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The Committee of European Securities Regulators
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Transparency of Corporate Bond, Structured Finance Product and Credit Derivatives Markets – Consultation Paper

The CFA Institute Centre for Financial Market Integrity ("CFA Institute Centre") welcomes the opportunity to comment on the Committee of European Securities Regulators ("CESR") consultation on "Transparency of corporate bond, structured finance product and credit derivatives markets" (the "Consultation").

The CFA Institute Centre[1] promotes fair, open, and transparent global capital markets, and advocates for investors' protection. We welcome CESR's efforts to examine the issues related to transparency in the corporate bond, structured finance and credit derivates markets. The problems related to structured finance instruments have been at the heart of the issues involved in the financial crisis. Subsequently, declining investor confidence in the reported value of financial instruments and counterparty exposures has led to widespread market dysfunction. Accordingly, efforts to address transparency – a cornerstone of investor confidence – are of great importance to restoring market efficiency.

EXECUTIVE SUMMARY

The Consultation addresses the specificities of the corporate bond, structured finance and credit derivatives markets; the issues arising from the recent market turmoil; key initiatives to address these issues; and the role and scope of post-trade transparency in these markets. The focus of the Consultation stems from CESR's work to address the recommendations of the Financial Stability Forum and the G20 to strengthen financial market transparency. Our main observations are as follows:

- The CFA Institute Centre believes that greater transparency in these markets would be in the best interests of investors. Generally, greater transparency about all relevant matters enables more efficient price formation, reduces informational asymmetries, and alleviates uncertainty with respect to valuations. These factors facilitate greater market depth and hence contribute to better trading conditions for market participants.

[1] The CFA Institute Centre develops, promulgates, and maintains the highest ethical standards for the investment community, including the CFA Institute Code of Ethics and Standards of Professional Conduct, Global Investment Performance Standards ("GIPS®"), and the Asset Manager Code of Professional Conduct ("AMC"). It represents the views of investment professionals and investors before standard setters, regulatory authorities, and legislative bodies worldwide on issues that affect the practice of financial analysis and investment management, education and licensing requirements for investment professionals, and the transparency and integrity of global financial markets.

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- In our view, transparency was not likely the main cause of the problems witnessed in the corporate bond, structured finance, and credit derivatives markets. To date, these problems have included a retreat in liquidity; thinner volumes; wider bid-offer spreads; and specifically in corporate bond markets, a dislocation from CDS reference pricing. However, we do believe that greater post-trade transparency could mitigate the severity of these adverse conditions. Specifically, greater transparency would bolster confidence in valuations and reduce price dispersion, thereby mitigating the extent of investor withdrawal from these markets. This would help offset the reduction in liquidity and limit the widening of bid-offer spreads witnessed in times of crisis.

- In corporate bond markets, greater post-trade transparency would help reduce informational asymmetries with respect to wholesale/retail markets. Presently, retail investors typically do not have the same access to information as wholesale market participants. Most notably, detailed post-trade information on corporate bonds may be costly to obtain for retail investors. Better access to existing information sources for retail investors would improve price discovery and lower search costs.

- With regards to investor protection, increased post-trade transparency would facilitate more accurate valuations of investors' holdings in bond portfolios. Greater transparency helps uphold market liquidity, enabling better mark-to-market pricing and thereby reducing the reliance on mark-to-model valuations, which are subjective and dependent on the calibration of inputs. Less reliance on model-based valuations would in turn lead to reduced price dispersion.

- An industry-led solution would be the most effective method of delivering additional transparency in the corporate bond market, which should build upon existing initiatives. A mandatory regulatory regime is likely to prove costly for market participants, and may be difficult to implement in a timely and efficient manner.

- The structured finance products addressed in the Consultation include Asset Backed Securities (ABS), Collateralised Debt Obligations (CDO), Asset Backed Commercial Paper (ABCP), and Credit Default Swaps (CDS). Trade transparency on prices and volumes are primarily provided by dealer quotations and end-of-day average/consensus prices compiled by data vendors.

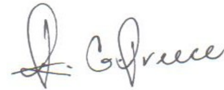
- Transactions in these markets are conducted on a private, bilateral basis, with investors most commonly adopting a 'buy-and-hold' strategy. Consequently, there is often little secondary market activity in these financial instruments. Accordingly, additional post-trade transparency measures may be of limited marginal benefit relative to the likely implementation costs. It may, therefore, be appropriate to adopt a segmented transparency regime in these markets, whereby transparency measures are only applied to those securities where an active secondary market exists.

- The relative size and liquidity of the CDS market, in addition to its importance as a source of reference pricing in other markets, means that these contracts are more suited to additional post-trade transparency than structured finance instruments. Such transparency measures should be based upon improvements to existing industry

information sources, and typically would apply to relatively standardised contracts such as single-name issues and index contracts.

We attach our response that addresses the specific questions of the Consultation. Please do not hesitate to contact us should you wish to discuss any of the points raised.

Yours faithfully,



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The CFA Institute Centre is part of CFA Institute[2]. With headquarters in Charlottesville, VA, and regional offices in New York, Hong Kong, and London, CFA Institute is a global, not-for-profit professional association of more than 101,000 investment analysts, portfolio managers, investment advisors, and other investment professionals in 134 countries, of whom nearly 87,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 136 member societies in 57 countries and territories.

SPECIFIC COMMENTS

PART 1: CORPORATE BONDS

Recent financial market turmoil: evidence of market failures in the corporate bond market and lack of post-trade information available in this market

Questions to market participants:

1. Do you believe the situation described above may be symptomatic of a market failure?
2. Have you perceived a potential asymmetry of information between market participants?

1. The Consultation cites the conditions experienced in the corporate bond market since mid-2007. These conditions include: a retreat in market liquidity; a widening of bid-offer spreads; a dislocation in the relationship between CDS prices and underlying cash bond prices; and dispersion in bond valuations arising from transactions conducted in an increasingly disorderly market.

   Collectively, these events may be perceived to be symptomatic of market failure. The initial retreat in liquidity was reflective of investor concerns over exposure to risk and uncertainty with respect to valuations (the initial phase of the 'credit crunch'). However, this resulted in a negative feedback loop, whereby the disappearance of liquidity led to heightened investor concerns, fuelling a further retreat in liquidity and a widening of bid-offer spreads. The self-reinforcing nature of these events can therefore be considered symptomatic of a market failure. That is, the inability of the market mechanism to equilibrate itself is a manifestation of dysfunction.

2. In the view of CFA Institute Centre, asymmetric information exists to the extent that smaller (typically retail) investors face constraints in accessing post-trade information in the corporate bond market. Larger, institutional investors (by far the primary participants in the corporate bond market) typically are able to use their scale to access information in much greater depth. Given the limited participation of retail investors, however, it is unclear whether asymmetric information can be linked to the market failure characterised in question 1.

Market liquidity:

3. In your view, what were the key reasons which have led to sharply reduced liquidity

[2] CFA Institute is best known for developing and administrating the Chartered Financial Analyst curriculum and examinations and issuing the CFA Charter.

in secondary trading of European corporate bonds since 2007?
4. Do you believe that additional post-trade transparency of European corporate bonds would have helped maintain liquidity in stressed market conditions? Can you please explain why?

3. The sharp reduction in liquidity in European corporate bonds is primarily attributable to a widespread loss of investor confidence, driven by concerns over risk exposures and poor disclosure, and uncertainty over security valuations. Please refer to our response to question 1.

4. Although it is not clear that additional post-trade transparency would have prevented a market failure (as characterised above), it would however have helped to mitigate the cyclicality of the retreat in liquidity. Specifically, greater post-trade transparency would have enabled more accurate marks on security positions held by investors as well as facilitating the accuracy of the net asset value calculation for bond funds. Greater transparency would therefore have helped alleviate uncertainty and would have strengthened investor confidence in security valuations. This would have resulted in greater market participation, thus minimising adverse feedback effects on the initial retreat in liquidity.

Bid/offer spread:

5. In your view, what were the key reasons for the widening of the bid/offer spreads for European corporate bonds?
6. Do you believe that greater post-trade transparency would have been helpful in limiting the widening of the bid/offer spreads we have observed for European corporate bonds?

5. The widening of bid-offer spreads is attributable to a reduction in liquidity. Please refer to question 3.

6. In our view, greater post-trade transparency would have helped to limit the widening of bid-offer spreads. Generally, greater post-trade transparency improves the efficiency of the price discovery mechanism. Moreover, bid-offer spreads are a function of liquidity. As we note in question 4, greater post-trade transparency should mitigate the extent of the retreat in liquidity. It follows that greater post-trade transparency should limit the widening of bid-offer spreads.

CDS/corporate bonds relationship:

7. Do you use CDS prices for pricing European corporate cash bonds? If so, what are the key benefits?
8. Which methods of bond price valuation do you use in the current market turmoil? Do you think that the CDS market is still a reliable indicator for bond price valuation?
9. The spreads between the CDS and corporate cash bonds have widened significantly in the first quarter of 2008. Did this widening of the spreads make it more difficult to price European corporate bonds? If so, do you think that additional post-trade transparency of corporate bond prices would have helped you to price European corporate bonds? How do you assess the situation since mid-September 2008?
10. Do you expect that the relationship between the CDS market and the cash bonds

market will return to what has been observed historically once market conditions stabilise? If not, can you please articulate the reasons?

7. Through question 10: We are not active participants in the CDS market and are therefore unable to comment.

Valuation:

11. Have you experienced difficulties in valuing corporate bond holdings? If so, what were the main reasons?
12. Would additional post-trade transparency in distressed market conditions help valuation?

11. Though we are not active participants in the bond market, we are aware of the difficulties experienced by market participants in valuing corporate bonds. The main reason has been the difficulty in establishing accurate marks due to a reduction in liquidity, and in some cases, inactive markets. Consequently, in order to determine fair value, market participants have had to make greater use of model-based valuations. That is, mark-to-market valuations have not been possible in some instances due to an inability to conduct transactions in an orderly market. The subjective nature of these types of valuations, in addition to their sensitivity to model inputs, can result in a wide dispersion in valuations. This further undermines confidence and exacerbates illiquidity.

12. It follows from question 11 that additional post-trade transparency in distressed market conditions would improve the quality of valuations. Greater transparency would improve investor confidence, mitigate the reduction in liquidity, and help contribute to the restoration of orderly markets. This would enable more mark-to-market pricing and thereby reduce the incidence of dispersion due to mark-to-model valuations.

Potential benefits and drawbacks of increased post-trade transparency

Questions to market participants:

13. Do you agree with the potential benefits and drawbacks described above? Please provide evidence supporting your opinion. Please explain how the potential drawbacks might be mitigated.
14. Are there other main benefits or drawbacks of increased post-trade transparency in the bond markets which CESR needs to consider?

13. The main potential benefits of increased post-trade transparency cited in the Consultation include: better access to existing information sources for retail investors, leading to more efficient price discovery and lower costs; facilitation of compliance with other regulatory requirements and investor protection; and more accurate valuations for securities held in bond portfolios.

    The main potential draw-backs of increased post-trade transparency cited in the Consultation include: a reduction in liquidity arising from reduced incentives for liquidity providers to participate in bond markets; increased risk of transactions

becoming 'visible', resulting in market participants refraining from taking certain positions in the market; and a lack of clear evidence from some empirical studies that increased post-trade transparency has a significant impact on liquidity.

The CFA Institute Centre broadly agrees with these points. However, on balance we believe that the benefits outweigh the drawbacks. In the interests of fairness and investor protection, retail investors should have greater access to the same sources of information as wholesale market participants. This should reduce informational asymmetries and ultimately improve market efficiency. In our view, these benefits are likely to dominate the noted potential drawbacks.

14. We have no further comments; the Consultation adequately addresses the potential benefits and drawbacks of increased post-trade transparency.

Experience in the U.S market: the TRACE system

Questions to market participants:

15. What are your personal experiences with TRACE? Please specify whether you are directly trading in the U.S corporate bond markets on the buy or sell side.
16. Do you see other benefits or drawbacks of the introduction of a TRACE-like post-trade transparency regime for OTC trades in corporate bonds in Europe?
17. Are you of the view that the more notable volume declines experienced for 144a securities, compared to securities which are covered by TRACE, is due to a lack of post-trade information? Please provide a rationale.

15. We are not active participants in the bond markets and therefore have no specific comments on TRACE.

16. Paragraph 61 of the Consultation states that "TRACE is a system operated by FINRA for mandatory reporting and disclosure of over-the-counter secondary market transactions pertaining to eligible fixed income securities." Further detail is given in Annex 1 page 62:

"For each trade, the dealer is required to identify the bond, and to report – among others - the date and time of execution, trade size, trade price, yield, security identifier, capacity (i.e as principal or agent), stated commission, counterparty identifier, whether the dealer bought or sold the transaction. Firms are required to report any transactions in TRACE-eligible securities within 15 minutes of execution."

With regards to the main benefits of TRACE, the Consultation notes the following:

- Early studies found that market liquidity increased and bid-offer spreads narrowed following the introduction of TRACE.
- Research found that TRACE led to decreased bond price dispersion.
- Statistical evidence indicates that the introduction of post-trade transparency significantly reduced the cost that investors pay to dealer firms to execute their trades.

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- Retail trades exhibited increasingly faster price reactions surrounding information events.
- In the absence of transaction reporting and disclosure, customers find it difficult to know whether their trade price reflects market conditions.
- The introduction of TRACE reduced dealers' information advantage relative to customers.

The main drawbacks of TRACE cited in the Consultation include:

- Trade transparency typically makes it possible to ascertain when a dealer has taken a large position and the price he has paid. Other participants could act on this information, resulting in adverse price movements for the dealer. This may discourage dealers from committing capital.
- Most corporate bonds are inherently illiquid, and other than shortly after issuance, do not trade very frequently. There has been no demonstrated market failure to warrant the introduction of TRACE.
- The definition of liquidity is multi-faceted; therefore it is difficult to accurately gauge the impact on liquidity of post-trade transparency.

We believe CESR's analysis adequately addresses the benefits and drawbacks of a TRACE-like post-trade transparency regime. On balance, we believe that the benefits from the introduction of such a post-trade transparency regime in Europe would far outweigh the drawbacks.

However, we recognise that there are differences between the U.S and European corporate bond markets. For example, there is no single self-regulatory agency in Europe — such as FINRA in the U.S — that co-ordinates the dissemination of trade information. That said, we are aware of industry initiatives by the International Capital Markets Association (ICMA) and the Securities Industry Financial Market Association (SIFMA) to improve post-trade transparency. The CFA Institute Centre concurs with CESR's view that a market-led approach to the provision of post-trade information on non-equity markets is the most appropriate solution. As the Consultation notes, such a solution would avoid any unintended negative consequences which may arise from prescribing mandatory requirements.

17. The Consultation notes that, since October 2007, volumes for Rule 144A securities (private placement) have declined by more than the volumes of transparent TRACE-eligible bonds. We are not able to comment as to whether this is attributable to the lack of post-trade transparency for these securities.

<u>Market-led initiatives in the trade transparency area: ICMA and SIFMA</u>

Questions to market participants:

18. Please provide information on your experience, if any, in terms of timing, content and access to information of the market-led solutions outlined above. What is your assessment of the effectiveness of the present self-regulatory initiatives?
19. Please provide comments on the characteristics that market-led initiatives should, in your view, have.

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18. We are not active participants in the bond markets and are therefore unable to comment on specific experiences.

19. The Consultation notes that so far, market-led transparency initiatives have focused on aggregated data (instead of information on a trade-by-trade basis); reporting of information on a delayed basis; and limited coverage of issues and transactions.

    Market-led initiatives should provide retail investors with easy access to reasonably priced, consolidated post-trade information via the internet in a format that enables investors to download trade information in an accessible manner. Evidence from the respective websites for the ICMA and SIFMA initiatives indicates that this is broadly the case. However, the information would appear to be limited in breadth and offers the user limited flexibility to find specific information.

    In our view, the information that should be made available through these market-led initiatives should be based upon the information supplied via the U.S TRACE system. This would provide retail investors with the types of information more commonly available to wholesale market participants. As per the TRACE system, the information made available, among other things, would include: the date and time of execution, trade size, price, yield, security identifier, commission, and so forth. It would also be useful for investors to have access to historical data through these market-led initiatives.

<u>Conclusions and recommendations</u>

Questions to market participants:

20. Do you think that the introduction of additional post-trade information on prices could help restore market confidence and maintain market liquidity in times of future crisis?
21. Do you believe that additional post-trade transparency of European corporate bond markets would contribute to liquidity in normal market conditions? Can you please explain why?

20. The CFA Institute Centre concurs with CESR's view that, whilst insufficient post-trade transparency was not likely a primary factor behind recent bond market turbulence, greater post-trade transparency could improve market conditions. For example, as we have noted throughout our response, greater transparency would underpin confidence in valuations and reduce price dispersion, thereby mitigating the extent of investor withdrawal from the market. This would help offset the reduction in liquidity and limit the widening of bid-offer spreads witnessed in times of crisis.

21. We believe that additional post-trade transparency would contribute to liquidity in normal market conditions. Whilst it is acknowledged that wholesale market participants generally have sufficient access to post-trade information, retail investors are typically constrained from accessing the same degree of post-trade information as wholesale investors. Consequently, asymmetric information exists to the detriment of retail investors. Greater post-trade transparency would reduce

informational asymmetries, enable greater retail participation in bond markets, and therefore improve market efficiency and lower costs. Please also refer to our response to question 13.

Questions to market participants:

22. To what extent can corporate bond markets be characterised as wholesale or retail markets? How would you distinguish between wholesale and retail markets? What are the differences across the EU?
23. What would be the benefits and the downsides of a harmonised pan-European transparency regime for:
    a) the wholesale market;
    b) the retail market.

    Please provide arguments and fact-based data on the potential impact.

22. The predominant participants in corporate bond markets are institutional investors. Accordingly, corporate bond markets may be characterised as predominantly wholesale, whereby transactions are conducted between professional counterparties on behalf of financial institutions. Retail investors are typically individuals who may participate in bond markets through a financial intermediary who conducts transactions on behalf of the individual's account. Retail investors represent a relatively small proportion of total market participation in corporate bonds. As the Consultation notes, Italy[3] has a larger proportion of retail participants in corporate bond markets than most other EU jurisdictions; however we are not able to comment further on the experiences of different Member States.

23. Please refer to our response to question 13 which addresses the benefits and drawbacks of increased post-trade transparency for market participants. Such a regime is likely to be of greatest benefit to retail investors, who presently only have limited access to post-trade information on corporate bonds (in contrast to wholesale investors). Accordingly, CESR should carefully evaluate the merits of introducing a segmented transparency regime to differentiate between the needs of wholesale and retail investors (as indicated on page 28 of the Consultation).

Questions to market participants:

24. Is the reduced reliability of the CDS market as an indicator/proxy for calculating the value/price in the cash market under certain market conditions an issue which calls for more post-trade transparency of cash corporate bonds?
25. Do you think that transparency requirements could help address wider issues such as those relating to accurate valuations?
26. What would be the most cost-effective way of delivering additional transparency: an industry-led solution, possibly based on a road map set by regulators, or mandatory regulatory post-trade transparency requirements?
    a) The retail market.
    b) The wholesale market.

[3] The option under Recital 46 of the Markets in Financial Instruments Directive has been exercised in Italy. This option enables Member States to apply pre- and post-trade transparency requirements to financial instruments other than shares.

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Please provide a rationale.

24. We are not active participants in the CDS market, therefore we are unable to make specific observations. However, generally, more post-trade transparency in both the cash corporate bond and CDS markets would improve the price discovery mechanism. While the dislocation in the pricing relationship between the CDS market and cash market is more likely a primary function of the credit crisis than being primarily attributable to the level of transparency, we believe that greater post-trade transparency in these markets would facilitate better reference pricing in each market.

25. The CFA Institute Centre believes that transparency requirements would significantly help address issues relating to accurate valuations. Please refer to our response to questions 11 and 12.

26. An industry-led solution would be the most effective method of delivering additional transparency in the corporate bond market, for both retail and wholesale participants. A mandatory regulatory regime is likely to prove costly for market participants, and may be difficult to implement in a swift and timely manner. In contrast, an industry-led approach, building on the existing initiatives established by ICMA and SIFMA, is likely to be more cost-effective and quicker to implement. Moreover, an industry-led approach would represent the views of professional investors, who — as active participants — have the necessary knowledge and experience to determine what exact requirements are appropriate having regard to the specificities of the corporate bond market. We believe that these actors are best placed to implement a post-trade transparency regime and serve the best interests of investors.

Technical issues:

27. Which should be in your view the key components of a post-trade transparency framework for corporate bonds? Please provide your view with respect to depth and breadth of information as well as to timeliness of data as described above.
28. Should the information on the volume be reported only below a certain size, what would be the threshold to avoid any risk of market impact?
29. Would you see some benefits in a step-by-step implementation, starting with the most liquid bonds, as employed when TRACE has been introduced?

27. Please refer to our response to question 19.

28. First, the disclosures are made after the trades are complete. The disclosures would only reflect activities that have occurred in the recent past and therefore would not impair investors' trading strategies.

    Moreover, these are matters of concern in the equity markets. In those instances, the reporting includes the volume regardless of the size of the trade. Investors have responded to these circumstances and rules by dividing their orders into smaller, less-conspicuous lots, by spreading their orders across a number of brokers, or by using computer trading systems that automatically spread the orders. While such efforts do not eliminate completely the market effects of the purchase or sale of

large positions, they provide other market participants with highly relevant information that they can incorporate into their investment decisions. We believe that participants in the fixed-income markets would benefit from similar information, and that the positive effects from such disclosure would outweigh any negatives.

29. A phased implementation of a post-trade transparency regime would be most appropriate and cost-effective. This would allow market participants to ensure that their operations and resources are well placed to fulfil additional transparency obligations. It would also facilitate an assessment of the effectiveness of the initiative at each stage of the process.

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PART II: STRUCTURED FINANCE PRODUCTS AND CREDIT DERIVATIVES

The role of post trade-transparency

Questions to market participants:

30. Does this analysis represent your practical experience regarding information relevant and available for pricing of each of the products covered by this consultation paper?
31. Are there other sources of information available which you use for pricing and valuation purposes? Can you provide details regarding the respective role of pricing services using proprietary models and consensus pricing services?

30. The products covered in Part II of the Consultation include Asset Backed Securities (ABS), Collateralised Debt Obligations (CDO), Asset Backed Commercial Paper (ABCP), and Credit Default Swaps (CDS).

    The Consultation notes that, in these markets, transactions are conducted over-the-counter (OTC) or via private placements. Hence, there is generally no post-trade information available from regulated markets or multi-lateral trading facilities (MTFs). Trade transparency on prices and volumes are primarily provided by dealer quotations and end-of-day average/consensus prices compiled by data vendors. However, prices supplied to vendors are not identified by contributors as being either indicative or actual traded prices. Therefore, it may be difficult to gauge the extent to which average/consensus prices are composed of actual traded prices.

    For the CDS market, at least, trade information is much more widely available. Data vendors compile information on both an intra-day and end-of-day basis, and CDS spreads are acknowledged to be reliable indicators of credit risk. Recent initiatives, such as the Depositary Trust & Clearing Corporation's Trade Information Warehouse, have led to further improvements in trade transparency for this market.

    The Consultation adequately addresses the information relevant and available for the pricing of structured finance products and credit derivatives. We have no additional comments.

31. We are not directly involved in the pricing and valuation of these securities; therefore we are unable to offer specific comments.

ABS Securities

Questions to market participants:

32. What do you think are the benefits and/or downsides of a post-trade transparency regime for ABS? Please support your arguments with evidence and explain how the possible downsides could be mitigated.
33. Do you believe that post-trade transparency would be desirable for all types of ABS? If not, can you explain which types of instruments/tranches (e.g. AAA RMBS) should be subject to post-trade transparency?

32. As the Consultation notes, the ABS market is almost entirely institutional, with trades conducted bilaterally between dealers. Investors adopt a buy-and-hold strategy and so there are no well-established secondary markets for these securities (with the possible exception of triple-A rated residential mortgage backed securities). Consequently, there is little post-trade transparency.

    In light of these market characteristics, CESR should carefully determine whether a post-trade transparency regime would be appropriate for ABS, having regard to the likely costs of implementing such transparency requirements. The benefits of increased post-trade transparency are likely to include more accurate valuations of investment portfolios containing ABS, and possibly more accurate information to facilitate risk management modelling and testing. However, given the current information supplied by dealers and data vendors, such as consensus prices, CESR should carefully determine whether these advantages would yield significant marginal benefits relative to the likely implementation costs of additional transparency requirements.

33. As noted above, other than for residential mortgage backed securities, there is little (if any) secondary trading in the ABS market. On this basis, and considering the likely cost of a market-wide initiative, it may be appropriate to limit post-trade transparency to more common types of ABS (such as, among others, residential mortgage backed securities, and ABS backed by credit card receivables). It would be inappropriate to apply a similar post-trade transparency regime for bespoke securities. The specific nature of these contracts would make such a transparency regime impractical and of limited benefit to other market participants. Therefore, the application of a post-trade transparency regime should be consistent with the level of investor interest in the security in question.

    It may, however, be inappropriate to target a particular segment of the RMBS market, such as triple-A. Notwithstanding the questionable appropriateness of using credit ratings to distinguish between classes of securities, market participants may be incentivised to engage in ratings arbitrage if one class of RMBS securities were subject to transparency requirements whereas other classes were not.

Questions to market participants:

34. Would it be meaningful to segment a post-trade transparency regime between 'higher liquidity' ABS (i.e. commoditised products, standardised structures, higher credit quality and homogeneous collateral) from 'low liquidity' ABS (i.e bespoke products, non-standardised structures, lower credit quality, heterogeneous collateral)? In this case could you explain what could be considered as low liquidity ABS?
35. What post-trade information should be published? In addition to information about the price at which the transaction was executed, the volume and the time of the transaction, would there be any benefit in publishing information about portfolio composition, asset class, the initial interest (seller or buyer)? Is there any other information which would be relevant?

34. Having regard to the limited extent of secondary markets in ABS, it may be appropriate to segment any transparency regime. In our view, the segmentation

should be based upon the extent of secondary market activity, as opposed to being based on an arbitrary definition of 'high' or 'low' liquidity. For example, if there is no active secondary market, then a transparency regime may not be appropriate. The extent of secondary market activity is itself a function of the level of investor interest in the security. Therefore, as we note in question 33, post-trade transparency should be limited to the more common types of ABS.

35. We are not aware of any further relevant information beyond that cited in the question.

Questions to market participants:

36. When should post-trade information be published? Should it be published immediately after a trade has been concluded? Please explain rationale.
37. Do you believe that a post-trade transparency regime should or could be implemented in connection with other regulatory interventions at the same time (e.g. relating to the quality of information of the underlying assets, standardisation of reporting)?
38. Would you like to make any other observations relevant for CESR work on the need for post-trade transparency for ABS?
39. Please indicate whether you represent an organisation which is involved in:
    a) originating ABS
    b) selling ABS
    c) buying ABS
    d) providing pricing information on ABS; or
    e) rating ABS.

36. In our view, it would be most appropriate to publish post-trade information immediately after the conclusion of a given trade. This would provide investors with the most timely, relevant information on which to base their decisions, and consequently may encourage further participation in these markets.

37. If a post-trade transparency regime is implemented, it may be inappropriate to supplement this with additional regulatory interventions at the same time. Market participants should be given the opportunity to adjust their operations and resources as necessary in order to meet the transparency requirements, without being over-burdened by the imposition of additional regulatory requirements. However, if the instrument is widely used, and its notional and at-risk exposures are sufficiently large, it may be appropriate to supplement post-trade transparency with additional measures to improve the quality of information disclosed.

38. We have no further observations relevant to ABS.

39. We are not involved in the activities a) through e).

<u>Collateralised Debt Obligations</u>

Questions to market participants:

40. What do you think are the benefits and/or downsides of a post-trade transparency

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regime for CDOs? Please support your arguments with evidence and explain how the possible downsides could be mitigated.
41. Do you believe that post-trade transparency would be desirable for all types of CDOs? If not, can you explain which types of structures/tranches (e.g. cash CDOs vs. synthetic CDOs) should be subject to post-trade transparency??

40. Please refer to our response to question 32; we believe the same benefits and drawbacks broadly apply to the CDO market.

41. Given that CDOs are inherently illiquid and rarely trade on a secondary basis, a post-trade transparency regime for all types of CDO may be of limited marginal benefit relative to the likely implementation costs of introducing such a regime. If any additional post-trade transparency requirements were to be introduced, they would likely be of most benefit in the synthetic CDO market, for which the collateral pool is largely comprised of credit default swaps. Synthetic CDOs are typically highly standardised and more liquid, making these contracts more easily transferable. Accordingly, they would be more suited to a post-trade transparency regime than other classes of CDO. Please also refer to our response to question 33.

Questions to market participants:

42. Would it be meaningful to segment a post-trade transparency regime between 'vanilla' CDOs (i.e. comparable to the ABS with standardised structures, higher credit quality and homogeneous collateral) from Structured Finance CDOs (i.e. bespoke products, non-standardised structures, lower credit quality, heterogeneous collateral)? In this case, could you explain what could be considered as less 'vanilla' CDOs?
43. To what extent would post-trade transparency be helpful to reduce the bid and ask spread or price dispersion for a particular transaction/instrument?
44. What post-trade information should be published? In addition to information about the price at which the transaction was executed, the volume and the time of the transaction, would there be any benefit in reporting information about portfolio composition, asset class, the initial interest (seller or buyer)? Is there any other information which would be relevant?

42. Please refer to our response to question 34; any segmentation should be defined according to the extent of secondary market activity. The extent of secondary market activity is itself a function of the level of investor interest in the security. Therefore, as we note in question 33, post-trade transparency should be limited to the more common types of structured finance security. In contrast, it would be inappropriate to apply a similar post-trade transparency regime for bespoke securities.

43. Generally, the principal benefit of post-trade transparency would be to bolster investor confidence and maintain participation levels in markets, thereby mitigating the adverse effects of illiquidity such as a widening of bid-offer spreads.

44. We are not aware of any further relevant information beyond that cited in the question.

Questions to market participants:

45. When should post-trade information be published? Should it be published immediately after a trade has been concluded? Please explain rationale.
46. When facing inactive markets, to what extent would a post-trade information regime be applicable? If not, could you detail the rationale for an alternative system when markets are no longer active?
47. To what extent can observable prices in the secondary market help to test or promote internal valuation models?

45. In our view, it would be most appropriate to publish post-trade information immediately after the conclusion of a given trade. This would provide investors with the most timely, relevant information on which to base their decisions, and consequently may encourage further participation in these markets.

46. As indicated in our response to question 42, post-trade transparency should be based, in the first instance, on the extent of any secondary market in the financial instrument. The absence of an active secondary market would imply that a post-trade transparency regime would be of little marginal benefit relative to the implementation costs.

47. Observable prices in the secondary market can strengthen firm's internal models. Primarily, such prices enable an assessment of the validity of valuation models. They also enable firms to validate a variety of statistical modelling techniques and hence strengthen the risk management process.

Questions to market participants:

48. Do you believe that a post-trade transparency regime should or could be implemented in connection with other regulatory interventions at the same time (e.g. relating to the quality of information of the underlying assets, standardisation of reporting)?
49. Would you like to make any other observations relevant for CESR work on the need for post-trade transparency for CDOs?
50. Please indicate whether you represent an organisation which is involved in:
    a) originating CDOs
    b) selling CDOs
    c) buying CDOs
    d) providing pricing information on CDOs; or
    e) rating CDOs

48. Please refer to our response to question 37.

49. We have no further observations relevant to CDOs.

50. We are not involved in the activities a) through e).

<u>Asset Backed Commercial Paper</u>

Questions to market participants:

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51. What do you think are the benefits and/or downsides of a post-trade transparency regime for ABCPs? Please support your arguments with evidence and explain how the possible downsides could be mitigated.
52. Do you believe that post-trade transparency would be desirable for all ABCPs, whatever their structures or maturities? If not, can you explain which types of structures should be subject to post-trade transparency?
53. What post-trade information should be published?

51. Please refer to our response to question 32; we believe the same benefits and drawbacks broadly apply to the ABCP market.

52. Given that ABCPs are typically illiquid and are largely transacted on a buy-and-hold basis, a post-trade transparency regime for all types of ABCP is likely to be of limited marginal benefit relative to the likely implementation costs of introducing such a regime.

53. Please refer to our response to question 52; we have no further comments.

Questions to market participants:

54. Would you like to make any other observations relevant for CESR work on the need for post-trade transparency for European ABCPs?
55. Please indicate whether you represent an organisation which is involved in:
    a) originating ABCP
    b) selling ABCP
    c) buying ABCP
    d) providing pricing information on ABCP; or
    e) rating ABCP.

54. We have no further observations relevant to ABCP.

55. We are not involved in the activities a) through e).

<u>Credit Default Swaps</u>

Questions to market participants:

56. What do you think are the benefits and/or downsides of a post-trade transparency regime for CDS? Please support your arguments with evidence and explain how the possible downsides could be mitigated.
57. Do you believe that post-trade transparency would be applicable to all types of CDS? If so, can you explain the rationale for which types of CDS (e.g. single name CDS) should be excluded from post-trade transparency?

56. As with structured finance products, CDS contracts are transacted privately in the over-the-counter market, and the primary sources of price information are dealer quotations and consensus prices compiled by data vendors. However, coverage of CDS prices is much wider than for the structured finance securities addressed in Part II of the Consultation. For example, CDS spreads are quoted for a wide range of

reference entities on both an intra-day and end-of-day basis. Additionally, the Depositary Trust and Clearing Corporation's Trade Information Warehouse now publishes weekly data on notional volumes and number of contracts for the top 1,000 reference entities. Finally, CDS contracts are generally more liquid (given the large size of this market) compared to most structured finance securities.

Having regard to the importance of the CDS market for reference pricing in other markets (such as the corporate bond market), additional transparency measures would likely be beneficial. Specifically, additional transparency would further contribute to the efficiency of price discovery in this market and in other markets for which price formation is inter-related with movements in CDS spreads. Moreover, given the size of this market[4], coupled with the role of novation[5] (which effectively creates a secondary market in CDS), the importance of additional post-trade transparency should exceed any cost of implementation.

The existing transparency initiatives provide a useful basis for expanding the level of post-trade information to be provided to participants in this market.

57. Post-trade transparency measures should be applicable to those contracts that have a secondary market (that is, where contracts can be novated). For example, this would comprise most single-name CDS contracts and index contracts, which are liquid and highly standardised. It would be inappropriate to apply a similar post-trade transparency regime for bespoke contracts that are tailored to the specific needs of two counterparties. The specific nature of these contracts would make such a transparency regime impractical and of limited benefit to other market participants.

Questions to market participants:

58. What post-trade information should be published? CDS spread, notional amount, reference entity, maturity?
59. When should trade information be published? Should it be published immediately after a trade has been concluded? Please explain rationale.

58. At a minimum, information on the spread, notional amount, reference entity (including class of debt being referenced), sector, and maturity date, should be made available. It should be up to market participants to determine what other relevant information (if any) should be published.

59. Please refer to our response to question 36.

Questions to market participants:

60. Do you believe that a post-trade transparency regime should or could be implemented in connection with other regulatory interventions at the same time (e.g. relating to the quality of information on the underlying assets, standardisation

[4] The gross notional amount outstanding was approximately $25 trillion as at end of January 2009, according to the DTCC Trade Information Warehouse.
[5] Novation is the process by which a CDS contract is transferred from one counterparty to another.

	of reporting)?
61.	Would you like to make any other observations relevant for CESR work on the need for post-trade transparency for CDS?

60. Please refer to our response to question 37.

61. We have no further observations relevant to the CDS market.

19th February 2009.