



September 14, 2006

Call for evidence - Pre- and post-trade transparency provisions of the Markets in Financial Instruments Directive (MiFID) in relation to transactions in classes of financial instruments other than shares.

TLX S.p.A. manages a regulated market (TLX) and a MTF (EuroTLX), both dedicated to non professional investors. TLX S.p.A. has standardized the level of transparency of the two systems. This implies that the set of information the company supplies to investors is higher than the one required by the applicable Italian law, especially for what concerns the ATS.

Based on the information derived from a comparison between the different Italian trading systems, it may be argued that the level of transparency chosen by not-regulated markets is flattened on the *minimum requirements* imposed by law. For this reason, the EuroTLX case could be interesting in assessing the positive effects of market transparency in secondary markets for non professional investors.

TLX S.p.A. position overview

We experienced a higher level of market transparency than that required for ATS. Such experience leads us to support the extension of the MiFID transparency regime to other classes of financial securities. We can affirm that pre and post trade transparency have a positive impact on price formation in the secondary cash bonds markets where retail investors can operate. This is due to the reduction of the asymmetry between retail investors and professional ones.

In addition to the positive effects on investor protection, we consider also the positive ones on the promotion and enforcement of the new best execution regime, which represents the most important factor that can facilitate the market integration at the European level.

Answers to the Question listed in the Report

Question 1.: Do you have any comment on the proposed scope of the Report?

We agree with the proposed approach. As highlighted above, we support the extension of the MiFID transparency regime to other classes of financial securities because of its potential and positive effects on the retail investor protection and European market integration. Pre and post trade transparency can foster the new best execution regime, facilitating its effectiveness.

In our opinion, cash bonds represent the most relevant class on which focusing and prioritize the attention because of their wide presence in retail investor portfolios.



Question 2.: Do you consider this classifications scheme to be sufficient for the purpose of the review?

We propose to introduce under “cash bonds” a further sub-class, called “financial bonds”, which are usually more complex than corporate bonds. They are issued by banks or investment firms subject to a specific oversight by financial authorities. Issuers of financial bonds have also to comply with peculiar accounting rules.

Question 3.: Do you consider there are possible policy rationales for mandatory transparency we have not listed?

Under FSAP we consider the promotion of market integration at European level an another possible item that could be treated as an independent policy rationale.

Question 4.: Do you agree with our proposals for prioritization of the review?

Yes, we agree. We consider cash bonds to be the market with more prominent potential investor protection concerns. Should “financial bonds” be added as sub-class (see our proposal under question 2), this sub-class would require a good prioritization (their ranking could be for example between “cash high-yield corporate bonds” and asset backed securities”).

Question 5.: To what extent do you consider there to be:

- a. observable or demonstrable problems with respect to the possible policy rationales for mandatory transparency identified above in relation to one or more of the instrument markets under review?**
- b. evidence that mandatory pre- or post-trade transparency would solve any of those problems?**

From our experience we can affirm that pre and post trade transparency have a positive impact on price formation in the secondary cash bonds markets where retail investors can operate. This is due to the reduction of the asymmetry between retail investors and professional ones. Retail investors do not generally have the competences, the instruments and the access to information which are necessary to determine the price (*price takers*) as well as the professional markets (*price makers*). In this context, the higher level of price transparency can reduce the information gap. For details please refer to our response to the IOSCO consultation on transparency of corporate bond market (IOSCO Report of May 2004), here attached.

Question 6.: To what extent could recent and upcoming technological and market developments in relation to the instrument markets under review:

- a. contribute to a relatively inexpensive extension of mandatory transparency?**
- b. render mandatory transparency unnecessary?**

Question 7.: To what extent are non-equity financial instruments different from equities so that lower levels of mandatory transparency in those markets may be justified?



Question 8.: What data sources do you consider relevant to the issues you have raised (if appropriate, cross-refer to your answers below)? Would you or your organisation be prepared to provide any relevant data if necessary?

As highlighted above we support a mandatory transparency regime.

Question 9.: Are there academic or institutional papers or ongoing work that should be considered in preparing the Report not included in our bibliography?

We do not have suggestion to widen your bibliography.

Question 10.: What conclusions do you draw from the existing academic debate and the work being conducted by other interested parties?

Our opinion is mainly based on our direct experience that lead us to privilege and consider more reliable analysis that confirm the positive effects of a higher level of market transparency, especially when retail investors can operate.

Question 11.: In your view, how applicable is the academic or institutional literature concerning transparency in the cash equities markets to the present discussion?

Price formation in bond markets has much higher scientific basis than what can be observed on equity markets. In particular, the limited number of factors which influence the fair value of a corporate bond (interest rate, credit risk, etc.) allows to determinate the security value on the basis of mathematical algorithm. This procedure is not always effective if applied on the equity market and in any case it is usually not appropriate for the *spot* valuation of securities quotations.

The different price formation methodology and the easier determination of bond value accentuates information asymmetry among market participants: when the level of competence, the resources and the access to a plurality of information are increasing, professional investors are able to determine the security price with a particularly high quality level (in other words, they are *price maker*); on the contrary, *retail* investors do not generally have the competences, the instruments and the access to information which are necessary to determine the price (*price taker*). In this framework, pre and post trade transparency contributes to the reduction of asymmetry among market participants.

When consulting literature on concerning transparency in the cash equities, the impact of the factors mentioned above should be considered. However, we think that there are no reasons to believe that the bond market for *retail* investors is very different from the equity market.

Question 12.: What similarities, and what differences, are there between US and EU markets that should be borne in mind when seeking to draw inferences from the TRACE11 experience in the US?

Basically, it should be considered that at the European level the main goal of a full market integration has not been reached. Market transparency can lead to a more effective best execution regime, which represents the most important factor to foster market integration.



Question 13.: To the extent that you have identified problems or believe that others might do so, do you agree that only EU-level action would be appropriate in the present case?

We agree.

Question 14.: If you have identified problems or believe that others might do so, to what extent do you consider those problems would disappear as a natural product of market evolution in the short-to-medium term?

The best execution regime asks for a higher level of market transparency than those set by MiFID, even in relation to cash equities. It is likely that the enforcement of the best execution regime can lead to this level of market transparency but such event remains uncertain. A mandatory regime can avoid failures and delays. The consideration of the importance of the market integration should lead to favour a mandatory regime.

Question 15.: In respect of both pre- and post-trade transparency, are the four options the right ones to consider, and in particular should other options be considered?

They are the right ones even if we do not believe that a TRACE-like system can be effective at least for enhancing pre trade transparency. This is due to the delay that characterizes such an information collection.

Question 16.: Would you, in light of your answers to the other questions, favour any of the four options in relation to pre- and post-trade transparency (or another option you might propose for consideration) in respect of transactions in any of:

cash government bonds;

cash investment-grade corporate bonds;

cash high-yield corporate bonds;

asset-backed securities;

credit default swaps, interest rate swaps and bond futures; or

any other financial instrument you consider relevant?

We support a MiFID-like system.