BVI · Eschenheimer Anlage 28 · D-60318 Frankfurt am Main

Bundesverband Investment
und Asset Management e.V.

Mr.
Carlo Comporti
CESR The Committee of European Securities
Regulators
11-13 avenue de Friedland
75008 Paris
FRANKREICH

Contact:
Felix Ertl
Phone: +49 69/154090-262
Fax: +49 69/154090-162
felix.ertl@bvi.de

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CESR call for evidence: Micro-structural issues of the European equity markets (CESR/10-142)

Dear Mr. Comporti,

In response to the above mentioned consultation, please find below BVI's[1] views on the subject at hand. We are pleased to have the opportunity to comment on micro-structural issues of the European equity markets.

In general, BVI welcomes CESR´s initiative on micro-structural activities in the European equity markets. It has to be noted, however, that the Buy-Side is affected by the practices mentioned only to a small extent (e.g. indication of interest).

I. High frequency trading (HFT):

General remarks:

CESR's statement "HFT is different from what is generally referred to as algorithmic trading or black box trading" leaves room for interpretation. We agree that these terms do not describe the same market practice. In

[1] BVI Bundesverband Investment and Asset Management e.V. represents the interest of the German investment fund and asset management industry. Its 85 members currently manage assets in excess of EUR 1.7 trillion both in mutual funds and mandates for some 16 million investors. For more information, please visit www.bvi.de.

Director General:
Stefan Seip
Managing Director:
Rudolf Siebel

Eschenheimer Anlage 28
D-60318 Frankfurt am Main
Postfach 10 04 37
D-60004 Frankfurt am Main
Phone: +49.69.154090.0
Fax: +49.69.5971406
info@bvi.de
www.bvi.de

our understanding, however, both algorithmic and black box trading can, but not necessarily need to be conducted as HFT. It might be worthwhile to clarify the issue further.

Question 3 – key drivers of HFT:

The key drivers of HFT might be in general efficient IT infrastructure, low starting costs (fix costs) and large profit margins.

Question 4 – impact of HFT:

High frequency trading might have a positive effect on ticket size, market liquidity, turnover, bid/offer spreads, volatility and the price formation process. For limitations, see our answers to questions 6 and 7.

Question 6 – Does HFT pose risks to the markets?

Potentially yes. It cannot be ruled out that such activities may adversely increase the speed a market is taking, e.g. in a crash situation comparable to the circumstances which enforced the 1987 US equity crash. There are currently not enough safety levels in place.

Question 7 – Is HFT beneficial or detrimental to the markets?

Under normal conditions, HFT can mostly be deemed to be beneficial to market liquidity. It is questionable, however, if this assessment holds true also under exceptional circumstances, e.g. when there is a general liquidity shortage in the market or if the kind of liquidity provided by HFT may undesirably accelerate market moves.

Question 8 – developing in Europe:

HFT will develop over the time in Europe. It is likely to open new sources of revenue for the relevant service providers.

Question 9 – additional regulation:

There should be more safety levels in place.

II. Sponsored access (SA):

Question 1 – benefits of SA:

The concept of direct market access (DMA) should considerably speed up transactions. We do not expect any significant increase in IT costs caused by DMA.

Question 2 – risk of SA:

It remains open whether the sponsoring firms have complete overview and comprehensive risk control. Therefore the sponsoring firms should be held accountable if they allow direct market access (DMA). The usage of the DMA might result in incorrect order routing. Therefore, additional safety measures are necessary.

Questions 4 – need for additional regulatory requirements:

b – restriction on clients that use SA: Yes.
d – pre-trade filters and controls on submitted orders: Yes.

III. Co-location:

Questions 4, 5 and 6 – issues for the fairness and efficiency of the markets and within the MiFID obligations on trading platforms:

Co-location is likely to undermine fair access for all market participants for the benefit of additional income for the exchanges. The regulator has to examine this issue in detail.

IV. Fee structures:

No comment.

V. Tick size regimes:

No comment.

VI. Indications of interest (IOI):

Question 2 – benefits/downsides of IOI:

IOIs used by dark pools might in principle result in less volatility, however the price formation process might be detrimentally affected.

Question 3 – Should actionable IOIs be included in the pre-trade transparency requirements in regard to the MiFID review?

No.

Question 4 – circumstances for IOIs to be reported to a selected group of market participants:

Yes, unfriendly takeovers should be reported.

We hope you will find our comments helpful. Our response can be made public.

With kind regards

BVI Bundesverband Investment und Asset Management e.V.

(signed)
Marcus Mecklenburg
Senior Vice President

(signed)
Felix Ertl
Associate