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Gerben Everts

Former Member of the Executive Board, Dutch Authority for the Financial Markets (AFM)

Equity and non-equity transparency: the final pieces of the puzzle

In July 2020, ESMA published its final report on the MiFID II review for equity transparency. For non-equity transparency, the final report will be published in September. In this article, I'd like to describe a few of the current problems with equity and non-equity transparency. The measures proposed by ESMA may alleviate to some extent the observed problems with MiFID II transparency.

In the area of equity transparency, the AFM observes the complexity of the waiver structure, increasing market fragmentation due to increasing competition of systematic internalisers (SIs), issues with post-trade data quality and the lack of a consolidated tape.

Waivers for pre-trade transparency can be useful to bring transactions on venue, in particular the Large-in-Scale waiver (LIS). However, the waiver structure is complex yet not easy to improve. The double volume cap (DVC) has very few supporters. It appears over-engineered and not achieving its purpose. We support simplifying the DVC by eliminating the 4% threshold at the level of individual trading venues.

Trading has become more fragmented across venues, with SIs taking a larger part of the volumes. We support policy measures that will further align the level playing field between trading venues and SIs.

We view a real-time post-trade Consolidated Tape Provider (CTP) as important for enhancing transparency and we see the CTP an essential part of promoting the CMU and its necessary acceleration as proposed by the European Commission. It will enable aggregated information from increasingly fragmented markets. While we support the establishment of CTP, we also note some practical constraints which should temper expectations.

MiFID II has not yet delivered on its goals in the non-equity markets and can still be considered work in progress. In our analysis MiFID II's focus on transparency based on liquidity has proven to be counterproductive given the lack of liquidity in the fixed income markets where many instruments are tailor-made and not designed with the intention to be traded on a secondary market.

Market participants argue that MiFID II has merely sought to replicate equity market conventions onto so-called "non-equity" segments and that enforcing transparency on such markets is counterproductive. Instead, it can be argued that sufficiently liquid fixed income markets with sustainable higher levels of transparency can only be achieved by incentivizing standardization of instruments and addressing primary market fundamentals.

Overall, there is still broad support for the original G20 goals of migrating fixed income markets and derivatives towards more transparent and open markets. At this stage, MiFID II can be considered unfinished business and requires action from regulatory authorities to ensure it reaches its goals. Besides the goal for addressing market fundamentals through creating incentives for more standardization, we support improving the level playing field between bilateral and transparent multilateral forms of trading by creating more regulatory certainty. In addition, the right conditions for meaningful transparency can be achieved by focusing on improving data quality through an enhanced focus on liquid instruments, as well as the introduction of a post-trade consolidated tape. ●