



Aviva Investors' response to CESR's Technical Advice to the European Commission in the context of the MiFID Review: Non-equity markets transparency

Aviva plc is the world's fifth-largest¹ insurance group, the largest insurance services provider in the UK and is one of the leading providers of life and pension products in Europe and is actively growing its long-term savings businesses in Asia Pacific and the USA. Aviva's main business activities are long-term savings, asset management and general insurance.

Aviva Investors is the global asset management business of Aviva plc, managing assets in excess of £249² billion across a range of real estate, equity, fixed income, money market and alternative funds. The business operates under a single brand with over 1,300 employees in 16 countries across North America, United Kingdom, Continental Europe, and Asia Pacific. We are dedicated to building and providing focused investment solutions for clients which include local government organisations, pension funds, wholesale and retail banks, insurance companies, charities and private wealth managers.

Please note that we ask for our submission to remain private and therefore, not be made available for public inspection.

We have consulted with various different product specialists within our business and this response reflects these views.

Please find below our answers to the specific questions raised.

GENERAL ACCESS TO PRE- AND POST-TRADE INFORMATION

Q. 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

Pre-trade: We go to a number of brokers for prices. We look at dealer quotes and market pricing and availability, spreads to government bonds, spreads to asset swaps and spreads to Z-spreads.

Post-trade: We look at Bloomberg and observe how prices change and from this we interpolate what has happened.

b) structured finance products (ABS and CDOs)

We have no specific comments to make.

c) CDS

Pre-trade and post-trade: We receive information by telephone and from Bloomberg emails.

d) interest rate derivatives

Pre-trade: There is already a degree of pre-trade information for certain types of business. Market makers place indicative prices on screens (Bloomberg and/or Reuters).

¹ Based on gross worldwide premiums for the year ended 31 December 2008

² As at 31 December 2009

Post-trade: There is virtually no post-trade information (other than discussion in the market place) but most trades are too bespoke to be of any comparable value. A trade could be placed for various reasons which would not be known to receivers of post-trade information and thus there is a risk that post-trade information could be misinterpreted by the market.

e) equity derivatives

Pre-trade: There is no published pre-trade information. Prices are obtained by telephoning three counterparties or just two if it is important not to let the market know about a large trade. For OTC equity options, it is possible to look at the listed markets for an idea of where the OTC should be trading. If there are listed options on the underlying (but with a different maturity or strike) then it is possible to interpolate from these prices. If there are no listed options or if the listed option market is very small, then price discovery is more difficult.

Post-trade: OTC trade information is not reported.

f) foreign exchange derivatives

Pre-trade: Bloomberg and Reuters aggregate sample prices from counterparties and this gives an estimate for prices but it is not very meaningful. Bloomberg has indicative two way prices. Also, there is FXall for forwards (but this has a limited number of participants), Electronic Broking System (EBS), Reuters D2 Dealing System, FXstreet.com and IG Index

Post-trade: There is a gap for OTC post-trade information.

g) commodity derivatives

Pre-trade: Price estimates can be calculated from looking at similar instruments on screens or by calculating option premium. If the trade is similar to an exchange traded instrument then there will be some pre-trade transparency. However, most OTC derivative trades are, almost by definition, not transparent. The OTC market is bespoke and the universe of possible transactions almost infinite. Therefore, it is very difficult to conceptualise how a pre-trade transparency regime would work in such a large number of instruments. In practice, quotes are obtained from two or three counterparties. If quotes were obtained from more counterparties, then there would be wider knowledge of the trade and the risk of front-running by the counterparties who did not win the trade. The risk is borne by the counterparty that wins the trade and then has to unwind the risk. The greater the transparency, the greater will be their risk and this will be reflected in the price.

Post-trade: There is no post-trade transparency. Again, there would be limited usefulness because it is unlikely that reported trades would be similar to any other trade and also because prices can vary significantly from day to day so reported information is very quickly out of date.

CORPORATE BONDS

1. Scope of corporate bonds transparency regime

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

We have no specific comments to make.

Q. 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.

Yes, we consider that it would be more appropriate to consider covered bonds as structured finance products as these are effectively ABS.

2. Pre-trade transparency for corporate bonds

- Q. 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?

We believe that market participants receive sufficient pre-trade transparency to make trade decisions.

- Q. 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.

We consider that the majority of European corporate bond markets are wholesale and that the typical nominal value of corporate bond trades excludes retail investors. In respect of wholesale investors, we consider that the sell side may have access to more information than the buy side.

- Q. 6 Is pre-trade transparency efficiently disseminated to market participants? Should pre-trade information be available on a consolidated basis?

We believe that market participants receive sufficient pre-trade transparency to make trade decisions.

- Q. 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.

As a portfolio manager for professional clients we will focus our response on the wholesale market only. Please note however that the ultimate beneficiaries of the institutional pension and insurance funds that we manage are retail clients.

The potential benefit of a pre-trade transparency regime for the wholesale market for corporate bonds is that transparency should in theory increase efficiency. We have supported pre and post-trade transparency regimes in equity markets for this very reason. However, it can be argued that a potential drawback of a pre-trade transparency regime for the wholesale corporate bond market is that it may lead to illiquidity as banks may withdraw from the market if they are forced to be transparent about how much capital they have at risk. Alternatively, banks might remain in the market but cost in this additional risk into pricing which is also a drawback as this would ultimately reduce investors' returns. These potential drawbacks could be mitigated by the size at which market makers must provide prices (pre-trade information) and on the post-trade side by delaying reporting of large trades to end of day and reporting very large trades as 'above x' rather than giving actual size.

Another potential drawback is that more transparency could cause the corporate bond market to become polarised, with trading focusing on liquid bonds and further reducing for illiquid bonds. This effect could also be explained however by the availability of the corresponding CDS market for the more liquid corporate bonds.

- Q. 8 What key components should a pre-trade transparency framework for corporate bonds have? What pre-trade information should be disclosed?

We have no specific comments to make.

3. Post-trade transparency for corporate bonds

Q. 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?

We do not think that this is necessary.

Q.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).

If a regime were to be introduced, then our views would be as follows:

- *We would strongly support delaying publication of large trades to end of day as we are comfortable with end of day post-trade reporting but consider that intra-day is too risky.*
- *We would agree with reporting actual volume up until a certain level then reporting 'above €x million'.*

Q.11 Should other criteria be considered for establishing appropriate post-trade transparency thresholds?

It is possible that different values for transaction size might be appropriate for different bond types, for example, €1 million for high yield and €5 million for investment grade. However, we recognise that one common framework would be clearer to operate.

Q.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"?

Trading methodologies are less automated in the corporate bonds market than the equities market. It is worth noting that the required speed of trade capture may involve process changes and investment in systems and the aggregated cost of this should be taken into account in cost/benefit analysis.

If this requirement only requires data from the broker, then we believe that 15 minutes may be possible but this should be confirmed with these participants. If this requirement will require further information from the buy-side then a longer time delay would be required. This is because the majority of buy-side firms rely on their brokers to trade report in accordance with MiFID Article 28 and therefore current systems and processes are very unlikely be able to capture and report the required information.

STRUCTURED FINANCE PRODUCTS (ABS AND CDOS)

1. Pre-trade transparency for structured finance products

a) ABS

Q. 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?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

Q. 14 Is pre-trade transparency information readily available to all potential market participants?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

- Q. 15 Is pre-trade information currently available in the ABS market consolidated and effectively disseminated to those market participants who make use of it?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

- Q. 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.

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

- Q. 17 Which key components should a pre-trade transparency framework for ABS have? Which pre-trade information should be disclosed?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

b) CDOs

- Q. 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?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

- Q.19 Is pre-trade transparency information readily available to all potential market participants?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

- Q. 20 Is pre-trade information currently available in the CDO markets consolidated and effectively disseminated to those market participants who make use of it?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

- Q. 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.

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

- Q. 22 Which key components should a pre-trade transparency framework for CDOs, have? Which pre-trade information should be disclosed?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

2. Post-trade transparency for structured finance products (ABS and CDOs)

- Q. 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?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

Q. 24 Do you have specific ideas on which kind of ABS and which kind of CDOs should be covered by the first phase?

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

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

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

Q.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? Please indicate whether your response is relevant for both ABS and CDOs.

We have no specific comments to make as we have unfortunately not been able to review this section of the consultation paper in the time given.

CREDIT DEFAULT SWAPS (CDS)

General comment on the CDS market

We have serious concerns about proposals for pre and post-trade transparency in the CDS market. There are fewer participants in this market than before the financial crisis and we are still waiting for counterparties to come back into the market. We are concerned that these transparency proposals might discourage those participants from returning. The CDS market works because participants do not know the size that each one has. Less transparency in fact leads to greater market stability. If transparency were increased, there might be greater volatility. The CDS market is driven by perception and can exhibit herd behaviour and therefore it is important to avoid creating panic. We believe that these proposals would exacerbate these features of the CDS market. We are concerned that, with full transparency, trading would become more polarised, bid/offer spreads would widen and liquidity would be reduced.

1. Pre-trade transparency for CDS

Q.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?

No, we have not experienced any lack of pre-trade transparency that needs to be addressed. There is a great deal of research available and we receive sufficient information to make informed trading decisions.

Q. 28 Is pre-trade transparency information readily available to all potential market participants?

Yes, pre-trade transparency information is readily available to all potential market participants with access to Bloomberg and who have signed up with investment banks in order to receive such information.

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

Yes, we consider that the information is consolidated and disseminated effectively.

Q. 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.

We think that there is a risk that legislators do not fully understanding how these distinct markets work prior to making policy proposals. We would like therefore to offer our assistance and are very willing to participate in telephone or video conference calls to explain how these markets work in practice.

Q. 31 Which key components should a pre-trade transparency framework for CDS have? Which pre-trade information should be disclosed?

We have no specific comments to make.

2. Post-trade transparency for CDS

Q.32 In your view, would the post-trade transparency calibration parameters (i.e. transaction size thresholds, information to be 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 proposed alternative parameters (including justifications).

We have strong concerns about a post-trade transparency regime for CDS. We would suggest instead that it would be preferable to trade CDSs on exchange. This solution would also help the counterparty risk problem; fewer ISDAs would be required; and there would be better margin collateral.

a) single name CDS

We are very concerned that a post-trade transparency regime would be counter-productive for single name CDS. If the market is able to observe someone selling down a position in a single name CDS, there is the risk of herd behaviour where other players follow suit, fearing that someone knows something that they do not. This would then increase volatility. Whilst hedge funds might benefit from this, if they are trading on momentum, long-only market participants would suffer.

b) Index CDS

We think that a post-trade transparency regime might be more successful for index CDS than for single name CDS. This is because the bid/offer spread is smaller and there are more buyers and sellers in the market. We do not have any strong view in respect of the calibration parameters.

We are concerned about the costs of post-trade transparency for CDS as any costs incurred would be passed on via wider spreads thereby affecting the overall returns achieved by the end investors without this being matched with comparable benefits.

It has been suggested that it is possible to arbitrage the transparency regime as proposed.

Q.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).

Our views for sovereign CDS are the same as those for single name CDS under question 32 above.

DERIVATIVES (Interest rate derivatives, Equity derivatives, Commodity derivatives and FOREX derivatives)

1. Pre-trade transparency for derivatives

Q. 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) interest rate derivatives

No, we have not perceived a lack of pre-trade transparency in terms of access to pre-trade information. We consider that there is a reasonably efficient system of price discovery. Prices are very much indicative and not regarded as firm since information on firm bid and offer prices in a particular size is not that useful or relevant in this market. The market has evolved to operate an efficient system. Please note that this is not a retail market. It is important to note the following characteristics of these OTC trades:

- *OTC derivatives are not cash-settled and are not instantly completed. They may have a long life of up to 50 years.*
- *There are other considerations such as credit assessments, credit lines and ISDAs.*
- *These trades are usually linked to something else.*
- *These trades cannot be sliced into smaller parts as can be done with equity trades.*

b) equity derivatives

Yes, there is a lack of pre-trade transparency but this is not necessarily a problem. If you do not like the OTC price, you can choose to trade listed or not trade at all. The OTC market is made up of very illiquid instruments that cannot be hedged. If a third party were to find out about a trade, they could completely undermine it. It would then be impossible to trade out of the position and these can be very large positions.

c) commodity derivatives

No, we have not perceived a lack of pre-trade transparency in terms of access to pre-trade information for commodity derivatives. Price estimates can be calculated from looking at similar instruments on screens or by calculating option premium. If the trade is similar to an exchange traded instrument then there will be some pre-trade transparency. However, most OTC derivative trades are, almost by definition, not transparent. The OTC market is bespoke and the universe of possible transactions almost infinite. Therefore, it is very difficult to conceptualise how a pre-trade transparency regime would work in such a large number of instruments. In practice, quotes are obtained from two or three counterparties. If quotes were obtained from more counterparties, then there would be wider knowledge of the trade and this could compromise our position in obtaining best execution. The risk is borne by the counterparty that wins the trade and then has to unwind the risk. The greater the transparency, the greater will be their risk and this will be reflected in the price.

d) FOREX derivatives

No, we have not perceived a lack of pre-trade transparency in terms of access to pre-trade information for FOREX derivatives. There is less pre-trade information for emerging currencies as there is a lack of liquidity.

Q. 35 Is pre-trade transparency readily available to all potential market participants?

Please note that these are wholesale markets and not used by retail investors. Yes, we consider that pre-trade transparency is readily available to all potential market participants for most of these markets but with the following exceptions. Pre-trade transparency is less available for equity derivatives. Generally, the sell-side has more information than the buy-side. In the FOREX derivatives market and information access is dependent on relationships with counterparties and access to brokers.

- Q. 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.

In the interest rate derivatives market, some market makers publish more information than others. In the FOREX derivatives market Bloomberg consolidates data from 100 feeds from counterparties in order to create the Bloomberg price.

- Q. 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) interest rate derivatives

Pre-trade transparency may be beneficial for plain vanilla business but information already exists via Bloomberg and Reuters. A drawback is that this is not useful for bespoke business. Also, even though a market maker may display a price, it is not possible to trade with that counterparty unless there is an ISDA in place.

b) equity derivatives

A potential benefit might be more efficient prices but this would be balanced by the drawback of loss of anonymity. Loss of anonymity would increase risk and potential cause extremely unfavourable prices or even make it impossible to trade out of a position.

c) commodity derivatives

The OTC market is bespoke and the universe of possible transactions almost infinite. Therefore, it is very difficult to conceptualise how a pre-trade transparency regime would work in such a large number of instruments. In practice, quotes are obtained from two or three counterparties. If quotes were obtained from more counterparties, then there would be wider knowledge of the trade and this could compromise our position in obtaining best execution. The risk is borne by the counterparty that wins the trade and then has to unwind the risk. The greater the transparency, the greater will be their risk and this will be reflected in the price.

d) FOREX derivatives

A potential benefit would be firm prices but these are already available in EBS. Certainty of market depth i.e. what volume can be traded at a given price, could provide both benefits and drawbacks. This information is helpful for trading. However, if the actual depth is known, there is more scope for manipulation.

- Q. 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) interest rate derivatives

No, we do not consider that a pre-trade transparency framework would be desirable for OTC derivatives as its value is limited in respect of bespoke transactions.

b) equity derivatives

No, we do not think that a pre-trade transparency framework would be desirable for equity derivatives.

c) commodity derivatives

The OTC market is bespoke and the universe of possible transactions almost infinite. Therefore, it is very difficult to conceptualise how a pre-trade transparency regime would work in such a large number of instruments.

d) FOREX derivatives

We consider that pre-trade transparency information is already available.

2. Post-trade transparency for derivatives

Q.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) interest rate derivatives

There is little post-trade transparency in as much as there are not enough trades in OTC markets to report for there to be a clear picture. However, we do not perceive this as a lack of post-trade transparency because we do not make trading decisions on the basis of other participants' trades. We do not consider that post-trade transparency is useful for bespoke business such as LDI trades as these are commercially sensitive trades to hedge pension risks for our clients.

b) equity derivatives

Yes, there is a lack of post-trade transparency but this is a given aspect of trading OTC.

c) commodity derivatives

There is no post-trade transparency but this would be of limited usefulness because it is unlikely that reported trades would be similar to any other trade and also because prices can vary significantly from day to day so reported information is very quickly out of date.

d) FOREX derivatives

Yes, there is a lack of post-trade transparency. It is not possible to see what has been filled at what price. It is possible to see prices change but not to know what has caused that change.

Q.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?

No, we do not consider that additional post-trade transparency would be desirable for these instruments. We did however receive one comment, in respect of FOREX derivatives, that additional post-trade transparency could be helpful for compliance purposes to demonstrate why a decision was taken if this is queried.

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

Post-trade transparency is not readily available as it is not required.

Q.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) interest rate derivatives

We see the following drawback. Interest rate trades are not done in isolation but against something else that is not transparent. It may be part of an anchor trade e.g. a relative value trade. It is not necessarily a view on interest rates but part of something else. Therefore it is misleading to report one element on its own.

b) equity derivatives

The greatest drawback is the loss of anonymity.

c) commodity derivatives

We have no specific comments to make.

d) FOREX derivatives

It would be beneficial to know the volume of trades that went through in a day although this may be available in some data feeds already.

Q.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?

We are not in favour of a post-trade transparency regime and have set out some specific reasons below in relation to OTC derivatives.

a) interest rate derivatives

We do not think that a post-trade transparency framework will work for very bespoke areas. Given the potential size of this universe, there would be too much information for anyone to be able to use.

b) equity derivatives

Anonymity is key. Also, it is crucial to preserve the OTC market and not move this market on exchange.

c) commodity derivatives

We have no specific comments to make.

d) FOREX derivatives

Anonymity is the key component. It is critical not to disclose large positions as this would cause the price to move against you.

Q.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?

a) interest rate derivatives

We do not think that post-trade transparency on derivatives in isolation will add value as these are too bespoke. If we have placed a trade to hedge a risk, the counterparty is then taking on risk. If our side is disclosed and the counterparty has not been able to offload the risk, then their risk is increased. This may then make the trade more expensive for us. It is not clear that post-trade transparency will improve the cost efficiency of the market.

b) equity derivatives

We recognise that a post-trade transparency regime would improve valuation, making it easier, more accurate and less subjective.

c) commodity derivatives

We have no specific comments to make.

d) FOREX derivatives

Yes, we think post-trade transparency could be useful in demonstrating that we did a good job or in proving why we did something. For example, it could be used to prove why you had to have wider prices if there was a lack of volume/liquidity that day.