NON EQUITY TRANSPARENCY
REF: CESR/08 – 1014

INTRODUCTION

TLX S.p.A. is a market operator company, operating two trading venues: a regulated market TLX and a multilateral trading facility EuroTLX, both dedicated to trading of fixed income securities and calibrated to meet the investment needs of non-professional investors. The company has always supported the extension of MiFID equity transparency regime to other classes of financial instruments. We believe that post-trade transparency is a necessary tool for any meaningful implementation of the Financial Services Action Plan of 1999: fair competition in the financial services industry and transparency, all leading to better investor protection.

TLX S.p.A. from the outset ensured a standardized set of pre- and post trade transparency for all financial instruments traded, going well beyond the existing transparency requirements. In the recent year we saw trading volumes double on our two trading venues, a clear sign that investor do appreciate trade transparency.

EVIDENCE

Furthermore, we have evidence at hand that transparency actually nurtures liquidity, at least in the realm of retail markets. As already noted, the crisis practically made a secondary market collapse, sweeping away liquidity, as liquidity providers retreated from market making. This phenomenon was best seen in the OTC markets, where the usual indicative quotes lost even this quality. Instead, during this same period, the Italian organized bond markets, i.e. MOT operated by Borsa Italiana and TLX and EuroTLX operated by TLX S.p.A., saw an increase in trading volumes, even if liquidity providers had difficulty keeping quoting during every trading session.
Thus our experience of the recent crisis is that liquidity and transparency need not contradict each other: as far as retail investors are concerned, transparency attracts trades.

In order to appreciate the increase in volume on MOT and TLX/EuroTLX during the worst period of the crisis, please see the table below.

Number of contracts on TLX/EuroTLX and MOT, see the crisis months in **bold**.

Period	TLX/EuroTLX	MOT
gen-08	161,149	281,591
feb-08	183,414	243,017
mar-08	162,197	207,240
apr-08	181,984	242,760

mag-08	185,731	238,304
giu-08	195,198	248,207
lug-08	185,875	233,008
ago-08	117,727	142,333
set-08	**226,975**	**263,499**
ott-08	**284,573**	**390,353**
nov-08	**221,618**	**295,722**
dic-08	202,862	264,740

EXECUTIVE SUMMARY

We expect that the present consultation will not simply aim at measuring how non-equity post trade transparency can prevent and/or mitigate the many market crises to come. It is not its regulatory objective. Transparency is a tool to render the distribution of risk more equal among investors, big, small or intermediate as they may be.

Thus, transparency, including post trade transparency, is a means to improve investor protection in the European financial markets, and not a remedy for the recent liquidity crisis whose origins lie elsewhere.

Transparency is the most cost-efficient measure to protect retail investors. It underlies the best execution duties and other fiduciary duties imposed on intermediaries vis-à-vis their retail clients. Any serious effort to enforce the best execution obligation must insist on better transparency, including post-trade transparency, so that both intermediaries and their clients have a reference point. Otherwise the retail clients will be left – literally – to their own devices in their investment activity, loosing their confidence in the fair operation of the market and jeopardizing the objective of integration of the European financial markets.

Below we answer on the issues that are directly relevant for our activity and for which we can offer a practical insight.

SPECIFIC QUESTIONS AND ANSWERS

PART I, SECTION 2

Q1: Do you believe the situation described above may be symptomatic of a market failure ?

We believe that the situation described above is symptomatic of a market failure even if we are reluctant to attribute it all to the information asymmetry.

Q2: Have you perceived a potential asymmetry of information between market participants?

We believe that answering the above question is unnecessary: that the asymmetry of information between, roughly speaking, professional and non-professional investors exists is a well established phenomenon that CESR itself admitted in its prior consultation of 2007 and in the present one. The real question revolves around whether such asymmetry is detrimental to the interests of some categories of investors and/or to the financial market as such.

MARKET LIQUIDITY

Q3: In your view, what were the key reasons which have led to sharply reduced liquidity in secondary trading of European corporate bonds since 2007?

We believe that CESR rightly named the key reasons of the liquidity crunch experienced since 2007.

We also believe that a "fear factor" played a role here, understood as uncertainty as to which assets are truly "toxic", which ratings are fair and which issuers will be hit next, as a spill over effect.

Q4: Do you believe that additional post-trade transparency of European corporate bonds would have helped maintain liquidity in stressed market conditions? Can you please explain why?

One has to keep in mind that post trade transparency is not to prevent liquidity shortages but merely to attenuate its adverse consequences for "price takers"; it is the market's integrity and good governance index. That said, we believe that – by overcoming the above noted uncertainty - additional post trade transparency could have helped maintain liquidity in the stressed conditions.

BID/OFFER SPREAD

Q5: In your view, what were the key reasons for the widening of the bid/offer spreads for European corporate bonds?

We agree with CESR that increased uncertainty and volatility were the key reasons for the widening of bid/offer spreads for European corporate bonds.

Q6: Do you believe that greater post trade transparency would have been helpful in limiting the widening of the bid/offer spreads we have observed for European corporate bonds?

Just like in case of liquidity crunch and for the same reasons (please see answers under Q3 and Q4) we believe that greater transparency could have helped limit the widening of spreads.

[...]

VALUATIONS

Q12: Would additional post trade transparency in distressed market conditions help valuation?

Although we do not engage in valuating financial instruments, we believe that greater post trade transparency always helps more accurate valuation of securities. Likewise it does so help in times of market distress even if leading to actual de-valuation of a security. The point is to ensure that both the intermediary and its retail clients have a reference point against which to measure the security's performance and, in the latter case, the intermediary's.

SECTION 3

Q13: Do you agree with the potential benefits and drawbacks described above? Please provide evidence supporting your opinion. Please explain how the potential drawbacks might be mitigated.

We fully agree with the benefits of post-trade transparency described in this Section.

As to the evidence of positive correlation between increase in transparency and decrease in liquidity, as already explained above in the Introduction, we witnessed a contrary trend during the recent crisis: liquidity requirements imposed on the market makers operating on our trading venues helped maintain prices, which in turn attracted more trades. It is our conviction that in the retail markets there exists a virtuous rather than vicious circle by which increased transparency translates into more liquidity, the latter understood as market depth and/or trade volume.

Then on a more general level, we do not agree with the suggestion that <u>possibly negative impact</u> of post-trade transparency on liquidity should be decisive for regulatory non-action. First, as CESR itself rightly observes in Section 4, it all depends on the definition of "liquidity". Then "liquidity" is conditional on a number of factors such as security type and size of market participants. Without having defined first what feature of the bond market is claimed to be prejudiced by post-trade transparency, it is difficult to strike a balanced decision. We would therefore advise caution in drawing regulatory conclusions based on vague or ill-defined parameters.

Q14: Are there other main benefits or drawbacks of increased post-trade transparency in the bond markets which CESR needs to consider?

We wish to remind that clear and understandable information for "consumers" was one of the key actions to take in order to ensure implementation of the Financial Services Action Plan.

Furthermore, we believe that another long term objective of post trade transparency is the reduction of transaction costs to attract greater participation by retail and medium sized investors in the European bond market. That in turn would contribute to greater liquidity, understood as market depth and/or trade volume. Lastly, post trade transparency is a pre-condition to implement any serious best execution requirement in the European financial services regulation.

SECTION 4

Q15: What are your personal experiences with TRACE? Please specify whether you are directly trading in the US corporate bond markets on the buy or sell side.

Given the activity of TLX S.p.A. we do not engage in trading in the US corporate bond markets.

Q16: Do you see other benefits or drawbacks of the introduction of a TRACE-like post trade transparency regime for OTC trades in corporate bonds in Europe?

We believe that concentration and later dissemination of trade data by one agency/authority boosts the efficiency of post trade transparency.

Q17: Are you of the view that the more notable volume declines experienced for 144a securities, compared to securities which are covered by TRACE, is due to a lack of post trade information? Please provide rationale.

Consistently with our position under Q3, we believe that post trade transparency helps overcome uncertainty as to pricing of a security. And it is uncertainty and lack of a reference point that prevents investors from trading.

SECTION 5

Q18: Please provide information on your experience, if any, in terms of timing, content and access to information of the market-led solutions outlined above? What is your assessment of the effectiveness of the present self-regulatory scheme?

Given the activity of TLX S.p.A. we do not have direct experience neither with ICMA Standard of Good Practice nor with SIFMA.

Q19: Please provide comments on the characteristics that market-led solutions should, in your view, have.

We do not believe that the market is capable of delivering an efficient solution.

Should it attempt to do so it should cover not only high grade liquid blue chip companies but - first and foremost - high yield, illiquid and structured products, i.e. those that present most risks to the less-experienced investors. Then it should deliver all trade information in simple, standardized and comparable manner across all relevant European markets. It should furthermore be easily accessible, free of charge for its users and centralized. It should disclose all trades in real time.

As proposed by CESR itself, and as currently required of equity markets, post trade transparency could apply to trades below a certain threshold only, without adversely affecting liquidity of the market, should such link exist.

SECTION 7

Q20: Do you think that the introduction of additional post trade information on prices could help restore market confidence and maintain market liquidity in times of future crisis?
We believe that, at this point, greater post trade transparency, set along the above requisites, could help restore market confidence and maintain liquidity.

We are of the opinion, however, that post trade transparency need not pass a strict test of remedying a financial crisis in order to be considered a legitimate regulatory measure.

Q21: Do you believe that additional post trade transparency of European corporate bond markets would contribute to liquidity in normal market conditions? Can you please explain why?
As already evidenced in the Introduction and then explained under Q14, we believe that post trade transparency, meaningful, standardized and comparable, attracts trading interests.

Q22: To what extent can corporate bond market be characterised as wholesale or retail markets? How would you distinguish between wholesale and retail markets? What are the differences across the EU?
The Italian bond market has got a large retail share.
The divide line between wholesale and retail market is capacity (own account or on behalf of clients) and the order size.

On our retail market, in order to calculate the Market Performance Index, the index of price performance as against our competitor, we use the median retail size order of €50.000 for government bonds and €30.000 for other fixed income (we do not treat derivatives, except for a few Residential Mortgage and/or Public Sector Loans ABS). Given that the divide line between the wholesale and the retail market depends on the security type and the volume of the issue one cannot set a bright line.

Q23: What would be the benefits and downsides of a harmonized pan European transparency regime for:

a) **the wholesale market;**
b) **the retail market.**

Please provide arguments and fact-based data on the potential impact.
Nowhere in this paper do we postulate a pan European transparency regime for wholesale markets. We believe that market participants operating there already have access to sufficient information.

A harmonized pan European transparency regime would lower the transactions costs for all retail, small and medium size investors and provide them with a measure of performance of their investment and of their intermediary. Thus it would be a tool of investor protection.

Q24: Is the reduced reliability of the CDs market as an indicator/proxy for calculating the value/price in the cash market under certain market conditions an issue which calls for more post trade transparency of cash corporate bonds?
We are wary of postulating to introduce post trade transparency in order to boost the reliability of the CDs market as a proxy for pricing the cash bond market. In a more straightforward manner, better post trade transparency of cash bond market serves better valuation of the same.

Q25: Do you think that transparency requirements could help address wider issues such as those relating to accurate valuations?
The evidence of TRACE, cited by CESR itself, attests that post trade transparency does benefit investors by improving the valuation of corporate bonds covered by TRACE. This finding agrees with our experience.

Q26: What would be the most cost-effective way of delivering additional transparency: an industry-led solution, possibly based on a road map set by regulators, or mandatory regulatory post trade transparency requirements?

a) the retail market;

b) the wholesale market.

Please provide rationale.
Please see our answer under Q23.

In our view the most cost-effective solution for the retail market is a mandatory regulatory post trade transparency. It would provide most comprehensive and standardized scheme of post trade transparency.

Q27: Which should be in your view the key components of a post trade transparency framework for corporate bonds? Please provide your view with respect to depth and breadth of information as well as to timeliness of data as described above?
Please see our response to Q19.
A transparency framework for corporate bonds should be comprehensive of all security types under a certain order size, capable of delivering information in a clear, standardized and comparable manner. It should cover all trades reported real time. It should be easily accessible, free of charge and centralized.

Q28: Should the information on the volume be reported only below a certain size, what would be the threshold to avoid any risk of market impact?
In order to cover the retail segment we believe that a scheme similar to one for equity instruments, i.e. linking the retail order size to the average value of transaction of the given “class”, should be set up.

Q29: Would you see some benefits in step-by-step implementation of, starting with the most liquid bonds, as employed when TRACE has been introduced?

We believe that phasing the introduction of post trade transparency over a period of time would help the industry to adapt. Yet the real benefits of the system would be seen once less liquid bonds are covered.