

Open Letter to Members of the Economic and Financial Affairs Council (ECOFIN)

Minister Bruno Le Maire

President of the ECOFIN Council (January-June 2022)

Minister of the Economy, Finance and the Recovery of France

139 rue de Bercy, 75012 Paris

21 February 2022

Dear Minister Le Maire,
Dear Members of the ECOFIN Council,

Competitive secondary markets should be at the core of the EU's financial services strategy

As EU Economy and Finance Ministers gather in Paris on 25-26 February, AFME members – which include leading participants in EU wholesale markets, headquartered both within and outside of the EU – wish to reaffirm their commitment to the Capital Markets Union (CMU) and the objective of growing the capacity of EU capital markets.

The CMU project has reached a critical juncture. In a context marked by increased international competition and the significant scale of investment required to finance the green and digital transitions, there is a pressing need for the EU to scale-up its capital markets. The United Kingdom's withdrawal from the EU has also amplified the need for the EU to significantly expand its international reach and capacity in wholesale market areas.

AFME members recognise that EU policymaking aims to simultaneously foster the benefits of open markets, connected to the international capital pools which are critical to building EU capacity in capital markets, financial stability and a sound investor protection framework. In today's environment, it is particularly important that policymaking contributes not only to advancing these objectives, but also to encouraging increased participation in EU capital markets from both local and international players in a competitive international environment.

The current context demands a greater emphasis on the policy goal of preserving – and further strengthening – the attractiveness and competitiveness of EU wholesale markets. We believe these core principles should underpin current efforts to increase the capacity of EU capital markets and achieve greater strategic autonomy in financial services.

While it is not the sole contributor, well-designed regulation plays a role in the competitiveness of financial services systems. The current review of the Markets in Financial Instruments Regulation ("MiFIR"), as well as the banking reforms which will determine the prudential treatment of banks' trading and hedging services, therefore represent an important test in advancing EU competitiveness.

AFME members believe that an attractive, well-regulated trading ecosystem, focused on promoting efficiency and strong outcomes for investors as well as corporate and SME issuers, is the most appropriate policy philosophy to nurture world-leading infrastructures and

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promote enlarged pools of liquidity within the EU. Deep liquidity pools, high quality regulation and competitive financial markets are a solid foundation on which to build the EU's capacity.

The largest and most successful global financial centres are characterised by their high regulatory standards, openness, access to global pools of capital, scale of the financial ecosystem, and quality of their legal frameworks. The EU is no different.

Moreover, wholesale banks – wherever they are headquartered – are key participants in EU capital markets as liquidity providers and play an important role in generating investment and servicing clients in the EU and globally. Their capacity to provide intermediation is central to the EU secondary markets architecture, fulfilling a role that is complementary to, and no less important than, the services provided by other market participants and infrastructures.

Certain proposals within the MiFIR Review risk undermining Europe's global competitiveness and the CMU objectives

Diverse and competitive secondary markets are key for the advancement of the CMU strategy. They provide deep pools of liquidity that reduce the cost of primary funding, allowing businesses and governments to raise finance more cheaply, and provide issuers with higher valuations. They encourage IPOs and bond issuances and attract more investors by helping them to achieve higher and more sustainable returns over the medium to long term.

The MiFIR Review should preserve this diversity in EU secondary markets with its range of trading mechanisms serving different investor needs. To achieve this, the function of risk-intermediated trading by market makers committing their balance sheets to provide liquidity to the ecosystem must be recognised. This intermediation is vital to support market depth and liquidity across the spectrum of asset classes and throughout changing market conditions¹.

European and global capital markets have long moved away from an environment centred on national securities markets monopolies. Similarly, the accompanying regulatory framework should continue to support orderly markets while reflecting the evolution of investors' trading preferences and behaviours in global markets.

While we support a number of its policy aims, particularly the establishment of a consolidated tape for both equities and fixed income, we are concerned that certain aspects of the Commission's MiFIR Review proposals risk severely undermining the competitiveness of EU capital markets.

We therefore wish to draw to your attention the proposals which impose additional restrictions on Systematic Internalisers ("SIs") as these will expose committed bank liquidity providers to increased risk, with potentially damaging effects on competition in European

¹ In addition to improving capital raising and investment conditions, liquidity provided by committed market makers is also essential to reduce price volatility and increase securities markets' resilience to shocks. This serves financial stability and is also a key factor in the implementation and smooth transmission of monetary policy.

equity and fixed income markets. This is because a bank acting in an SI capacity uses its capital and balance sheet to facilitate cheaper, more efficient investment transactions to its clients and the matching mechanisms provided by trading venues are not a substitute for this service. Consequently, the proposals as they stand will limit execution options for those who wish to invest in the EU.

In **equities markets**, our concern manifests itself via proposals for additional restrictions on SI quoting obligations. Quoting obligations should preserve a level playing field with the standard trade sizes available and visible on trading venues. Further restrictions will erode the level playing field and inhibit SIs' efficient facilitation for institutional investors, which ultimately represent the retail interests of pensioners and savers. We are also concerned by proposals that – on top of the existing share trading obligation – further curtail the ability of market participants to access liquidity in the trading modality of their choice, and reimpose a “concentration rule” in favour of certain types of venues. These include limiting the use of the reference price waiver only to transactions above a certain size and replacing the double volume cap for trading on alternative venues by a lower, EU-wide, single cap.

In **fixed income markets**, the proposed changes to transparency thresholds and the timing of publication of trading data risks exposing market-makers to undue risk. The fixed income transparency regime needs to be better calibrated than proposed to allow committed liquidity providers to continue to be able to trade in large sizes, as well as in illiquid instruments. The calibration must also provide sufficient time to market-makers to hedge or unwind their positions, both in a benign environment as well as during periods of high market volatility. The level one text should set out the principles which need to be taken into account when determining these calibrations, but the calibration exercise itself, in our view, should be delegated to ESMA on the basis of a thorough impact assessment.

These areas of the MiFIR Review proposals are suboptimal when considering the EU's market structure in isolation but it is also important for policymakers to be mindful of the wider international wholesale markets context and the choices investors have in deploying their capital. A shift in EU policymaking towards a market structure which is ultimately less supportive of investor choice by inhibiting them from accessing the most optimal trading conditions will not only result in additional costs for pensioners and savers, it also risks undermining the competitiveness of European capital markets in relation to other jurisdictions.

A well-designed consolidated tape should be prioritised

We welcome that the MiFIR Review includes a proposal for the establishment of a consolidated tape for both equities and fixed income markets. A well-designed tape for these instruments will promote more attractive and competitive capital markets in EU and contribute to reducing home country bias in the Union, where investors tend to prefer companies from their own Member State.

Making real-time equity market data available to all investors will provide a single view of trading in Europe, which is key for creating a truly pan-European market. Regrettably, the proposal does not prioritise a consolidated tape for equities with pre-trade trading data. We strongly encourage the co-legislators to be ambitious and include pre-trade data in the equities tape at the outset.

Similarly, a post-trade consolidated tape that recognises the distinct features of bond markets will provide all investors, regardless of resources or sophistication, with a comprehensive and standardised view of the European fixed income trading environment. It is though important to note that a bond consolidated tape will not solely address the issues of particularly high market data costs in this market.

While the development of a fully-fledged consolidated tape would be a game-changer for the CMU, its positive impact would be undermined if the other restrictions to the trading environment highlighted above are introduced as this will be to the detriment of investors.

Conclusion

The EU has unique strengths to support a world-leading wholesale market ecosystem, including the scale of the single market, the euro and global leadership in ESG financing, among others.

AFME members strongly believe that a competitive regulatory environment is fundamental to further develop these strengths. We are, however, concerned that the current direction of the MiFIR Review risks resulting in a less efficient, unfavourable trading architecture compared to the EU's competitors, without achieving better outcomes for investors.

We therefore urge EU authorities to seek policy outcomes in the MiFIR Review that focus on investor and corporate needs and which create the right conditions for building the EU's wholesale markets capacity and potential to be at forefront of innovation in global financial markets.

Yours sincerely,



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CEO, AFME

CC:

-Irene Tinagli MEP, Chair of the European Parliament Economic and Monetary Affairs Committee (ECON)

-Danuta Hübner MEP, European Parliament Rapporteur on MiFIR Review

-Valdis Dombrovskis, Executive Vice President of the European Commission for An Economy that Works for People

-Mairead McGuinness, European Commissioner for financial services, financial stability and Capital Markets Union