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CESR CONSULTATION ON TRANSPARENCY OF CORPORATE BOND, STRUCTURED FINANCE PRODUCT AND CREDIT DERIVATIVE MARKETS

Reply of NASDAQ OMX

In view of the current financial crisis and the need to restore as soon as possible market confidence and stability in financial markets, CESR is right to re-open the issue of the transparency prevailing in the corporate bond, structured finance product and credit derivative markets with a view to draw conclusions on desirable policy actions in this respect.

In this contribution NASDAQ OMX will not reply to each and every question asked by CESR as we feel that many of them are not addressed to us. Instead, we will offer more general opinions on what we believe are the core issues.

NASDAQ OMX is of the view that greater post-trade transparency would be beneficial to restore liquidity in the corporate bond market.

In particular, we believe that more post-trade transparency will improve market quality. Liquidity can be enhanced by introducing price transparency because it leads to greater willingness to trade. One should however note that depending on the bonds and strategies there maybe more or less motivation to trade frequently specific bonds. In addition, the availability of more price data will allow diminishing asymmetry of information and has the potential to reduce spreads.

It should also reassure investors that, due to the crisis, are now more often questioning prices offered to them by the sell-side as well as the way internal conflict of interests are managed. Post-trade transparency is also essential to ensure that best execution has been met. Best execution being a central part of the MiFID regime and protection of investors, it is key that such concept undoubtedly works in order to restore market confidence. How can any investor or regulator carry out checks on whether or not best execution has been delivered, if there is no reliable source of post-trade information? It has to be noted that retail investors are active in the corporate bond markets (in certain EU Member State quite heavily) which makes it even more important to ensure that transparency acts as a protection for them. Moreover, the crisis and the huge losses incurred by professional investors has made less convincing arguments based on the fact that professional investors do not need transparency as such investors would be sufficiently aware or able to get the information by their own means. The financial crisis has given ample examples that this hypothesis is not a reliable one.

In addition, the lack of price to properly valuate products has been one important cause of the current crisis. The clarity that post-trade information brings on prices, especially when such post-trade information is made public close to real time, greatly facilitates the proper valuation of products. However, we definitely recognise that not all trades should be submitted to immediate post-trade transparency. Like for equity, an appropriate regime should be setup for large transactions and customised products. We also underline that a specific regime will have to be designed for corporate bonds as the current MiFID regime for equity may not be entirely suitable. With the exception of large trades, it appears to us that post-trade transparency is likely to reinforce liquidity, as mentioned above. Cases where firms would commit capital relate to large orders/transactions for which a specific regime would have to be put in place reducing the likeliness of potential adverse effect on liquidity.

There is a variety of situations in the markets where we operate. For instance, since many years the transparency in the Danish bond market has been very high compared to other European bond markets. This is probably closely related to the fact that "retail investors" are very active in such market. This is especially true for the mortgage bonds market – which is by far the biggest bond market segment in Denmark. The size of this market is approximately 2.4 Trillion Danish Kroner. Danish housing finance is to a large extent managed by the Mortgage Banks and the cost of borrowing directly related to the price of bonds issued to fund these loans. The Danish borrowers and the mortgage banks have historically used the official prices from the Danish Exchange as the benchmark or more precisely as the prices of the individual loans. In that way both the mortgage banks and the borrowers are interested in a high level of transparency. Since the beginning of electronic trading in the late 1980's members as well as investors have had access to post trade information on a real-time basis.

Today everyone has access to real-time information of bond prices via vendors or even via NASDAQ OMX WEB. It is also worth mentioning information on almost every trade done in the Danish bond market is available – at least in the mortgage bond market. Only very big trades (100 MDKK or more) are not published in real-time. When MiFID was implemented the Danish Authorities decided that every trade in bonds (except for Government bonds) should be published no later than three (3) minutes after the time of agreement. This was only a small change compared to the former publication rules – as since the mid 1990's all financial firms were required to publish all trades in bonds within 5 minutes via the Danish Stock Exchange information system. When new rules were to be introduced in Denmark as a consequence of MiFID, all stakeholders (including dealers and issuers) agreed that there should continue to be a high level of transparency. This agreement on the post trade transparency requirements is the primary reason allowing retail investors to have access to information about market prices. At the same time, it seems that publishing this information is not restricting dealers from taking risk due to the possibility to delay dissemination of large trades.

The Swedish and Finnish markets do not have this kind of transparency but we support a move towards more post-trade transparency for the reasons explained above.

We further believe that it would be relevant for the regulators to impose rules regarding post-trade transparency in the corporate bond market. Transparency rules should be applicable to both listed and un-listed bond securities in order to avoid that such requirements play as a disincentive to the listing of bonds, which would have the adverse effect of making such markets less transparent than at present. A market driven solution has been advocated for a long time and has not yet emerged. We therefore consider that it is now time to regulate. In particular, since corporations have increased needs in accessing capital quickly as a result of the financial crisis, it is important to put in place a sound market place.

In this respect, we think that it would be useful to introduce in Europe a bond price reporting system similar to the TRACE system implemented in the US. The TRACE system offers a powerful reporting tool capable of providing nearly immediate trade reports for a broad range of bonds. One of the main benefits of the TRACE price reporting system is that quality data is more broadly available for market participants to employ in models that help determine estimated prices for instruments that trade infrequently.

With regard to structured finance products and credit derivative markets, we also support post-trade transparency and reporting obligations as a way to ensure more awareness of risks and where those risks lie. In those markets as well, transparency should have a beneficial effect on confidence, liquidity and overall market quality with the exception of the highly customised products.

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