Vision for the future of EU wholesale financial markets:

AFME recommendations on the MiFIR review

Association for Financial Markets in Europe
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Vision for the future of EU wholesale financial markets

Over the recent period of geo-political instability and global pandemic, EU capital markets continued to intermediate liquidity and facilitate risk management for corporates and investors.

Open, competitive, and efficient market and banking systems proved their resilience and purpose, helping corporates raise record levels of financing and investors reallocate portfolios and investments at a time of heightened volatility.

EU capital markets, however, remain fragmented along national lines despite years of pro-integration initiatives. EU markets do not yet reflect the size of the EU economy, and, crucially, are underpowered in the support that they could otherwise provide for the EU economic growth.

Having EU equity and fixed income wholesale market eco-systems that work for investors, corporates and other users of capital markets would significantly help the European economic recovery, investments and growth. We set out below recommendations for the MiFIR review that would help achieve those objectives on equity and fixed income markets.

Executive Summary and Key Recommendations

I. Healthy wholesale financial market ecosystems are key to complete CMU

- Well-functioning, diverse and competitive secondary market eco-systems provide deep pools of liquidity for investors and issuers, and reduce cost of primary funding for corporates.

- Primary and secondary market eco-systems are mutually dependent. Diverse and liquid secondary markets determine asset valuations (liquidity *premia*), which in turn influence issuance in the primary market. Likewise, an active primary market is necessary to encourage the trading of a diverse range of assets to satisfy investor demands for instruments with differing risk profiles.

- The MIFIR review should therefore focus on unlocking the full potential of European capital markets by making them more innovative, competitive and attractive for corporates and investors globally.

II. The MiFIR review could negatively impact existing liquidity pools

- An open and competitive marketplace is key to ensuring more efficient European capital markets. Banks, trading venues and other financial service providers all play a critical role in such an ecosystem. Banks, acting as market markers, play an essential role in "making markets" where liquidity is difficult to find.

- Banks' risk intermediation function, where they deploy their balance sheet to provide liquidity is the only trading mechanism that can provide execution against risk capital. This increases execution options for investors, who are therefore able to trade even where there are no natural buyers or sellers, as banks can take the other side of an investor trade and manage the ensuing risk on their books. This increases liquidity, dampens volatility and allows investors on European markets to manage their own exposures better. It is therefore vital that this function is preserved as part of the EU's market eco-system.

- AFME believes that an appropriately calibrated transparency regime is beneficial for markets. It is crucial that the calibrations are carefully considered. If untested limitations are imposed on banks' ability to provide liquidity across equity and fixed income markets, the overall attractiveness of European markets in the global context could be negatively impacted. The services provided by committed liquidity providers need to be preserved to ensure that the EU's markets continue to provide adequate levels of liquidity and meet the needs of all investors.

- For equity markets, the proposals to impose additional transparency obligations on banks providing liquidity to their clients or to curtail banks' ability to trade on a bilateral basis at different price points, including at mid-point between the best bid and offer price, will damage the diversity and competition in European equity markets.

AFME Recommendations to ensure liquidity is not negatively affected

For ***equity markets***, AFME recommends that:

- The systematic internaliser quoting obligation is increased tenfold from 10% of the standard market size to 100% of the standard market size, provided the calculation of standard market size is not changed;
- The proposed limitations imposed on trading at mid-point of the best bid and offer price should be removed for both systematic internalisers and trading venues, which would align EU markets with the globally accepted *fair execution price* standard.

For ***bond markets***, AFME recommends that:

- All retail size corporate bond transactions (i.e. transactions below 500,000 thousand euros or equivalent) are made near-real time transparent (i.e. within 15 minutes from their conclusion), which would represent around 70% of all trades[1];

[1] According to AFME analysis "MiFIR 2021 Corporate Bond Trade Data Analysis and Risk Offset Impact Quantification", in cooperation with Finbourne Technologies. A similar data analysis and risk offset impact quantification for sovereign bonds will also be undertaken by AFME.

- The future deferral regime for bonds goes beyond the Commission proposal that currently limits the price deferral to a maximum of end of day, and the volume deferral to a maximum of 2 weeks, and includes a defined number of price and volume deferral periods, ranging from 15 minutes to end of the day, 1, 2 and 4 weeks, 3 months and indefinite;
- The remaining elements of the deferral regime, including the detailed price and volume of transactions deferral calibration, are not hardwired into legislation;
- Instead, ESMA should be mandated to calibrate which asset classes and transaction sizes should be placed into the different deferral categories from both a price and volume standpoint, and that such detailed quantitative analysis is conducted using accurate and complete data, sourced from the projected consolidated tape for bonds;
- The price and volume deferral categories and thresholds evolve overtime toward increased or decreased transparency, where the evidence supports such evolution;
- The current MiFIR liquidity and transparency framework should remain in place until this detailed quantitative analysis and calibration is undertaken by ESMA;
- The "size specific to the instrument" ("SSTI") waiver that helps protect liquidity providers from undue risk is retained or, failing that, the large in scale waiver threshold is commensurately lowered;
- The pre-trade transparency regime for bond markets is revisited, and, failing to demonstrate its effectiveness for users of bond markets, is recalibrated by limiting the scope of the regime to systems such as electronic order books and periodic auctions (but not to voice trading or request for quote systems).

III. The consolidated tape creates a common view of EU markets

- EU capital markets remain fragmented along national lines despite years of pro-integration initiatives. This disadvantages both investors and issuers, and reduces the appeal of EU capital markets as a whole. The establishment of a consolidated tape for equities and bonds would help *de facto* integrate EU markets, reduce home biases in investments and attract international capital to the EU.

- The consolidated tape for equities and bonds can be one of the most powerful tools to increase retail investors participation in EU capital markets by allowing all investors to have access to the information about all shares and bonds traded in the EU. An appropriately constructed consolidated tape will also help improve the quality of market data, reduce its costs and decrease the complexity relating to market data licences.

AFME Recommendations for the consolidated tape[2]

While it is important to note that separate consolidated tapes for equities and bonds will be required to reflect the different market structures of these asset classes, AFME believes the following recommendations are vital to ensuring that the consolidated delivers on its objectives.

AFME recommends that:

- A single independent consolidator for each asset class (i.e. shares and bonds) is appointed;
- Mandatory contribution from all venues to the tape is required;
- The consolidated tape is offered at fair and appropriate price levels for professional and non-professional users respectively to ensure that is commercially successful;
- The consolidated tape is sold with a simple, single market data licensing framework covering a variety of use cases;
- Data quality is addressed alongside the development of the consolidated tape;
- Industry stakeholders are involved in the process of improving the quality of market data, including by actively participating in the EU Commission expert stakeholder group to advice on data quality;
- The EU Commission expert stakeholder group should advise on the quality and the substance of market data, on the common interpretation of market data and on the quality of the transmission protocols and should be set up as soon as practicable;
- There is no mandatory consumption of the consolidated tape.

[2] These recommendations only cover the consolidated tape for equities and for bonds. AFME has not considered recommendations for a possible consolidated tape for derivatives or for exchange traded funds.

For ***equity markets***, AFME recommends that[3]:

- The consolidate tape should be continuous, covering the full trading day, and as close to real-time as possible;
- The consolidated tape covers post trade and pre-trade information, showing investors prices from executed transactions as well as which prices are available for trading;
- The contributions to an equities pre-trade consolidated tape are made mandatory or, as a first step, voluntary before made mandatory in the short to medium term;
- The consolidated tape revenue sharing arrangement must fairly recognise the contribution to price formation from all different contributors (not just regulated markets);
- The consolidated tape revenue sharing arrangement should not be used as the main criteria to appoint the consolidated tape provider.

For ***fixed income markets***, AFME recommends that:

- The consolidated tape only covers post trade information throughout the trading day, showing investors prices from executed transactions;
- The post-trade consolidated tape ensures committed liquidity providers are not exposed to undue risk, especially when trading in illiquid instruments or transactions above a certain size, given that there are relatively long timeframes to unwind or hedge the trade in such instances;
- The consolidated tape does not publish post-trade details until after the deferral period has expired;
- An appropriately constructed bond consolidated tape provides actual, detailed trade data so that ESMA can properly calibrate which instruments belong to the various deferral periods recommended.

IV. Competition and choice provide better outcomes for investors

- Diversity in trading choices supports better, and more sustainable outcomes for end-users, at a more effective cost, and is a feature of a mature market structure. This is valid for both equity and fixed income markets. The MiFIR review should not limit investors' ability to choose the type of execution mechanism that is most suitable for their specific investment needs.

- AFME believes that continuing to have a framework that allows for different execution models and a strong and calibrated transparency regime is the best way to incentivise robust and fair price formation.

- AFME is very supportive of a price formation process for equity markets that is sound and robust and that incorporates price indications from different execution mechanisms that serve different investor needs. AFME does not believe that enforcing increased trading on incumbent stock exchanges would necessarily improve price formation and, conversely, there is evidence that it would impact the ability for firms to provide best execution for their underlying clients.

AFME Recommendation to improve outcomes for investors

AFME recommends that:

- The double volume cap is removed all together (i.e. both caps, including the single cap proposed by the EU Commission) to ensure that EU equity markets are aligned with the most competitive equity markets globally;
- The EU Commission is mandated to, upon ESMA's advice, restrict the use of the reference price and negotiated trade waivers only if there is evidence that the volume of such trading is undermining the efficiency of the price formation process;
- ESMA is mandated to ensure that the price formation process remains sound and robust by monitoring the level of trading executed under the reference price and negotiated traded waivers;
- The limitation to use the reference price waiver only to transaction above a certain size (above 200% of the standard market size) is not adopted;

[3] For a full detailed set of recommendations and principles that should inform the consolidated tape for equities: "A Cross-Industry Consensus on the EU Equity Consolidated Tape Proposal-Statement of Principles", May 2022, AFME, BVI, Cboe and EFAMA

- The use of the reference price waiver is allowed by reference to the price provided by the consolidated tape or by venues other than the most relevant market, which would help increase the resilience of EU equity markets.

V. The importance of an evidence-based policy making process

- Financial markets policy should be data-driven and based on evidence provided by robust data analysis. New market policies should demonstrate the benefits for end investors, issuers and other participants and be subject to robust impact assessment analysis.

- The EU Commission produced a very thorough impact assessment on why no consolidated tape provider has come forward after MiFID 2 was implemented and on the various options to finally facilitate the emergence of a consolidated tape provider. However, none of the other proposals put forward by the EU Commission were subject to any impact assessment.

- Given the quality and availability of the existing data requires further refinement and clarity, we believe that any material adjustment to the existing transparency and market structure framework for equity and fixed income markets should be assessed only after a thorough data enhancement exercise is undertaken. This would help ensure that EU policy makers can properly calibrate their policy measures at the right time.

AFME Recommendation for an evidence-based policy making process

AFME recommends that:

- The quality of data should be improved before any material adjustment to the existing transparency and market structure framework for equity and fixed income markets is undertaken;
- The proposed adjustments by the EU Commission to key equity and fixed income market structure provisions identified above should not be adopted but instead should be revisited at a later stage once there is enough evidence to be assessed.

VI. Delivering fair and proportionate regulation

- Delivering fair and proportionate regulation to market participants and investors is key to ensure that market participants can develop their activities seamlessly without unnecessary costs.

- AFME supports the removal of any obligations or requirements imposed on market participants where the desired policy objective can be achieved through a less onerous framework. Similarly, modifications to MiFIR should ensure that regulatory concepts and frameworks are still fit for purpose and effective.

AFME Recommendation for a fair and more proportionate regulatory framework

AFME recommends that:

- The best execution reporting requirements that do not benefit users of equity and fixed income markets are removed;
- The requirement for systematic internalisers always report a transaction undertaken with clients that are not systematic internalisers is removed. Alternatively, banks and investment firms that want to elect to become designated reporters for their clients should be able to do it;
- Other features that are unique to the EU and have not proven to be beneficial to investors are reviewed and possibly removed.

Healthy wholesale financial markets are key for the completion of CMU

Well-functioning, diverse and competitive secondary market eco-systems provide deep pools of liquidity for investors and issuers, and reduce cost of primary funding for corporates.

Virtuous cycle between primary and secondary markets

The link between primary markets, where corporates raise financing, and secondary markets, where securities are traded across a diverse set of execution venues, is critical. While primary markets channel investor cash to issuers, a healthy secondary trading environment encourages investments into those issuances and, as a consequence, has a direct impact on the ability of institutions to raise capital cost efficiently.

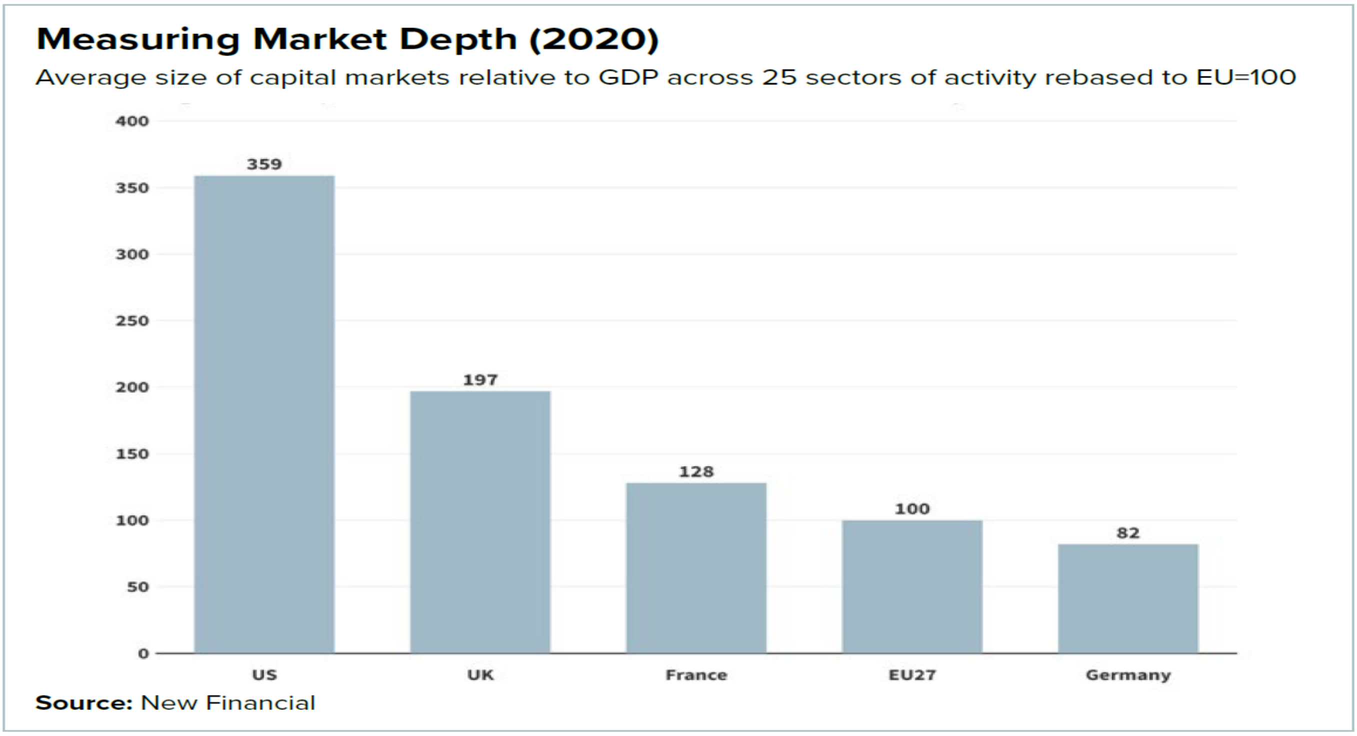
A diverse secondary markets eco-system is as important for primary market debt financing as it is for equity financing through initial or follow-on equity public offerings. Without a vibrant secondary market landscape it is much harder for issuers to place new debt in the primary market or for corporates willing to undertake an initial public offering to execute on their plans while achieving the best valuations for the placement of their shares.

Primary and secondary market eco-systems are therefore mutually dependent. Diverse and liquid secondary market eco-systems determine asset valuations (liquidity *premia*), which in turn influence issuance in the primary market. Likewise, an active primary market is necessary to encourage the trading of a diverse range of assets to satisfy investor demands for instruments with differing risk profiles.

For these reasons, the review of MIFIR should aim to unlock the full potential of European capital markets by making them more innovative, competitive and attractive for corporates and investors globally.

Considering that EU companies continue to avail themselves of other more competitive capital markets to finance their investment needs, AFME advocates that the MiFIR review should remove the provisions it contains that enable the continued entrenchment of dominant positions of incumbent, less innovative market participants and instead that it focusses on promoting more competitive markets to achieve better outcomes for corporates and investors.

This is also paramount for fostering EU's financial system's openness, strength and resilience after the UK withdrawal from the European Union and to ensure that EU markets reflect the size of its economy.



Bond Markets

EU bond markets are already reasonably competitive globally and have the potential for future efficiencies and growth. However, at the moment, growth is constrained by a combination of regulatory fragmentation, the high cost of fixed income market data and poor trade reporting efficiency and effectiveness.

At issuance level, corporates can determine the law applicable to the bond at their will. Issuers can also finance their needs in different currencies, depending on their financial flows. When seeking an admission to trading on an EU regulated market, issuers can also seek approval of their prospectus from the Competent Authority of their choice and typically admit the bonds to trading in a very efficient way.

At trading level, bonds issued by EU corporate or sovereign issuers are traded and reported in the EU across different execution venues such as regulated markets, multilateral trading facilities and systematic internalisers. This remains valid even when the bond is issued in a non-EU currency (i.e. when the bond is issued in USD or JPY). EU bond markets continue to be very attractive to foreign issuers when they finance their funding needs in Euros or in other currencies[4]. Also, investors continue to have a good choice between types of trading venues that better cater for their investment needs.

The cross-border, pan-European nature of EU debt capital market continues to bring together borrowers and investors from all over the world, helping countries, supranational organisations, financial institutions and companies meet their funding needs.

The EU should preserve key features of its healthy bond market and ensure that any future adjustments are based on detailed evidence and analysis. Considering the benefits of a healthy bond market, any improvements should also be progressively implemented and subject to careful analysis by measuring the impact on market liquidity, particularly for less liquid instruments and for large transactions .

Equity Markets

The size of EU equity markets does not compare favourably against other global capital markets, and it fails to accurately represent the size and breadth of the EU economy.

EU corporates continue to seek their initial public offerings ("IPOs") outside the EU where disclosure, accounting and reporting obligations are significantly more demanding and costly than the existing EU requirements[5]. Even when admitted to trading in EU markets, EU corporates tend to also pursue an additional listing on a foreign market to access bigger pools of investors and liquidity.

EU companies IPOs in third countries

Although the number of cross-border listings within the EU have been decreasing, the number of EU companies seeking to list outside the EU has been on the rise. Since 2010, there have been 40 Initial Public Offerings ("IPOs") of EU-27 companies in the USA compared to only one US firm conducting an IPO on an EU-27 exchange. In the same period, 110 EU companies sought their IPO in the UK.

There have also been some highly publicised examples of EU-27 companies seeking direct listings on US exchanges in recent years, including some of the most innovative and globally successful EU corporations.

In 2015, Ferrari completely its IPO on the NYSE. Spotify listed on the NYSE through a direct listing in 2018. The US market is also very attractive to EU biotechnology companies. In October 2019, BioNTech successfully completed its IPO in the US, and it is now one of the biggest German listed companies by market capitalisation. Another German biotechnology company, CureVac, launched its IPO in the US in August 2020 despite German State (KfW) 300m investment and ownership of 23% of the company and the massive EIB investments in its development.

Overall, more than 100 EU companies are primary or dual-listed in the US. Amongst the reasons to pursue a listing in the US, issuers declare that access to capital and access to specialised and knowledgeable investors is particularly important.

[4] A case in point is the number of bonds issued by foreign issuers subject to the EU MiFIR transparency framework.
[5] "Primary and secondary equity markets in the EU – Final report", Oxera Consulting LLP, November 2020

Also negatively impacting the attractiveness of EU equity markets is the fact that the liquidity landscape is highly concentrated on trading venues[6], and remains predominately fragmented across national lines. The EU equity market structure and transparency regime is disproportionately complex and protective of incumbent national stock exchanges, and it does not resemble other sophisticated equity markets globally.

The EU framework for the listing, trading, clearing and settlement of equities is intricate and difficult to navigate for regional and global investors alike. This complex regulatory and operational structure is unique to the EU, hampers global investors access to EU markets, and impacts issuers and investors decisions to become listed and to invest.

The development of a pan-European ecosystem of market infrastructures supporting secondary equity markets should be pursued and materially improved by promoting open access and interoperability links between equity CCPs, or facilitating cross-border mergers at the market infrastructure level[7].

The MiFIR review could negatively impact existing liquidity pools

An open and competitive marketplace is key to ensuring more efficient European capital markets. Banks, trading venues and other financial service providers all play a critical role in such an ecosystem.

The role of banks in providing liquidity to secondary markets

Banks, acting as market markers, play an essential role in "making markets" where liquidity is difficult to find.

A ***market maker, also legally defined as a "systematic internalise", is a committed liquidity provider*** that dedicates its balance sheet to providing continued pricing and immediacy of execution to its investors' clients throughout the day. This function of banks means that investors are able to buy or sell when they need, even when the other side of the trade is not immediately available, which is normally the case for certain transaction sizes and instruments. The availability of quotes from market makers ready to step in to fill this gap is therefore particularly important.

By performing this function, ***banks also act as a "shock absorber"*** by limiting detrimental price impacts on clients entering or exiting large investment positions, which otherwise would be significant if those investors were to execute their investment decisions through other execution mechanisms.

This "shock absorber" function ultimately benefits end investors, such as pensioners and savers who entrust their money to pension funds and asset managers, by ensuring that the managers of their pension pots and savings obtain the best possible results on their investment decision.

Banks' role in capital markets is fundamentally different from trading venues as banks utilise their own capital to trade with their clients and in doing so provide a bespoke facilitation role. By comparison, trading venues do not facilitate trades by placing their balance sheets at risk. Instead they simply bring buyers and sellers together by providing a matching mechanism.

Banks' risk intermediated function, where banks deploy their balance sheet to provide liquidity, and manage the ensuing risks, is the only trading mechanism that provides execution against risk capital. It is not substitutable and should continue to form part of an efficient, global competitive EU's market eco-system.

The MiFIR review could negatively impact this fundamental role, and the existing liquidity pools, if proposals that are designed to limit the ability of banks to perform their non-substitutable risk intermediated function of providing liquidity to investors across equity and fixed income markets were accepted.

[6] According to Oxera report "Understanding the Liquidity Landscape in European Equities Markets" for the first six months of 2020, 81% of addressable liquidity was executed on-venue, 13% on systematic internalisers and 6% over the counter (OTC).
[7] Along similar lines, Oxera on "Primary and secondary equity markets in the EU – Final report", Oxera Consulting LLP, November 2020

For **equity markets**[8], the EU Commission's MiFIR proposals to impose additional transparency obligations on banks providing liquidity to their clients (i.e. by increasing the systematic internaliser quoting obligations) or to curtail banks' ability to trade on a bilateral basis at different price points, including at mid-point between the best bid and offer price (i.e. by further limiting trading at mid-point), will damage the diversity and competition in European equity markets.

Extending liquidity providers' quoting obligations by a twentyfold increase, from 10% of the standard market size, to 200% of the standard market size, without having undertaken any meaningful impact assessment and disregarding industry and ESMA's recommendations, would put the liquidity provider at undue risk and would reduce the level of liquidity it can provide to its investor clients.

Similarly, curtailing the ability of the liquidity provider to execute a trade at the mid-point between the best bid and offer price would further limiting the ability of banks to serve their investor clients at the best possible price, and to provide the level of service normally available.

For **bond markets**[9] [10], the EU Commission proposals to remove a waiver that helps protect liquidity providers from undue risk (i.e. the removal of the "size specific to the instrument" waiver) would impact banks' ability to provide liquidity to less liquid markets or on large transactions.

Similarly, the EU Commission proposals to decrease the time deferral for the publication of prices of transactions by 80%, from 5 days to end of the day, and to halve the time deferral for the publication of volumes of transactions, from 4 weeks to just 2 weeks, would put committed liquidity providers at undue risk and would reduce available liquidity on corporate bond markets.

This is particular significant as these proposals were not subject to any meaningful impact assessment undertaken by the EU Commission pursuant to the EU's impact assessment guidelines, nor have they factored in the unwinding of central banks' monetary policy measures stemming from increased inflation and the unfolding of other political events prone to significantly impacting bond markets.

The services provided by committed liquidity providers need to be preserved to ensure that the EU's markets continue to provide adequate levels of liquidity and meet the needs of all investors.

AFME Recommendations to ensure liquidity is not negatively affected

For ***equity markets***, AFME recommends that:

- The systematic internaliser quoting obligation is increased tenfold from 10% of the standard market size to 100% of the standard market size, provided the calculation of standard market size is not changed;
- The proposed limitations imposed on trading at mid-point of the best bid and offer price should be removed for both systematic internalisers and trading venues, which would align EU markets with the globally accepted *fair execution price* standard.

[8] For a detailed analysis of the role of systematic internalisers in European equity markets: "The vital role of systematic internalisers (SIs) in European equities markets", AFME, February 2022.
[9] For a fixed income perspective of the role of market makers/systematic internalisers on fixed income markets, "Understanding EU Bond Market Structure and Dynamics", AFME, November, 2021
[10] For a detailed reasoning of AFME's recommendations to ensure liquidity is not negatively affected in corporate bond markets, and additional data evidence, AFME's "MiFIR 2021 Corporate Bond Trade Data Analysis and Risk Offset Impact Quantification", in cooperation with Finbourne Technologies. A similar data analysis and risk offset impact quantification for sovereign bonds will also be undertaken by AFME.

AFME Recommendations to ensure liquidity is not negatively affected

For ***bond markets***, AFME recommends that:

- All retail size corporate bond transactions (i.e. transactions below 500,000 thousand euros or equivalent) are made near-real time transparent (i.e. within 15 minutes from their conclusion), which would represent around 70% of all trades;
- The future deferral regime for bonds goes beyond the Commission proposal that currently limits the price deferral to a maximum of end of day, and the volume deferral to a maximum of 2 weeks, and includes a defined number of price and volume deferral periods, ranging from 15 minutes to end of the day, 1, 2 and 4 weeks, 3 months and indefinite;
- The remaining elements of the deferral regime, including the detailed price and volume of transactions deferral calibration, are not hardwired into legislation;
- Instead, ESMA should be mandated to calibrate which asset classes and transaction sizes should be placed into the different deferral categories from both a price and volume standpoint, and that such detailed quantitative analysis is conducted using accurate and complete data, sourced from the projected consolidated tape for bonds ;
- The price and volume deferral categories and thresholds evolve overtime toward increased or decreased transparency, where the evidence supports such evolution;
- The current MiFIR liquidity and transparency framework should remain in place until this detailed quantitative analysis and calibration is undertaken by ESMA;
- The "size specific to the instrument" ("SSTI") waiver that helps protect liquidity providers from undue risk is retained or, failing that, the large in scale waiver threshold is commensurately lowered;
- The pre-trade transparency regime for bond markets is revisited, and, failing to demonstrate its effectiveness for users of bond markets, is recalibrated by limiting the scope of the regime to systems such as electronic order books and periodic auctions (but not to voice trading or request for quote systems).

The consolidated tape creates a common view of EU markets

EU capital markets remain fragmented along national lines despite years of pro-integration initiatives. This disadvantages investors and reduces the appeal of EU capital markets as a whole.

The establishment of a consolidated tape for equities and bonds would help *de facto* integrate EU markets, reduce home biases in investments and attract international capital to the EU.

The consolidated tape would democratise access to information on how financial assets are traded by providing a comprehensive liquidity picture across the EU. This would make cross-border investments easier through the creation of a truly, virtually integrated pan-European market, which will ultimately benefit corporates raising capital and investors allocating their savings.

The creation of such integrated pan-European market will in turn contribute to the ultimate goal of increasing capital flows within the EU and defeating retail investors' existing "home bias", i.e. their tendency to hold a significant share of domestic assets in their portfolios.

The provision of an appropriately constructed consolidated tape will also facilitate and foster investors' access to EU markets with a comprehensive and standardised view of equities and fixed income trading environments. The clearer picture provided by the consolidated tape will contribute to making EU markets more competitive and attractive to all investors regardless of their resources, sophistication or origin, including to foreign investors.

Ultimately, at EU level, the consolidated tape can be one of the most powerful tools to increase retail investors participation in EU equity and fixed income markets by allowing all investors to have access to the information about all shares and bonds traded in the EU.

An appropriately constructed consolidated tape will also help improve the quality of market data, make it accessible to participants who currently are unable to consume it, and decrease the complexity relating to market data licences.

The increased awareness for a pan-European, better integrated capital market across asset classes that the consolidated tape can bring about will ultimately benefit the EU as a whole and should be considered in the context of its objective to promote EU's financial system openness, strength and resilience, better reflecting its potential in relation to the size of the single market.

The consolidated tape is also consistent with other initiatives the Commission is undertaking to improve data accessibility and sharing in the context of the CMU, such as the recent proposal to create a European Single Access Point ("ESAP") for investors to access financial and non-financial information disclosed by companies.

The recommendations below set out AFME's views and recommendations in more detail on the consolidated tape for equities[11] and for bonds[12]. AFME has not considered recommendations for a possible consolidated tape for derivatives or for exchange traded funds.

AFME Recommendations for the consolidated tape

While it is important to note that separate consolidated tapes for equities and bonds will be required to reflect the different market structures of these asset classes, AFME believes the following recommendations are vital to ensuring that the consolidated delivers on its objectives.

AFME recommends that:

- A single independent consolidator for each asset class (i.e. shares and bonds) is appointed;
- Mandatory contribution from all venues to the tape is required;
- The consolidated tape is offered at fair and appropriate price levels for professional and non-professional users respectively to ensure that is commercially successful;
- The consolidated tape is sold with a simple, single market data licensing framework covering a variety of use cases;
- Data quality is addressed alongside the development of the consolidated tape;
- Industry stakeholders are involved in the process of improving the quality of market data, including by actively participating in the EU Commission expert stakeholder group to advice on data quality;
- The EU Commission expert stakeholder group should advise on the quality and the substance of market data, on the common interpretation of market data and on the quality of the transmission protocols and should be set up as soon as practicable;
- There is no mandatory consumption of the consolidated tape.

For ***equity markets***, AFME recommends that:

- The consolidate tape should be continuous, covering the full trading day, and as close to real-time as possible;
- The consolidated tape covers post trade and pre-trade information, showing investors prices from executed transactions as well as what prices are available for trading;
- The contributions to an equities pre-trade consolidated tape are made mandatory or, as a first step, voluntary before made mandatory in the short to medium term;
- The consolidated tape revenue sharing arrangement must fairly recognise the contribution to price formation from all different contributors (not just regulated markets);
- The consolidated tape revenue sharing arrangement should not be used as the main criteria to appoint the consolidated tape provider.

[11] For a full detailed set of recommendations and principles that should inform the consolidated tape for equities: "A Cross-Industry Consensus on the EU Equity Consolidated Tape Proposal-Statement of Principles, May 2022, AFME, BVI, Cboe and EFAMA

[12] AFME also recommends that, amongst the core market data to be displayed by the consolidated tape for bonds, only the market identifier code of a trading venue is included, but not the actual identification of systematic internalisers dealing on own account. A different understanding would prevent the provision of liquidity on key fixed income markets. The actual identification of the systematic internaliser can be replaced by a generic identification as "SI".

AFME Recommendations for the consolidated tape

For ***fixed income markets***, AFME recommends that:

- The consolidated tape only covers post trade information throughout the trading day, showing investors prices from executed transactions;
- The post-trade consolidated tape ensures committed liquidity providers are not exposed to undue risk, especially when trading in illiquid instruments or transactions above a certain size, given that there are relatively long timeframes to unwind or hedge the trade in such instances;
- The consolidated tape does not publish post-trade details until after the deferral period has expired;
- An appropriately constructed bond consolidated tape provides actual, detailed trade data so that ESMA can properly calibrate which instruments belong to the various deferral periods recommended.

A new equity “concentration rule” would provide worse outcomes for investors

Diversity in trading choices supports better, and more sustainable outcomes for end-users, at a more effective cost, and is a feature of a mature market structure. This is valid for both equity and fixed income markets.

The MiFIR review should not limit investors’ ability to choose the type of execution mechanism that is most suitable for their specific investment needs.

A new equity “concentration rule”

The Commission proposals for equity markets would in practice account for the re-introduction of a *de facto* concentration rule for equity markets. which would only allow investors to trade on incumbent exchanges.

Reimposing a new "concentration rule" for equity trading in favour of incumbent stock exchanges would be against all the evidence and without any meaningful impact assessment of its potential effects, and would provide worse outcomes for investors.

That would also be detrimental to the EU’s overall objective of promoting its financial system’s openness, strength and resilience after the UK withdrawal from the European Union, and would not contribute to the ultimate objective of EU markets better reflecting their potential in relation to the size of the single market.

The Market in Financial Markets Directive (MiFID 1) that went into application in 2007 abolished the so-called “concentration rule” on equity markets, which required investment firms to route their investor client’s orders only to incumbent stock exchanges.

With that significant policy decision, incumbent stock exchanges were exposed to competition from multilateral trading facilities and from liquidity providers subject to similar pre and post trade transparency requirements as exchanges. As stated by the EU Commission at the time[13], “the concentration rule that some member states applied represented a barrier to the emergence of an integrated and competitive trading infrastructure and so needed to be removed.”

Analysis[14] has shown that this 2007 decision to remove the “concentration rule” resulted in a significant reduction in the costs of using trading platforms, with some financial centres indicating reductions of around 80% over the initial 2 years after application, and of more than 90% reduction of trading costs over a longer period[15].

[13] Markets in Financial Instruments Directive (MiFID): Frequently Asked Questions - Memo/07/049, 2007
[14] Oxera report prepared for EU Commission DG Internal Market and Services: “Monitoring prices, costs and volumes of trading and post-trading services”, 2011
[15] This analysis however did not consider the off-setting increase on market data costs by incumbent exchanges.

The EU Commission 2021 MiFIR Review proposals to limit trading away from incumbent stock exchanges to only a smaller percentage of the overall trading volumes (i.e. only to 7% of the overall volume, if a new single cap is imposed), and to large size transactions that are normally not executed between regular counterparties, would make the EU equity trading environment less competitive and integrated, and fundamentally would make markets much less efficient and more costly for its users and the overall investors' community.

Thirty years after the 1993 Investment Services Directive, where the original "concentration rule" was enacted, this EU Commission proposal would not even cater for the exceptions provided before where "*investors' differing needs for protection and in particular the ability of professional and institutional investors to act in their own best interests*"[16] were taken into account as an exception to the "concentration rule".

Robust price formation process

AFME members believe that price formation in Europe is robust and does not require remedial action, particularly in the form of more significant change to Europe's already complex market structure. There has not been any evidence indicating negative impacts on price formation since the "concentration rule" was abolished in 2007. Equally, the EU Commission has failed to substantiate why a further curtailment of the ability to trade away from incumbent stock exchanges would be beneficial to investors or to other market participants, other than to the incumbent stock exchanges themselves.

AFME believes that enforcing a framework that allows for different execution models and a strong and calibrated transparency regime is the best way to incentivise robust and fair price formation.

The European framework features one of the most stringent and restrictive pre-trade transparency regimes among other major jurisdictions globally.

The existing limitations to open and competitive equity markets (i.e. the MIFID double volume cap) and the restrictions proposed by the EU Commission pertaining to the use of the reference price waiver or execution at midpoint by systematic internalisers – i.e. limiting these transaction types to above two times the standard market size - should be removed and rejected.

MiFID 2 introduced the double volume caps mechanism in 2018, introducing limitation for trading on EU equity markets that are unprecedented and which still do not exist on other jurisdictions with more competitive equity markets. Maintaining these rules should be subject to there being good evidence that they are beneficial to today's European economy and conducive to the economic future Europe aims to achieve. However, this has not been demonstrated.

AFME is very supportive of a price formation process for equity markets that is sound and robust and that incorporates price indications from different execution mechanisms that serve different investor needs. Price indications from trading on incumbent lit exchanges play a role in price formation. However, that is not always the most appropriate way of trading and it is certainly not the only contributing factor to price formation. In fact, given that trades executed in the "dark" are based on reference prices determined on the lit exchanges, the overall market's price discovery process is more efficient for each stock traded simultaneously in the "dark" and in lit venues.

Forming a price is a function of a number of factors not limited to market sentiment, news, earnings and other issuer statistics disclosed under issuers' continuous disclosure obligations. Available pre-trade information is not necessarily more important than post-trade transparency information, where the details of the trades that have taken place in a given share are made public. This is particularly true for trades that are large in size, which indicate where the price and size at which institutional investors (i.e. pension fund managers) are willing to trade.

This diverse price formation process supports the most efficient allocation of capital by investors and the best price discovery at all transaction sizes. AFME does not believe that enforcing increased trading on incumbent

[16] Article 14/4 of the Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field

stock exchanges would necessarily improve price formation and, conversely, it may impact the ability for firms to provide best execution for their underlying clients.

AFME Recommendation to improve outcomes for investors

AFME recommends that:

- The double volume cap is removed all together (i.e. both caps, including the single cap proposed by the EU Commission) to ensure that EU equity markets are aligned with the most competitive equity markets globally;
- The EU Commission is mandated to, upon ESMA's advice, restrict the use of the reference price and negotiated trade waivers only if there is evidence that the volume of such trading is undermining the efficiency of the price formation process;
- ESMA is mandated to ensure that the price formation process remains sound and robust by monitoring that market quality metrics are not impeded by, inter alia, the level of trading executed under the reference price and negotiated traded waivers;
- The limitation to use the reference price waiver only to transaction above a certain size (above 200% of the standard market size) is not adopted;
- The use of the reference price waiver is allowed by reference to the price provided by the consolidated tape or by venues other than the most relevant market, which would help increase the resilience of EU equity markets.

The importance of an evidence-based policy making process

Financial markets policy should be data-driven and based on evidence provided by robust data analysis. New market policies should demonstrate the benefits for end investors, issuers and other participants and be subject to robust impact assessment analysis.

Importance of thorough impact assessments

The obligation to provide for robust impact assessments form a key part of the Commission's better regulation agenda, which seeks to design and evaluate EU policies and laws so that they achieve their objectives in the most efficient and effective way.

According to the EU Commission's own guidelines, impact assessments should collect evidence (including evaluation results) to assess whether future legislative or non-legislative EU action is justified and, if so, how it can best be designed to achieve relevant policy objectives[17].

The EU Commission produced a very thorough impact assessment that accompanied its proposals to review MIFIR although such analysis was limited to why no consolidated tape provider has come forward after MiFID 2 was implemented and only assesses the various options to finally facilitate the emergence of a consolidated tape provider.

All the other proposals put forward by the EU Commission, including the proposals identified in this document, were not subject to any impact assessment[18].

Importance of improving data quality

The MiFID review needs to be based on a careful evaluation of evidence as well as on a robust data gathering exercise, which may very well need to go beyond the data currently readily available to industry stakeholders

[17] Amongst other elements, such assessments must identify and describe the problem to be tackled; establish objectives for the EU action; formulate policy options, assess their potential impacts and, where appropriate, identify a preferred option; and set out how the expected results will be monitored and evaluate.

[18] Some of the EU Commission proposals were of its own initiative or stemmed from a set of ESMA's recommendations. ESMA is not bound by the obligation of impact assess legislative proposals to ascertain whether an action is required at EU level (subsidiarity principle), nor to ensure that the EU action does not exceed what is necessary to achieve the objectives (proportionality principle). It is also not ESMA's obligation to ensure that EU capital markets remain attractive and competitive globally, and that they continue to serve the economy and the wider community.

and regulators alike. We consider that the quality and availability of the existing data remains weak and unreliable.

We commend the EU Commission for appreciating that "*Due to the disparate quality of market data, it is difficult for market participants to compare those data, which devoid data consolidation of much added-value*." and that "*the requirements for the quality of data should specified by the Commission in a Delegated Act and should take into account the advice of a dedicated consultative group, composed of experts from the industry and from public authorities*"[19].

AFME is also very supportive of the Commission objective of setting up an expert stakeholder group to advice on the quality and the substance of market data, on the common interpretation of market data and on the quality of the data transmission protocols.

Equally, we welcome ESMA's acknowledgement that "*ESMA does currently not receive information on non-price forming transactions and/or non-addressable liquidity from market participants. Hence, any analysis based on ESMA data cannot fully reflect the market share of OTC vs. on-venue trading excluding non-price forming transactions, and in consequence cannot provide currently a clear answer as to the 'real' share of OTC-trading.*"[20].

AFME is firmly supportive of ESMA's tireless work to improve the quality of the existing data and to propose improvements to the current reporting framework to ensure that eventually ESMA will receive all data sets it needs to provide for more complete and accurate market analysis.

Improvement of the quality of the existing data sets is therefore critical to ensure EU policy makers can properly calibrate their policy measures at the right time.

AFME Recommendation for an evidence-based policy making process

AFME recommends that:

- The quality of data should be improved before any material adjustment to the existing transparency and market structure framework for equity and fixed income markets is undertaken;
- The proposed adjustments by the EU Commission to key equity and fixed income market structure provisions identified above should not be adopted but instead should be revisited at a later stage once there is enough evidence to be assessed.

Delivering fair and proportionate regulation

Improving the competitiveness of the EU's financial services sector, while maintaining high regulatory standards, should be a EU key objective.

The EU regulatory framework for secondary markets should facilitate investments and growth across the Union, while remaining fair and proportionate to the EU's ultimate policy objectives.

Delivering fair and proportionate regulation to market participants and investors is key to ensure that market participants can develop their activities seamlessly without unnecessary costs.

The EU principle of proportionality requires that legislative actions should not exceed what is necessary to achieve policy objectives, and should be removed if the objectives that were sought can be better achieved by other more proportionate and effective means.

[19] EU Commission proposal to amend MiFIR - COM(2021) 727 final of 25 November 2021
[20] ESMA Consultation paper on the review of RTS 1 (equity transparency) and RTS 2 (non-equity transparency), July 2021

AFME supports the removal of any obligations or requirements impose on market participants that can be achieved by a less onerous framework.

Best execution reports

In this context, certain provisions in MiFID that require the production of quarterly and annual best execution reports – i.e. reports produced under RTS 27 – should be revisited. Whilst AFME supports the current suspension of such obligations, considering that these reports are rarely read by the recipients and do not enable investors or any users to make meaningful comparisons based on the information provided, which will become superfluous as a result of the proposals to establish a consolidated tape for equities and bonds, they should be removed as proposed by the Commission.

The consolidated tape would be used as an effective tool for retail investors to assess the quality of execution and to allow them an increased range of investment opportunities, particularly in certain Member States where trading venues are smaller and offer fewer alternatives.

Improving EU's reporting framework

Similarly, modifications to MiFIR should ensure that regulatory concepts and frameworks are still fit for purpose and remain effective.

The EU reporting framework, and the ability of banks and investment firms to report transactions on behalf of their investor clients is anchored on whether the firms qualify as "systematic internalisers" or not. Unintendedly, this reporting framework has led to an increase in the number of systematic internalisers as execution venues simply to provide reporting services to clients, which in turn has been criticised as evidence that the European trading landscape remains fragmented and that more trading in incumbent stock exchanges is required.

AFME advocates that the reporting framework should not be anchored on whether market participants qualify as systematic internalisers or not. A bank or an investment firm should be allowed to service its clients by reporting transactions on their behalf without having to opt-in to become a systematic internaliser if its business model does not involve trading on own account in a systematic way.

A firm should be able to elect to be a reporter at either an asset class or entity level and should be allowed to take on its own reporting obligations and on the obligations of its clients irrespective of its qualification as a systematic internaliser.

A central database would keep a register of all of the designated "super" reporters, eliminating duplication and uncertainty over where the reporting obligation lies and, as a consequence, would contribute to improving the quality of the reported data.

Other existing limitations to open and competitive markets should be revisited to consider whether they are delivering on their original objectives and whether the balance of cost and benefit of such limitations is still appropriate in the current environment. Maintaining any limitations to more open and competitive markets should be subject to there being good evidence that they are beneficial to today's European economy and conducive to the economic future Europe aims to achieve.

AFME Recommendation for a fair and more proportionate regulatory framework

AFME recommends that:

- The best execution reporting requirements that do not benefit users of equity and fixed income markets are removed;
- The requirement for systematic internalisers always report a transaction undertaken with clients that are not systematic internalisers is removed. Alternatively, banks and investment firms that want to elect to become designated reporters for their clients should be able to do it;
- Other features that are unique to the EU and have not proven to be beneficial to investors are reviewed and possibly removed.

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About AFME

AFME (Association for Financial Markets in Europe) advocates for deep and integrated European capital markets which serve the needs of companies and investors, supporting economic growth and benefiting society. AFME is the voice of all Europe's wholesale financial markets, providing expertise across a broad range of regulatory and capital markets issues. AFME aims to act as a bridge between market participants and policymakers across Europe, drawing on its strong and long-standing relationships, its technical knowledge and fact-based work. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. AFME participates in a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) through the GFMA (Global Financial Markets Association). For more information please visit the AFME website: www.afme.eu.

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