



NON-EQUITY TRANSPARENCY

Ref: CESR/07-284

TLX S.p.A. is a company which operates two trading venues, a regulated market (TLX) and an MTF (EuroTLX), both calibrated to the needs of non-professional investors.

We would like to stress that the financial instruments mainly traded on our two trading platforms are non-equity instruments, that is the reason why TLX has been very active on the issue under consultation.

Since the beginning of the negotiations on MiFID's first level legislation we fully supported the extension of the MiFID transparency regime to other classes of financial instruments. We believe that such transparency regime applied to other financial instruments is a necessary requirement for a meaningful implementation of the Financial Services Action Plan of 1999 (of which the MiFID Directive is only a part): fair competition in the financial services industry and transparency, all leading to better investor protection.

Coming to our experience, TLX S.p.A. ensures a standardised set of pre- and post trade transparency of the two systems for all financial instruments traded, equity and non-equity alike. In doing so, TLX S.p.A. goes beyond the existing MiFID transparency requirements.

What we can say on the basis of our experience is that in the last year we saw an entry of a new market maker and an increase in trading volume of approx. 30%. In our view, these facts attest that both market makers and retail investors appreciate trading transparency, and that the latter had no negative impact on liquidity of our market makers. Indeed, we have good reasons to expect further grow in the volume of retail clients' orders routed by the market makers to our trading venues.

Specific Questions & Answers

Q1: To what extent do you agree with the CESR's assessment of the market failure in the secondary bond market?

In our view CESR correctly lists among the possible market failures in the cash bond market the asymmetry of information. We believe that the current transparency regime – limited to equities or otherwise to well-diffused instruments – tends to preserve the asymmetry of information between the professional traders/counterparties and investors, retail and mid-professional alike, in the market for non-equity instruments.

Such asymmetry of information, well perceived also by the interested parties, has got two direct consequences.

The first consequence is a very low participation of retail investors in the European bond market, as rightly noted by CESR and by some market participants. Thus, more trading transparency would encourage retail investors to invest in non-equity instruments. We believe it would also help overcome the current "home bias" that keeps the European securities markets still fragmented on the retail level.

The second consequence is the particularly damaging effect that the "corporate fraud cases" have had on the retail investors. Clearly, the corporate fraud and default cases happen and will continue to do so with or without the trading transparency. This issue is beyond the point. What matters is whether the current regime of trading transparency contributed or not to their wide spread adverse effects in the retail market.

We believe it did: in cases of *Cirio* and *Parmalat*, as well as in the default case of Argentinean bonds, this asymmetry of information permitted the intermediaries to dump the offending bonds on their unaware clients after these proved to be "junk".

Q2: To what extent do you agree with the CESR's conclusions regarding the impact of imposing mandatory pre- and post-trade transparency requirements ?

We wish to note that – as indicated in the recent European Central Bank's study¹ – as of today there is no study that would conclusively show a positive correlation between transparency and decrease in liquidity.

On the other hand, we fully agree with the contention that the difficulty in obtaining pre-trade information – of standardised quality and reliability – will create problems for the intermediaries in their meeting of the best execution requirements under MiFID.

Q3: To what extent do you think retail investor protection considerations would justify mandating pre- or post-trade transparency ?

It is not by chance that those that have uninhibited access to trading information - professional traders and counterparties - are *price makers* while others – mere *price takers*.

We believe that the concept of "informed investment" is an aspect of investor protection and that the pre- and post trade transparency is its important element in that it affects the price formation process, next to the public disclosure mandated by the Prospectus Directive and the Transparency Directive.

If one wants to take the protection of retail and unsophisticated investor protection seriously it cannot deny them the opportunity to have a reference point against which to judge the performance – both of the security and of one's intermediary.

We agree that Investor Education is another important factor in investor protection. Yet, it is not a substitution for but a supplement to the pre- and post-trade transparency.

Q4: To what extent do you think that the introduction of the new best execution requirements will result in a change in the level of transparency information provided on a voluntary basis by the industry ?

Whether or not the new best execution requirements will result in a change in the level of transparency provided on a voluntary basis by the industry – and so in the absence of regulatory requirements to be enforced by competent authorities – depends solely on the sophistication of the clients and on their contractual power vis-à-vis intermediaries.

Thus, the contention that the MiFID will lead to a better transparency regime begs the question that is at the centre of the current debate: whether or not one needs to add to the MiFID regulatory requirements so as to arrive at the commendable end of investor protection.

In a way, this question has been already answered by the European legislator: in case of equity instruments the answer was in the negative. Why should one assume that the voluntary transparency will fare better in case of non-equities that it could have done in case of equities?

Q5: How would you propose retail investor education be improved and delivered ?

Without pretending to educate investors, we seek to give the retail investors using our website the basic tools to understand the main characteristics and risks of the financial instruments traded on our markets. Thus we posted on the website a Guide to Reading a Term Sheet. A Term Sheet (*Scheda Prodotto*) is a concise, non-technical and standardised qualitative and quantitative description of a debt financial instrument. We provide it free of charge for all debt securities traded on our markets.

We believe that transparency and investor education are complementary measures, in that educating investors without giving them enough information to take an "informed decision" is a waste of time and money.

¹ M. Laganà, M. Peřina , I. von Köppen-Mertes, A. Persaud, *Implications for Liquidity from Innovation and Transparency in the European Corporate Bond Market*, ECB Occasional Paper Series, No. 50/August 2006, at 8, 10,11



Moreover both these factors are very important in building investors' confidence and, as already said with regard to transparency, they could raise the level of direct participation of retail investors in the non-equity markets.

Q6: To what extent do you agree with the suggestion that the defaults that have affected retail investors in recent years have been the result of factors other than transparency ? If you feel that transparency levels were of significance in these losses, please explain below.

Please see our answer under Q1.

We would like to underline that although the defaults which have affected retail investors in recent years have been the result of many different factors, we cannot diminish the relevance of the lack of trading transparency in such cases and underestimate the extent of its negative effects on the investors' confidence.

Q7: To what extent do you agree with the CESR's assessment that any transparency requirements could viably be segmented ?

We support any initiative likely to improve the current transparency regime for the non-equity instruments, even if directed at some classes of instruments or a group of investors only.

We believe that a system modelled on the MiFID equity trade transparency would be a viable solution in that it addresses the main problem and avoids introducing still greater complexity and opacity of the regulation (or self-regulation).

Q8: Do you agree that we have captured the most important criteria that the Commission should take into account in judging the possible self-regulatory initiatives? If you think there are other factors that should be noted, please provide details.

We believe the main criterion to be the capacity of the industry-led solution to provide standardised and reliable trading information, by all market participants concerned.

Just to conclude we would like to mention one topic which has not been specifically addressed by CESR's questions and which regards the difference in the price formation process of equity and of non-equity instruments.

We disagree with the contention that the difference in the price formation process renders the trading transparency of no value with regard to the non-equity instruments.

We believe that the transparency of the interaction of the demand and supply sides in the market for non-equity instruments contributes to the efficiency of the price formation process, despite the fact that the price of such instruments is mainly determined on mathematical basis.

Moreover, trading transparency provides a useful benchmark against which to check the value of a security, attributed to it by others, and thus it is a measure of protection against corporate fraud.

In our view, in the specific MiFID context, trading transparency is a pre-condition to any effective best execution regime. On the one hand, it is a tool for intermediaries, on the other – a reference point for investors against which to evaluate the best execution offered by the intermediary.

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