limited Activity and Limited Licence firms (as defined by the UK Financial Services Authority) that act solely as intermediaries in wholesale financial markets.
WMBA members are active in arranging liquidity and executing the majority of trades across all the relevant markets including equities, sovereign and corporate bonds. These trades are executed either on an OTC basis, on an MTF or on a regulated market. WMBA member firms together operate 36 MTFs, however these platforms do not establish individual nor common "close" prices.

Introduction

WMBA welcomes the opportunity to respond to the issues raised in the Call for Evidence in respect the evaluation of the Short Selling Regulation.

The WMBA considers it appropriate to only reply to this call for evidence in respect of areas which have direct relevance to its members and hence the response is limited to section VII - . Intervention powers and emergency measures.

Key messages:

- A distinction between liquid and illiquid bonds should be made, so that only bonds for which there is a liquid market would truly be considered when assessing whether or not to impose intra-day restrictions. This would mean that authorities would receive better and more meaningful data on short selling and it would lessen the risk of unnecessary restrictions in bond trading whilst aiding the overall health of the market.

- In scope price/yield movements should referenced singularly and be monitored by Trade Repositories. Not only is this more efficient, but also a single price close can be established daily from which variation can be assessed. Venues cannot comply with the requests being made to them to help disclose significant intraday price movements.

Response

Q28: Do you consider the current thresholds set to identify a significant intra-day fall in price of a financial instrument are appropriate for all instruments? If not what thresholds should be set and why?

WMBA members are concerned that the failure to distinguish between liquid and illiquid bonds when setting the threshold for this type of instrument will lead to regulators receiving substantial amounts of potentially irrelevant data which they will then need to query with firms on the basis it indicates some sort of short selling issue, when in fact it simply reflects that trading in many of these instruments is episodic. An increase in bond illiquidity has been shown to be the dominant factor in driving up yield spreads[1] – therefore price falls in bonds may simply be the result of there being an illiquid market for that type of bond, rather than as a result of short selling.

One solution to this might be to use the definition of 'liquid market' in the current text of MiFIR Article 2 (7a) to set the framework for distinguishing between bonds for which there is a liquid market and bonds for which there is not a liquid market. WMBA would then propose that submissions in respect of bonds are only required when the base price (and hence the movement) is within the last 30 days. Any movement outside this timescale should be documented and made available to the competent authority (who are also collecting data and monitoring transactions for market abuse) on request.

WMBA/LEBA would be pleased to substantiate both extent of products traded and issues around the episodic point with data should that be required by either the competent national authority or ESMA.

Q30: Do you have any other comments on the provisions of the Regulation concerning Intervention powers and emergency measures or how they have operated since 1 November 2012?

<u>Venues cannot comply with the requests being made to them to help disclose significant intraday price movements.</u>

For the financial instruments in scope which are listed on MTFs operated by wholesale market brokers *(listed in annex 3 of the Regulation; as well as those potentially to be executed on OTFs),* venues do not record any closing prices across all corporate bonds and associated CDS due to the episodic nature of trading in such instruments (see above). Listed financial instruments and derivatives may not trade on a daily basis, and the price may differ according to the nature of the counterparties and the post trade infrastructures or collateralisation. Indeed, any 'per venue' methodology could lead to different outcomes for the same instrument depending on its last trade at that venue.

In common with the WMBA stance on the commodity aspect of MiFID2, it feels that the correct position is to place the responsibility for monitoring price movements into the new Trade Repositories regimes where all trades and also participants' positions may be more efficiently monitored, with a single market close established daily. This task would be made more straightforward with the advent and implementation of a utile identifiers regime including 'LEI' & 'UTI' [or 'USI'] for reporting, aggregation and analysis.

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[1] The Illiquidity of Corporate Bonds, Jack Bao, Jun Pan, Jiang Wang
http://www.mit.edu/~junpan/bond_liquidity_jf.pdf