ICMA
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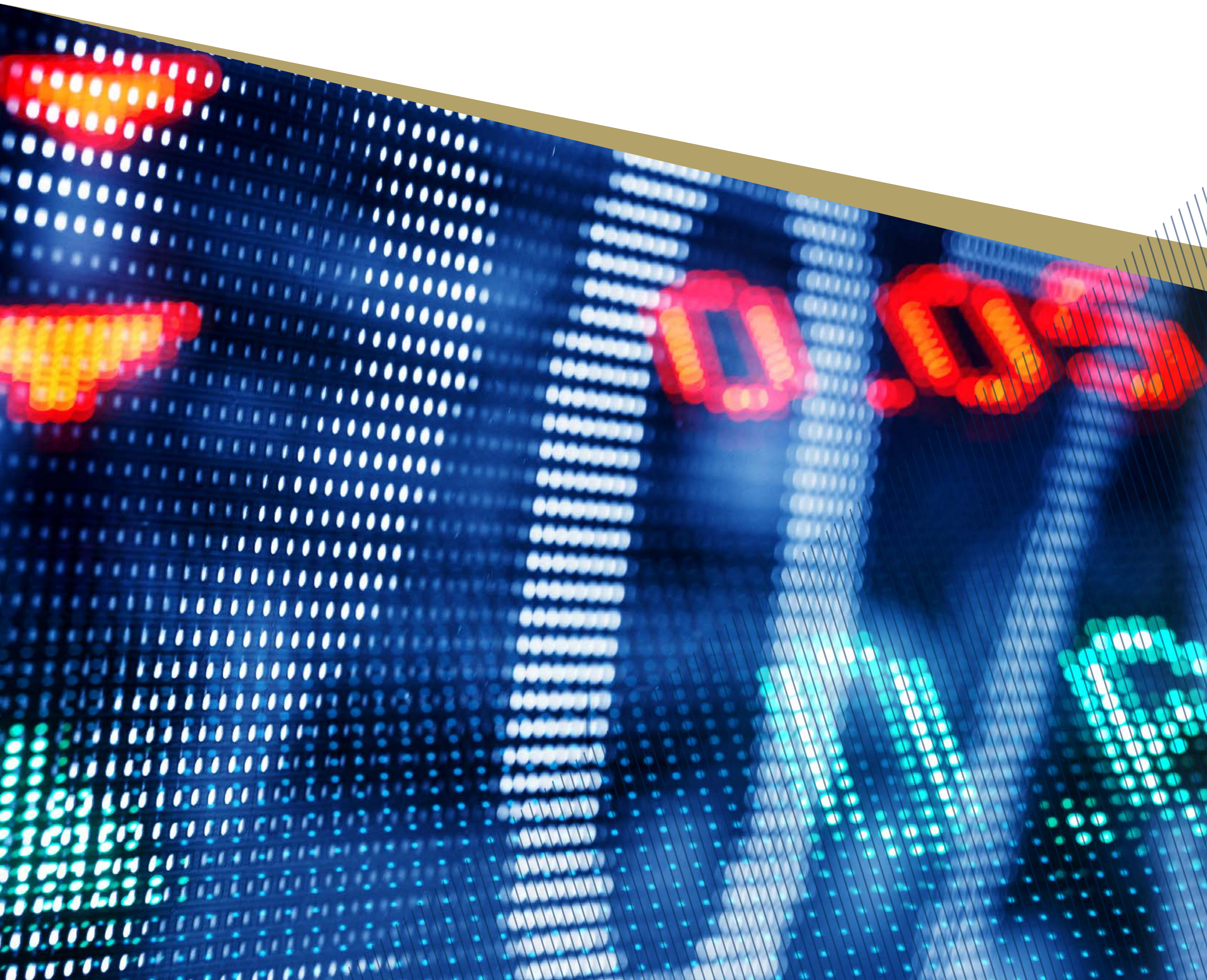
Association

MiFID II/R and the bond markets: the first year

An analysis of the impacts and challenges of MiFID II/R implementation since January 2018

December 2018



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Executive Summary

The feedback confirms that the first year of MiFID II/R implementation has not been without challenges for the bond markets and, in many cases, it has not yet fully achieved its objectives.

From a primary market perspective, the obligations regarding allocation justification recording, and disclosures of costs and charges have had little substantive impact other than an additional administrative burden. The interplay of the product governance requirements and PRIIPs, however, has proved challenging to implement and has caused significant concern and debate around the practicability of compliance in the Eurobond context. The introduction of these regimes has been followed by a marked drop in low-denomination bond issuance, limiting the investment possibilities for retail investors.

In terms of secondary market impacts, the headline is that liquidity and functioning appear to have remained mostly unchanged in the wake of the regulation, and that for the most part it is business as usual. However, there have been a number of shortcomings, particularly with respect to the transparency regime and the accessibility and quality of pre- and post-trade data. While there is some optimism that this will improve over time, the regulation seems to have missed an opportunity to provide a utility-based consolidated tape for fixed income.

In addition, the systematic internaliser regime has thus far failed either to improve transparency or create a level playing field. Public best execution reporting is challenging and expensive to produce, but barely used by anybody. Meanwhile, the regulation does seem to have helped push a little more trading onto venues, which is one of its main objectives.

The implications for FICC research also seem to be evolving. Many firms are finding it difficult to decide what research needs to be paid for, and there still seems to be a need for further regulatory guidance in this respect. While the number of research providers used by firms has decreased, most feel that the overall quality of research has remained unchanged, although views on the availability and breadth of SME focused research are more mixed. So far, firms have been able to cope with the reduction in accessible research and have not noticed a negative impact on fund performance.

In summary, the European bond markets continue to function following the implementation of MiFID II/R, but, at least so far, the regulation has not yet delivered on its objectives of improved investor protection, greater transparency, and a more competitive landscape. In some cases, it has produced unintended consequences, while for many it has mostly been an expensive and time-consuming exercise in regulatory compliance.

But MiFID II/R is as much a journey as a destination, and it is broadly understood that it will take time (perhaps years) for the many challenges to be addressed and for any benefits to become manifest. Reports such as this will hopefully help to guide market participants and regulators alike as they continue that shared journey.

Contents

Introduction

The introduction of the second Markets in Financial Instruments Directive (MiFID II) and Regulation (MiFIR) on 3 January 2018 is perhaps the most significant development to impact European bond markets in memory, with new requirements affecting everything from how new issues are marketed, to transaction reporting, trade transparency, secondary market structure, evidencing best execution, and even how fixed income research is distributed and consumed.

In the lead-up to implementation in 2018, ICMA's numerous MiFID II/R roundtables and workshops, across Europe and beyond, highlighted accumulating anxiety among sell-sides, buy-sides, and trading venues, as to how the new rules should be interpreted and implemented, the potential impacts on market functioning and liquidity, as well as the overall level of industry preparedness. Open questions remained about the ability for retail to access the bond markets, how different transparency obligations across jurisdictions would affect liquidity, the importance of sell-side firms becoming systematic internalisers, the flexibility to 'agree' trades OTC before 'consummating' them on a platform, how non-EU firms would be impacted, and whether market efficiency would suffer due to less availability of specialized market research.

In the first weeks of January 2018 it soon became clear that for European bond markets it was business as usual, and despite reports of numerous ongoing difficulties and more than a few hiccups, the market continued to function with little or no visible impact on liquidity. It also became apparent that MiFID II/R is a process, rather than an event, particularly as new requirements rolled into play, including best execution reporting and the systematic internaliser regime, and as firms grappled with what was expected of them, while also trying to make sense of the ESMA liquidity data. Regular, often detailed, regulatory guidance in the form of ESMA Q&As, as well as that from the various national competent authorities (NCAs), has helped to smooth the process. But again, many questions and issues still need to be addressed, and ICMA and others continue to work with the authorities and market participants to help harmonize approaches and improve the effectiveness of the regulation.

This report, which largely draws on input from ICMA's diverse sell-side and buy-side members active in the European fixed income markets, is intended to provide an overview of the first year of MiFID II/R from the perspective of bond markets, covering primary market issuance, secondary market trading, and research distribution and consumption. It is hoped that this will prove useful to market participants and regulators alike as the MiFID II/R implementation 'process' continues into 2019 and beyond.

I. Primary markets

Introduction

Fixed income primary markets have been affected by MiFID, as many underwriters participating in new issue syndicates are MiFID authorised entities. These new measures include allocation justification recording (in relation to underwriting & placing), the inducements and costs & charges regimes, and product governance.

The primary markets community has also experienced the Packaged Retail and Insurance-Based Investment Products (PRIIPs) regime, to the extent that certain bonds are potentially 'packaged' and are being made available to retail investors in the EEA.

Allocation justification recording

Concept – MiFID firms providing a MiFID placing service to issuers are required to keep an 'audit trail', non-public written record of the justification for each investor allocation made. The rationale for this is to identify potential conflicts of interests, as underwriters look to balance the interests of their issuer clients with the interests of their buy side relationships.

Practical experience – The underwriting community reached broad consensus on allocation recording principles, with the underwriter responsible for billing and delivery generally circulating an initial draft record that other syndicate members can then adopt (modifying it as relevant for their internal needs). The experience so far has mainly just resulted in added administration for underwriters, and it remains to be seen whether this measure will have meaningful benefits for issuers or investors.

Inducements and costs & charges

Concept – Firms providing MiFID services (e.g. order reception/transmission to any investor 'client') must disclose to their client in advance any fee/commission or non-monetary benefit received from a 'third party' in relation to the client service. Firms must also inter alia disclose ex ante and annually ex post the costs and charges relating to the services and financial instruments concerned, (also "*encompassing any third-party payments*").

Practical experience – Agreement on whether these rules apply to the disclosure of underwriting fees has varied in practice depending on the type of fees involved and how individual underwriters and/or how individual transactions are organised. Moreover, the prevailing view is that investors have little or no interest in the level of bond underwriting fees as these are very rarely a material factor in making an investment decision regarding bonds.

Product governance and PRIIPs

PRIIPs concept – Any person 'manufacturing' a 'packaged' product, before it is 'made available' to retail investors in the EEA, must publish a key information document (KID) of no more than three pages and then regularly review it, and if needed, publish a revised KID. Any person advising on, or selling, such a product must provide retail investors in the EEA with the KID in good time before those retail investors are bound by any contract or offer.

Product governance (PG) concept – MiFID II persons that "*create, develop, issue and/or design financial instruments, including when advising corporate issuers on the launch of new financial instruments*" are 'manufacturers' for PG purposes. Collaboration between manufacturers must be documented in an agreement. MiFID II persons that "*offer or sell*", or "*offer or recommend*", financial instruments are 'distributors' for PG purposes (with no connection to the manufacturer being explicitly required). Manufacturers must identify, and communicate to distributors, a compatible target market of investors and periodically review that target market. Distributors must identify their own target markets (by either adopting the manufacturer's target market or refining it). These requirements are all applicable on a 'proportionate' basis.

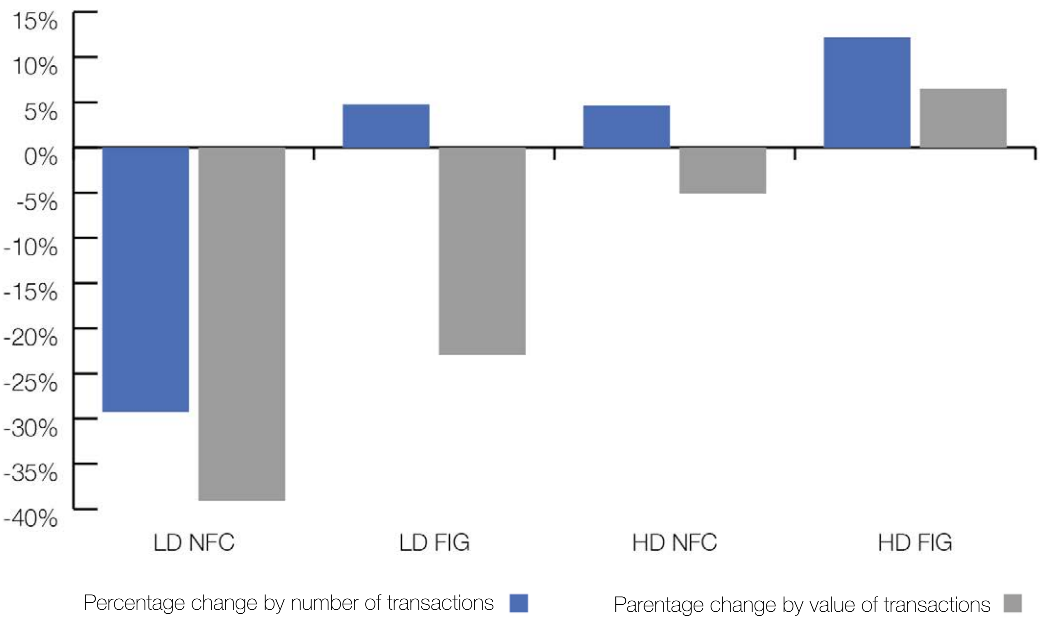
Practical experience of PRIIPs and PG – The PRIIPs regime is designed to enhance protection of retail investors participating in the structured products markets, while the PG regime imposes a type of suitability obligation on different market participants with respect to all products and investors. In this regard, the two regimes have significant problematic features that have led to unintended consequences and as well as raising concerns over the fundamental practicability of compliance.

Under PRIIPs, certain authorities have taken the position that the inclusion of a term or condition that deviates only slightly from what is regarded as a 'plain vanilla' bond will bring that security into scope as a 'packaged' product, requiring a KID to be produced. An example would be the inclusion of a 'make whole' provision. The fact that this and other terms can be to the benefit of investors but bring a bond within PRIIPs, combined with the fact that equities are not subject to the PRIIPs regime yet present greater risks to the retail investor, has led many to question the efficacy and rationality of the PRIIPs regime. Under PRIIPs, a KID must not only be accurate but may also be interpreted to require the inclusion of all material information. The imposition of this requirement with attendant issuer liability for both a three-page KID and a full 100+ page prospectus has not only created perplexity but more significantly led many issuers to refuse to produce a KID and instead restrict placement of newly issued bonds to non-retail investors in the EEA.

The PG regime has had similar consequences. It has effectively created an investor suitability obligation, not just at the point of sale (the approach taken in the past by regulation), but also imposing this obligation on issuers, underwriters, and secondary market sellers over the entire lifetime of the instrument. The practical burden of compliance with PG has caused many EU-originated issues to curtail altogether placement of bonds to retail investors.

In this respect, Figure 1 indicates a 30%-40% drop in low-denomination non-financial corporate (LD NFC) bond issuance for the first half of 2018 compared to the same period in 2017, which contrasts with the performance of high denomination (HD) and financial institution (FIG) issuance.

Figure 1 - 2018H1 vs 2017H1 percentage change in EUR benchmark issuance (by number and value of transactions)



Source: ICMA analysis using Dealogic data

Conclusion

While the goal of these primary market aspects of MiFID and PRIIPs is enhanced investor/consumer protection, it seems the impact has mainly been an increase in administrative burdens and a reduction in retail access to the bond markets. ICMA will continue to engage EU authorities and national competent authorities to better achieve desired regulatory outcomes while maintaining resilient and efficient markets.

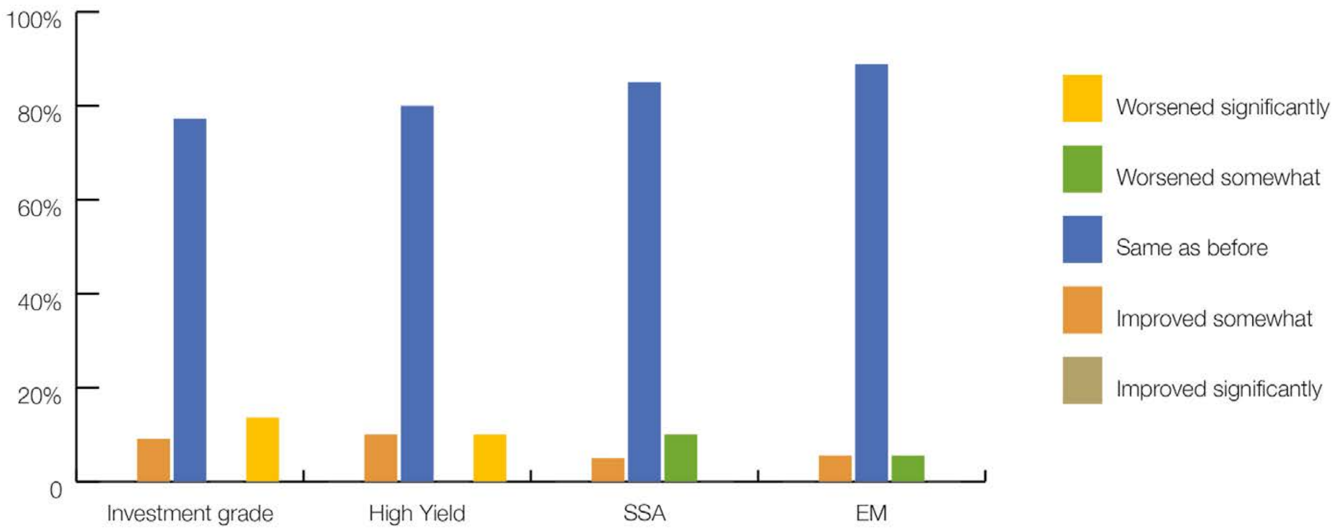
II. Secondary markets

37 member firms responded to the survey, of which 34 are MiFID regulated. 10 classify themselves as buy-side, 23 as sell-side (including 18 systematic internalisers for bonds), and 4 as regulated trading venues or 'platform providers'.

Market Liquidity

Q: Since MiFID II/R took effect on 3rd January 2018, how would you describe liquidity in fixed income markets, taking into consideration bid-ask spreads, time to execute, ticket size, and depth, inter alia?

Figure 2 - Bond market liquidity since January 2018

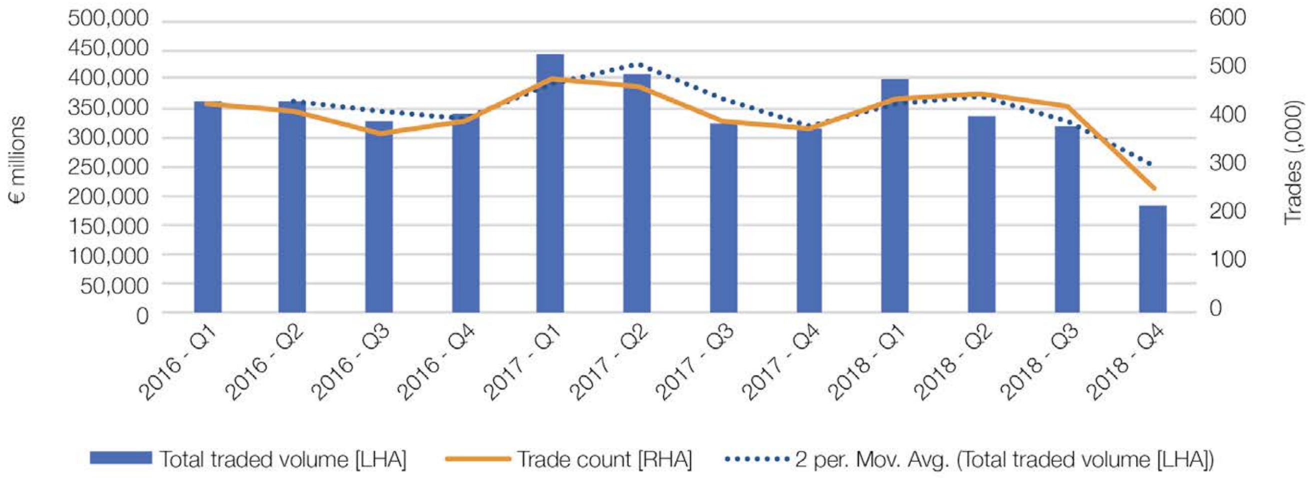


Responses to the survey seem to suggest that liquidity has remained largely unaffected across all bond asset classes. Where responses suggest some improvement or worsening, one cannot necessarily draw conclusions with respect to causality (e.g. market sentiment, ECB Asset Purchase Programme, etc. will also have impacted liquidity).

This would seem to be backed up by market data provided by Trax,[1] which shows that traded volumes (and trade count) in European IG credit, HY credit, and sovereign bond markets in 2018 are very much in line with 2017, with a small uptick in Q1 of 2018.

1 Trax Data from MarketAxess offers unique, timely insight into the European fixed income market. It combines voice and electronic traded flow, including price and volume data as well as regulatory reported information.

Figure 3 - IG Corporate bond trading volumes

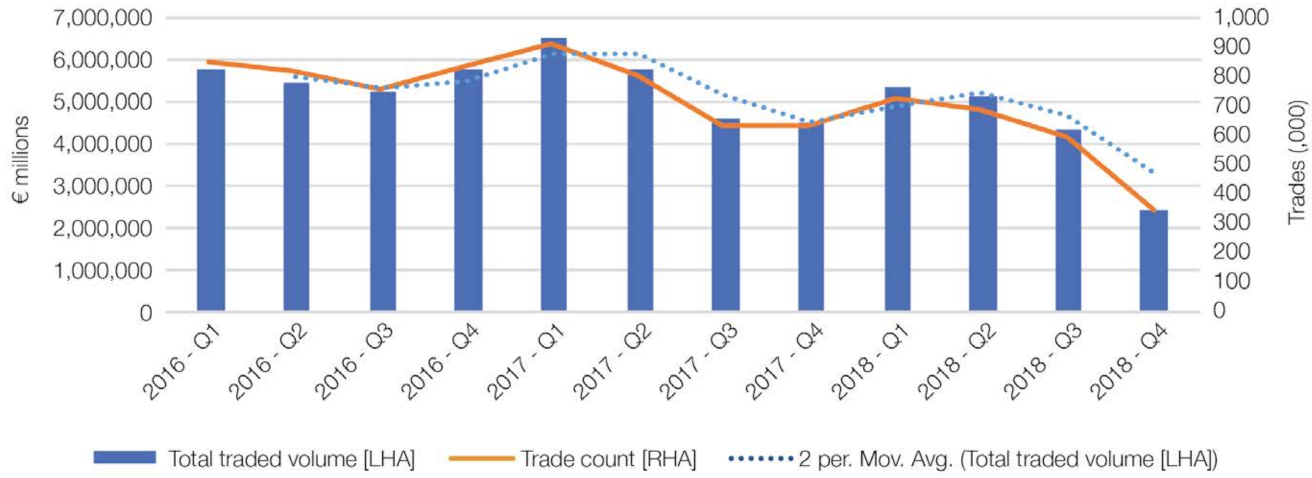


Source: ICMA analysis using Trax data (through November 13 2018)

Figure 4 - HY (NF) Corporate bond trading volumes

Source: ICMA analysis using Trax data (through November 13 2018)

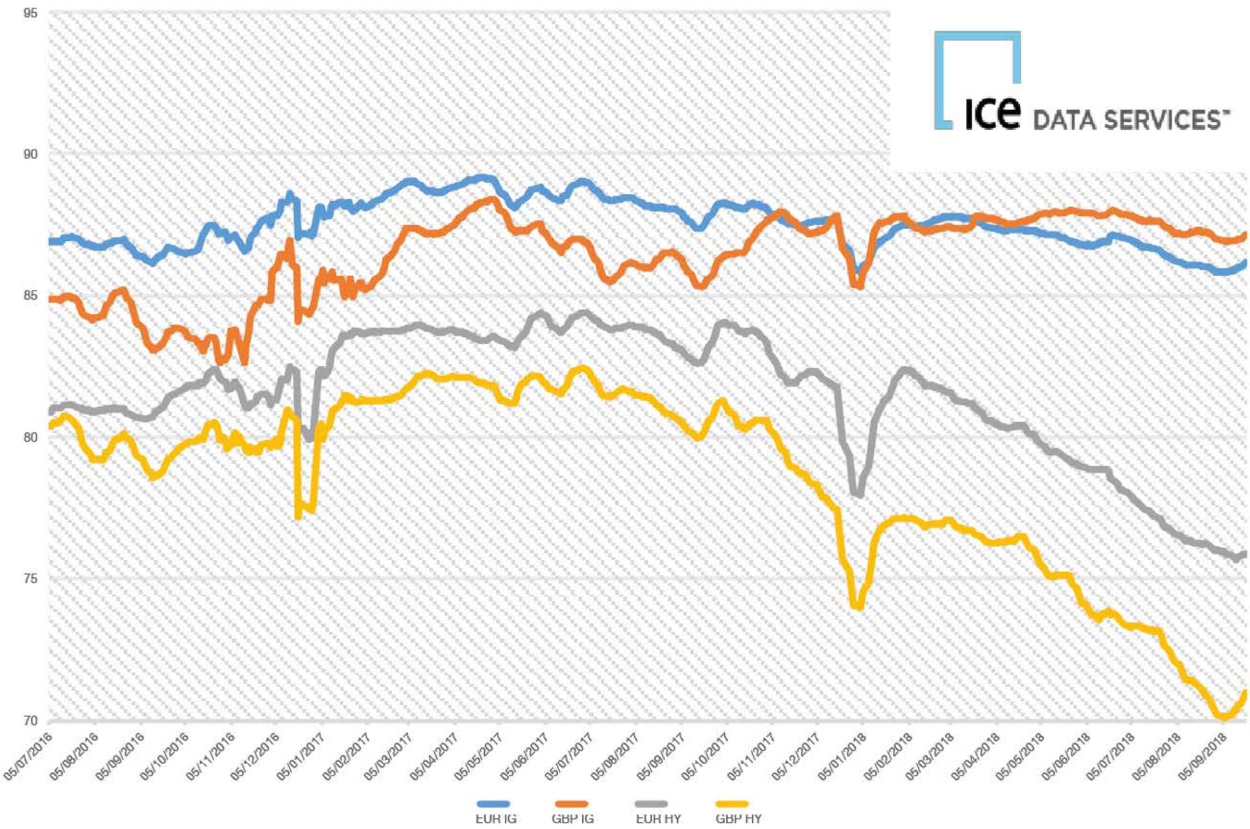
Figure 5 - Government & Sovereign bond trading volumes



Source: ICMA analysis using Trax data (through November 13 2018)

The ICE Data Services Corporate Bond Market Liquidity Tracker, which is prepared especially for ICMA and which employs statistical methods to measure liquidity dynamics[2] at the security level that are then aggregated at the portfolio level, suggest a sharp (largely seasonal) drop in liquidity over the 2017 year-end. Liquidity conditions for IG credit (both EUR and GBP) then appear to revert quickly to late 2017 levels and remain fairly constant through Q3 2018. The Trackers, however, suggests that HY market liquidity continues on a steady decline that began in Q3 of 2017.

Figure 6 - Liquidity Tracker



Source: The ICE Data Services Corporate Bond Market Liquidity Trackers

2 ICE Data Services incorporates a combination of publicly available data sets from trade repositories as well as proprietary and non-public sources of market colour and transactional data across global markets, along with evaluated pricing information and reference data to support statistical calibrations.

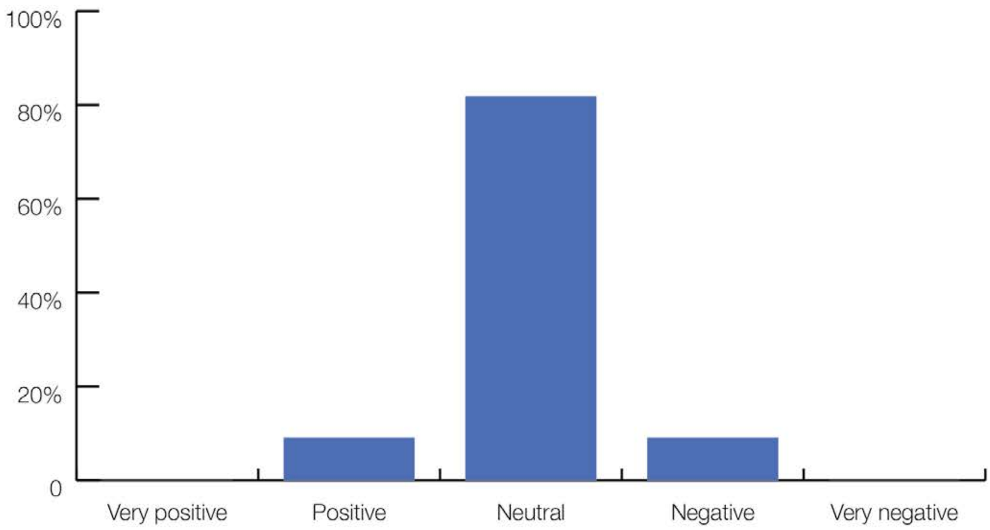
Transparency

While greater transparency is a key objective of the regulation, this very much seems to be work in progress as far as bond markets are concerned. Respondents suggest that, to date, post-trade transparency has not improved as a result of the regulation. This can partly be attributed to the challenge of accessing trade data (86% of respondents find it 'difficult' or 'very difficult') as well as to the quality of the data itself (73% of respondents believe that less than 10% of the available data is 'usable'). However, there seems to be a degree of optimism that in time the pre- and post-trade data will become more reliable; although, even by 2022, the expectations for the extent of usability seem to be mixed at best. It is perhaps no surprise that most respondents feel that price discovery is either the same or worse (90% of respondents) than pre-MiFID II/R.

Consistent with previous ICMA member feedback, the majority of respondents (86%) feel that a consolidated tape, provided as a utility (similar to TRACE in the US), would help to provide the level playing field that the regulation is intended to deliver.

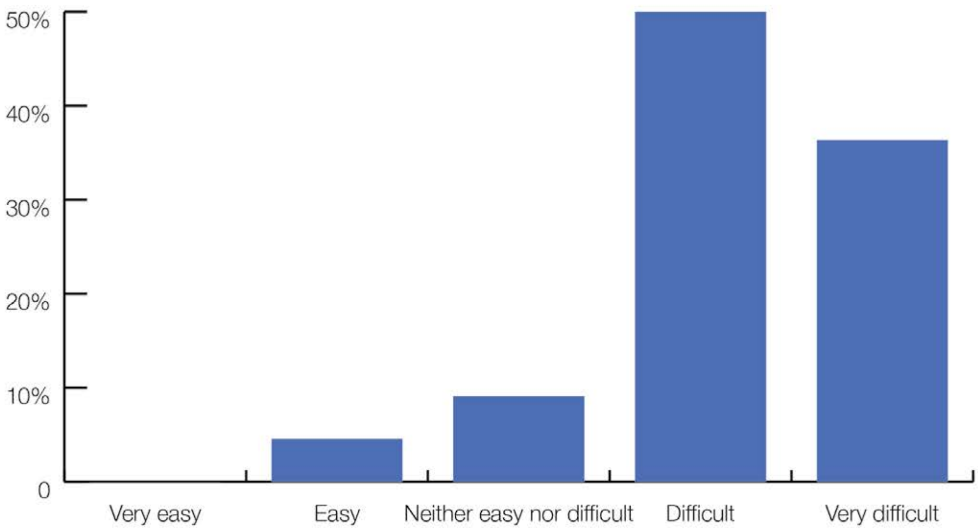
Q: How would you describe post-trade transparency in fixed income markets in comparison to a pre-MiFID II/R environment?

Figure 7 - Post-trade transparency post MiFID II/R



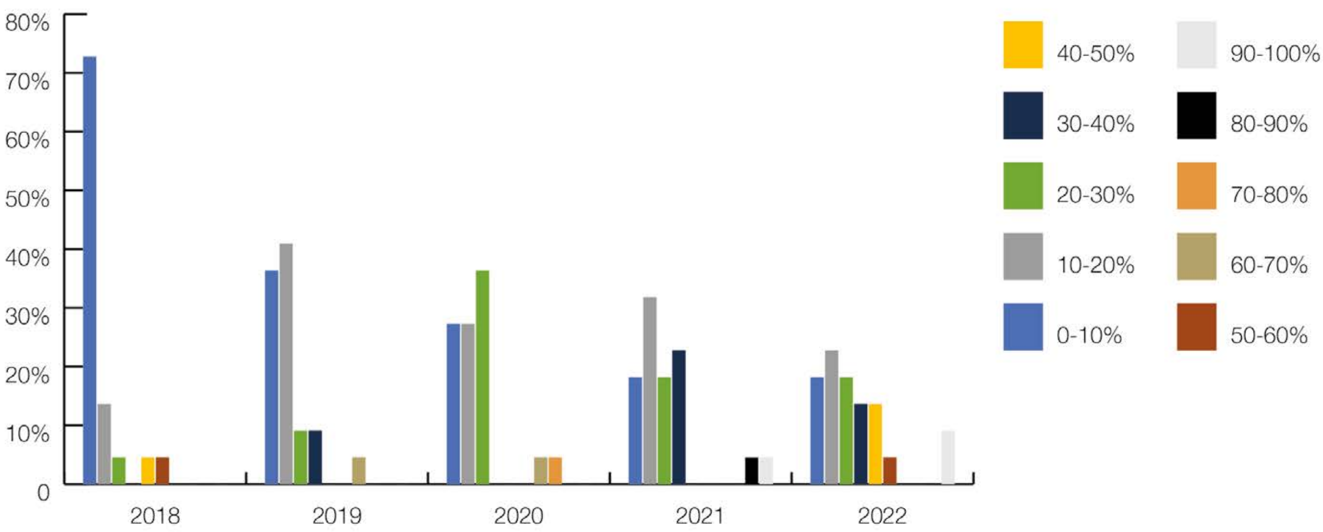
Q: How would you describe access to publicly available APA data (both data published in near-real time and after a deferral period)?

Figure 8 - Access to APA data



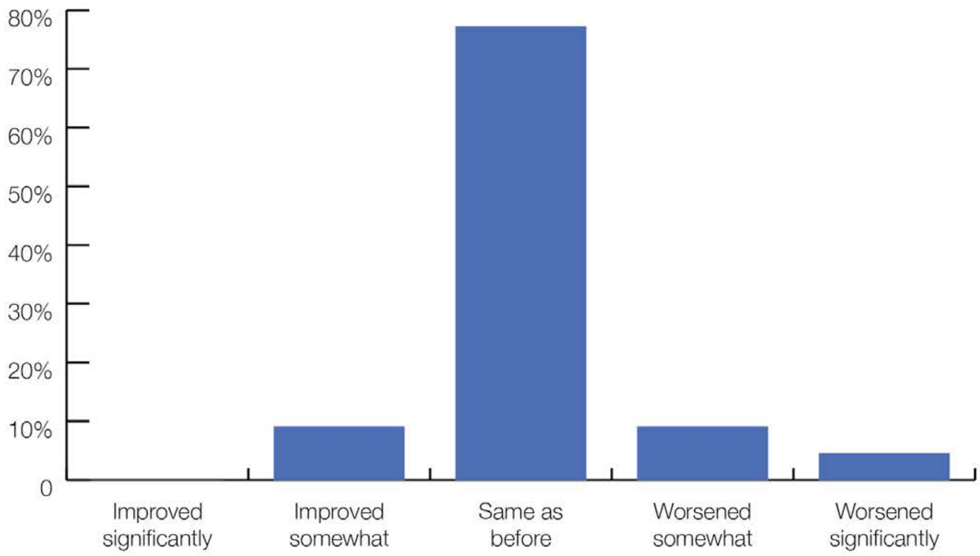
Q: What percentage of the publicly available transparency data under MiFID II/R (pre- and post-trade) would you consider to be usable, currently and in the future?

Figure 9 - % usable trade data



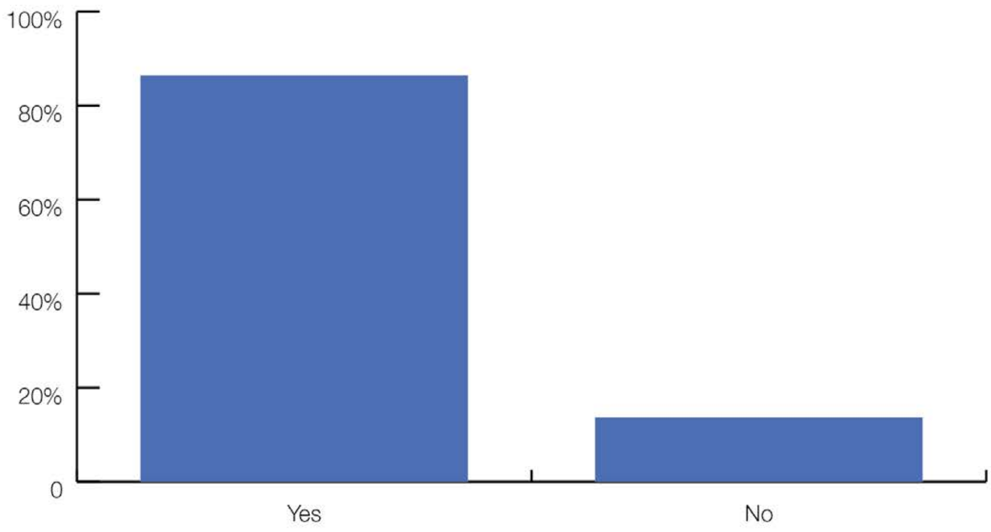
Q: How would you describe price discovery in fixed income markets in comparison to a pre-MiFID II/R environment?

Figure 10 - Price discovery post MiFID II/R



Q: Do you consider that a consolidated tape provider (CTP), in the form of a utility (for example, similar to the US Trade Reporting and Compliance Engine (TRACE)), would be beneficial for the industry and ensure a level playing field between market participants in terms of accessibility of transparency data?

Figure 11 - Would a utility CTP help to 'even the field'?

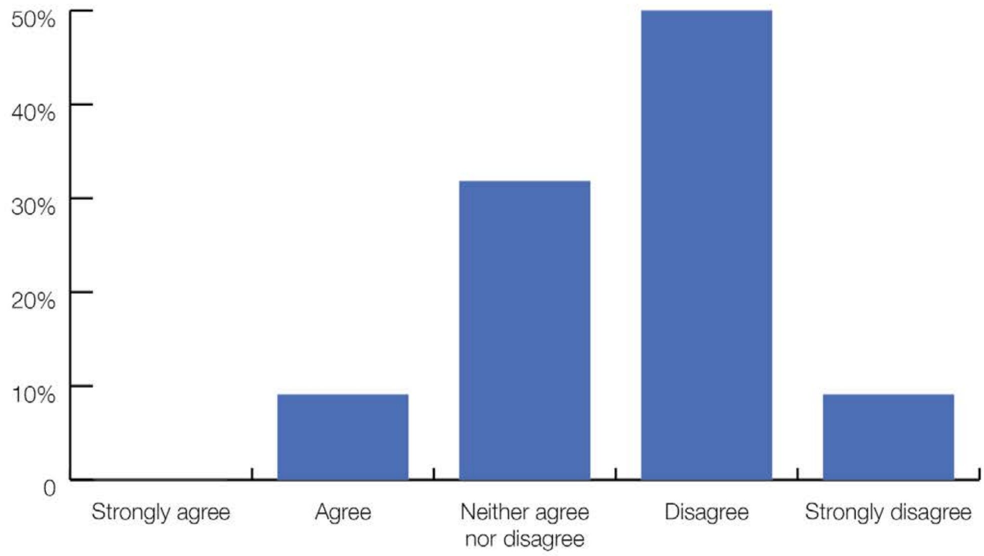


Introducing the systematic internaliser (SI) regime to fixed income is hoped to improve transparency in what has traditionally been an OTC market and so create a level playing field between on- and off-venue liquidity provision. Many firms opted-in to the regime from January 2018, and 18 of the 23 sell-side respondents to the survey identify themselves as SIs for bonds.

The feedback would seem to confirm that, so far at least, the SI regime has neither created a level playing field nor improved transparency. Comments further suggest that it has merely forced more trades that would otherwise be OTC onto venues, while creating an unlevel playing field with respect to transacting OTC in the EU versus non-EU. To the extent that trading with an SI is preferable, identifying which counterparties are SIs also appears to be challenging.

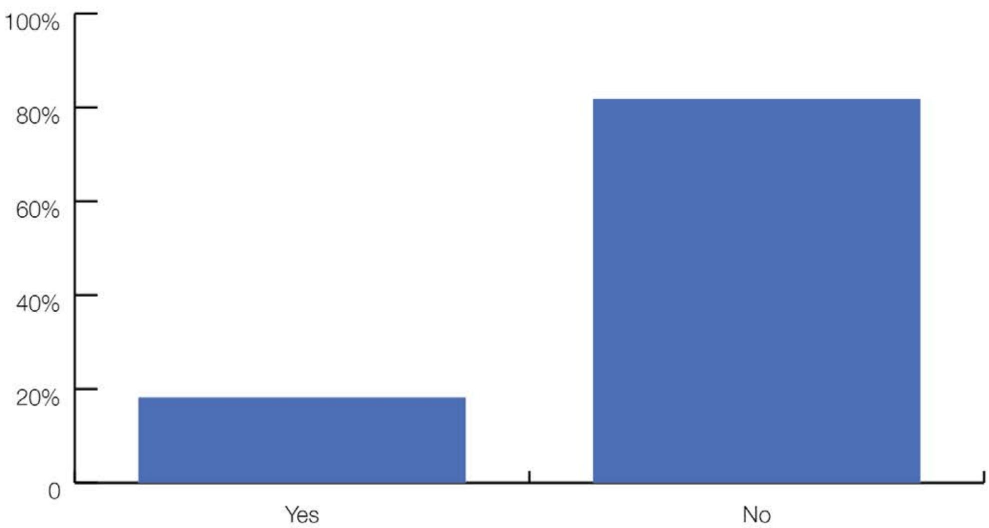
Q: One of the main objectives of MiFID II/R is to create a more 'level playing field' between trading venues on the one hand and market makers and other liquidity providers on the other. Do you agree that it is achieving this objective?

Figure 12 - The SI regime - creating a level playing field?



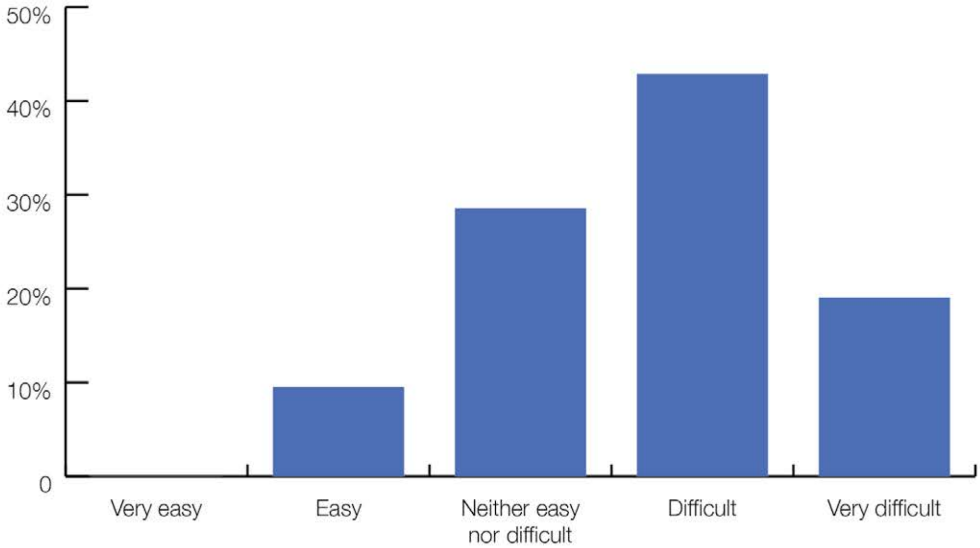
Q: In your view, has the SI regime improved transparency in fixed income markets?

Figure 13 - The SI regime - improving transparency?



Q: How would you describe the ease of identifying whether your counterparty is a Systematic Internaliser (SI)?

Figure 14 - Identifying SIs



Electronic trading

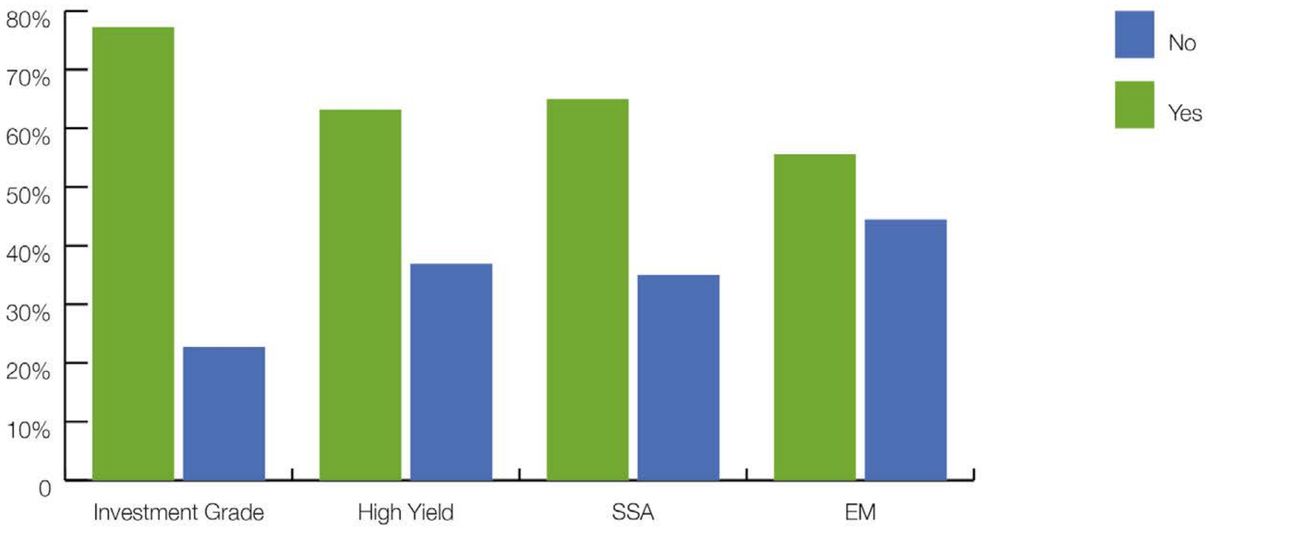
One of the objectives of MiFID II/R is to move trading in more traditional OTC asset classes (such as fixed income) onto regulated markets and trading venues. While European bond markets have been 'electronified' for more than two decades, with a growing propensity for both sell-side and buy-side to utilize the exponentially expanding choice of new trading venues and electronic protocols, the introduction of MiFID II/R seems to have provided this already well-established trend with a slight but discernible nudge.

The survey responses suggest that while the increase in electronic trading is not significant, it is prevalent (77% to 56% across bond asset classes) and perhaps more noticeable in the relatively more commoditized SSA and IG credit markets. What the comments (and the survey results, to an extent) do point to, however, is evidence of some firms opting to move most, if not all, of their trading onto venue (even in more traditionally OTC based markets, such as HY and EM).

It would further seem as if much of this incremental shift to more electronic trading is through the use of 'move to venue' protocols (sometimes referred to as 'processed trades'), whereby the original pre-trade negotiations take place off-venue (via messaging, 'chat', or over the phone), but the final execution takes place on-venue. Respondent comments suggest that 'move to venue' transactions are very much client driven, but also are by no means anything new.

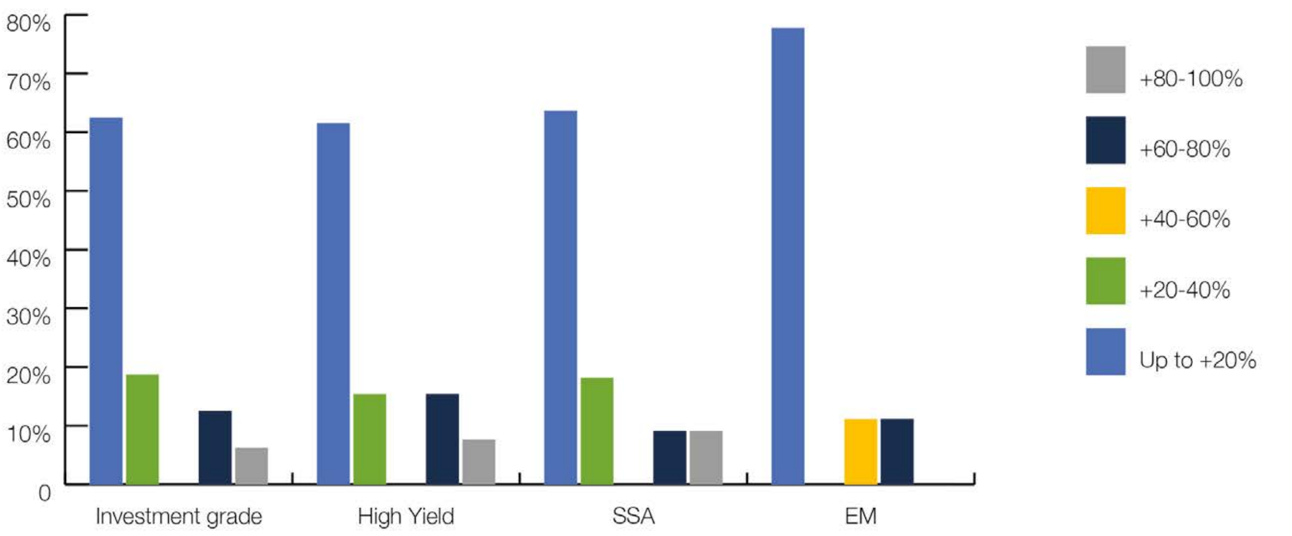
Q: Do you execute a larger share of your tradeflow electronically since MiFID II/R entered into force?

Figure 15 - Increase in electonic trading



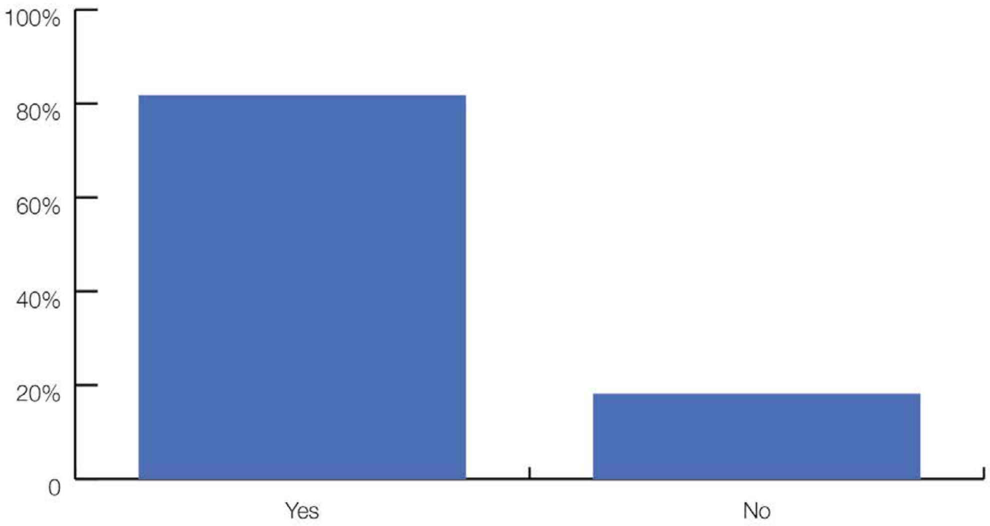
Q: If yes, how would you quantify the increase of electronic trading in comparison to OTC trading (year-on-year)?

Figure 16 - Quantifying increase in electronic trading



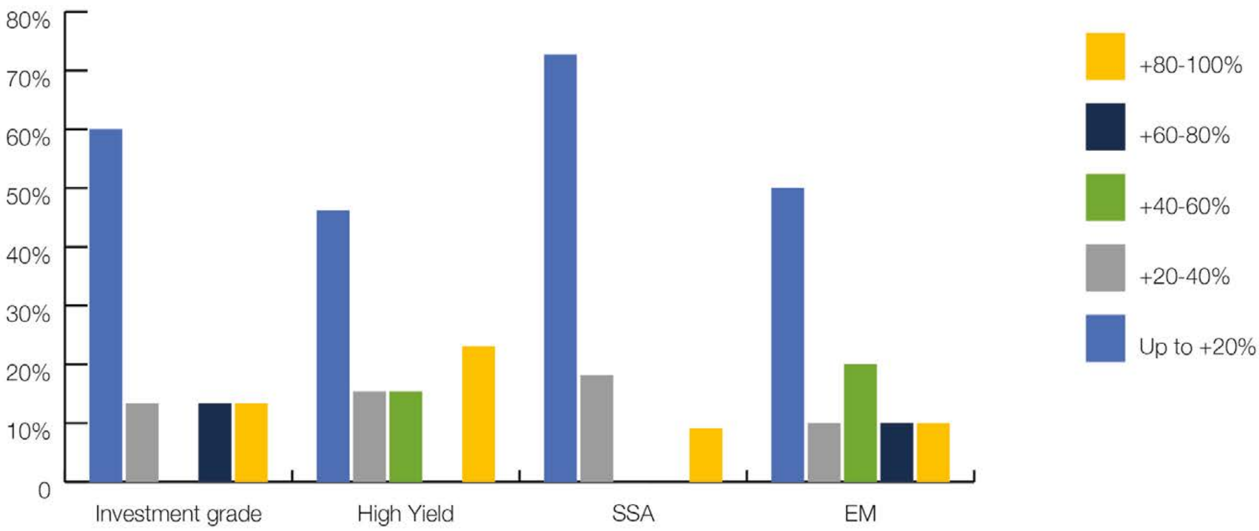
Q: 'Move-to-venue' (or 'processed') trades enable market participants to initiate a trade bilaterally, and formalise the transaction on-venue subject to the trading venue's rule book. Do you make use of this protocol?

Figure 17 - Use of 'move to venue' protocols



Q: If you answered 'Yes' in the previous question: How would you quantify the increased use of the 'move-to-venue' protocol in comparison to pre-MiFID II?

Figure 18 - Quantifying increase in electronic trading



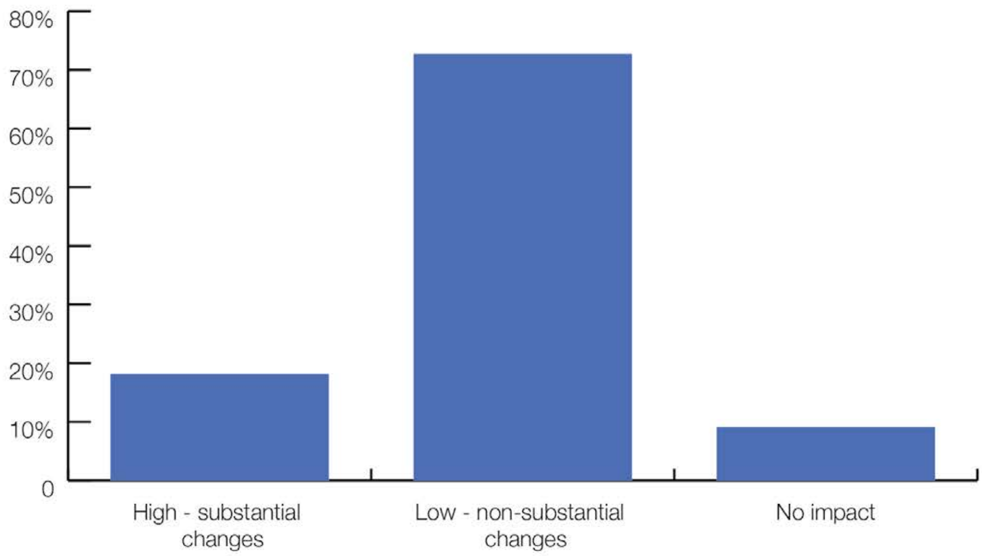
Best execution

The regulation requires investment firms to establish and implement an order execution policy, which must be disclosed to, and consented on by, the firm's clients. Trading venues, systematic internalisers, market makers, and other liquidity providers, are required to make data available to the public, on a regular basis, at no cost, on the quality of transaction execution. Best execution policies (including for fixed income) have existed long before MiFID II/R, while the extensive best execution related data public reporting obligations are not only a new requirement but would also seem to be of questionable value.

Survey responses confirm that firms already had in place robust best execution policies, communicated to clients, and that the regulation has not had any material impact on these (90%). The data (and comments) further confirm that the best execution data reporting requirements (under RTS 27 and 28) are challenging, time and resource draining, and of little or no value (95%). It would further seem that the most interest in the best execution data comes from competitors and journalists – not from clients, for whom it is intended.[3]

Q: How would you describe the impact of MiFID II/R best execution requirements on your trade execution process in comparison to a pre-MiFID II/R environment?

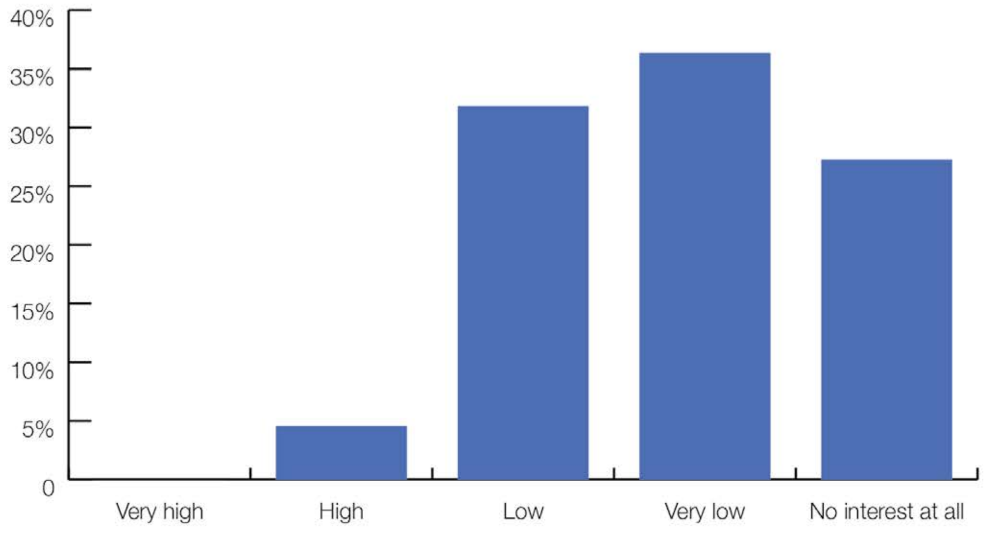
Figure 19 - Impact on existing 'best ex' process



3 Firms are able to see who downloads their RTS 27 & 28 reporting data files

Q: How would you describe interest in viewing the RTS 27/RTS 28 reports published by your firm?

Figure 20 - Interest in public 'best ex' reports



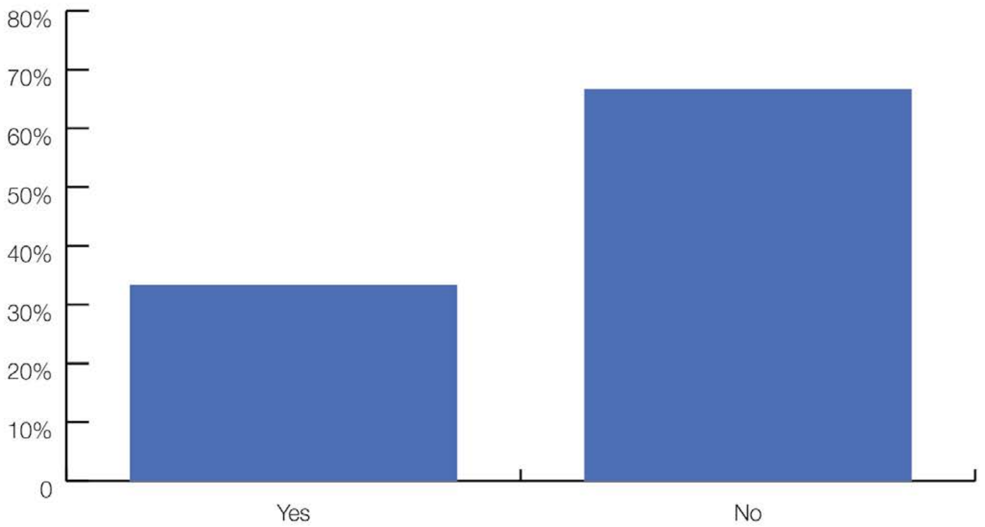
Extraterritorial impacts

In the lead-up to January 2018, ICMA, as well as other global associations, had relayed a number of concerns related to the extraterritorial implications of MiFID II/R, in particular the requirement for entities (issuers and trading parties) to provide legal entity identifiers (LEIs), detailed (even personal) information necessary to meet transaction obligations, as well as confusion over reporting and transparency responsibilities.

The survey suggests that many of these fears have been allayed, and that mostly (67%) business with non-EU/EEA firms has not been negatively impacted. However, the comments highlight issues with non-equivalent reporting regimes, as well as the fact that where market liquidity is available outside of the EU, this will be preferable for non-EU clients.

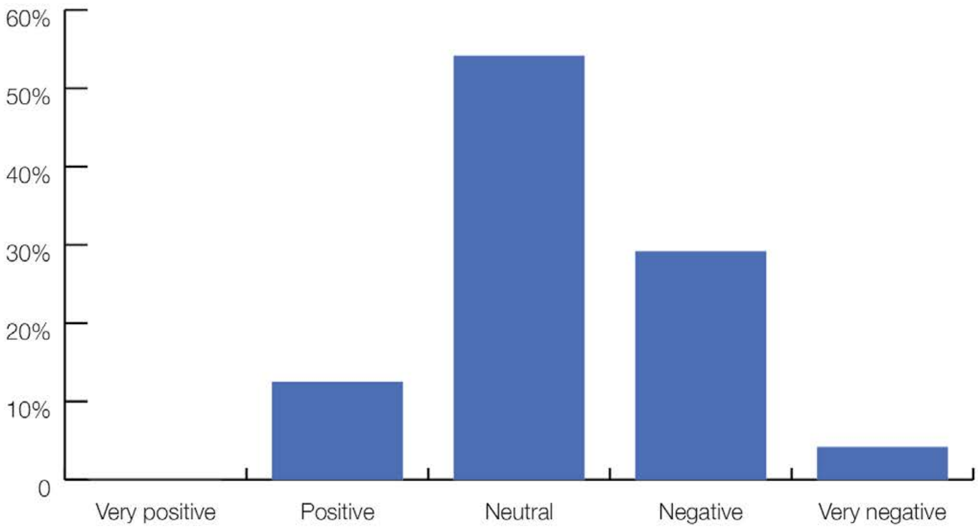
Q: Extraterritoriality: Are you experiencing outside the EU/EAA clients choosing to not trade with your (EU/EEA) firm platform due to MiFID II/R transparency rules, eg in Asia?

Figure 21 - Are non-EU/EEA firms avoiding trading with MiFID regulated firms?



Q: In your opinion, how would you describe the overall impact of MiFID II/R on cross-border fixed income markets?

Figure 22 - Impact on cross-border fixed income markets?

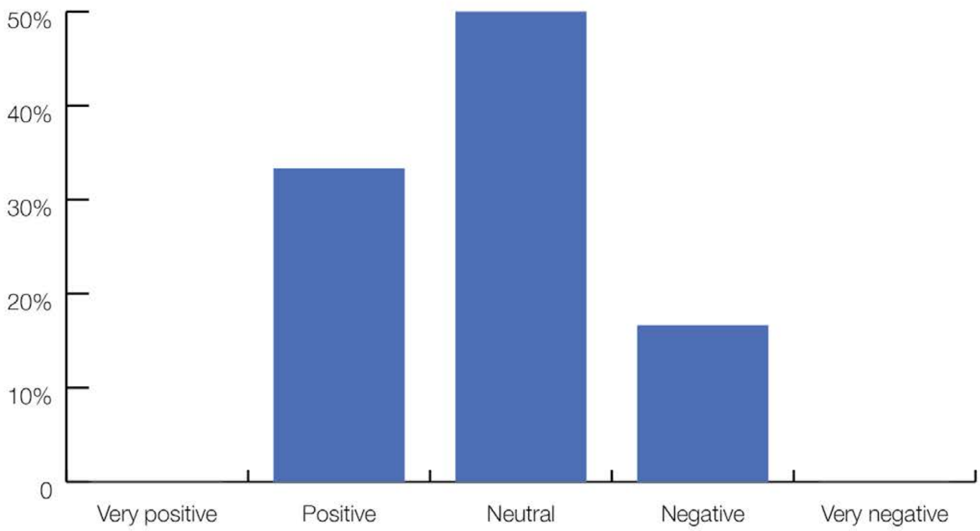


Regulatory guidance

Given the complexities and ambiguities involved in complying with such a regulatory juggernaut as MiFID II/R, firms (and their representative bodies) naturally looked to their local regulatory bodies, as well as to ESMA, for guidance in the lead-up to January 2018. While it is impossible to extrapolate form the survey the degree to which firms actively engaged regulators (whether directly or through their various representative bodies), the overriding perception on regulatory guidance is that it has been marginally positive for some, (33% for NCAs[4] and 17% for ESMA), but mostly neutral (50% NCAs, 58% ESMA) to negative (17% NCAs, 25% ESMA).

Q: From your perspective, how would you describe the guidance you received from your national regulator with respect to MiFID II/R?

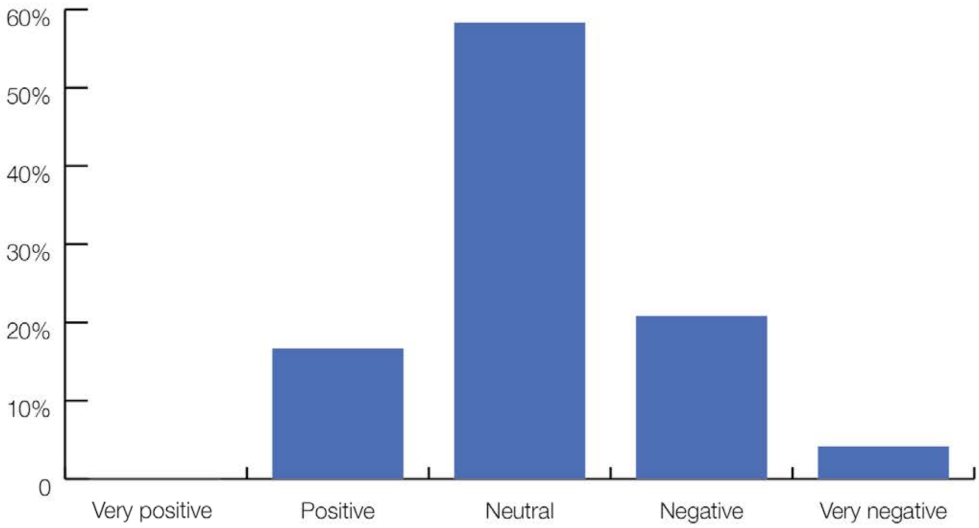
Figure 23 - Guidance from local NCAs



4 The respondents to this survey are regulated across 9 different EU jurisdictions and 2 non-EU. In many cases firms have more than one jurisdictional regulator.

Q: From your perspective, how would you describe the guidance you received from ESMA with respect to MiFID II/R?

Figure 24 - Guidance from ESMA

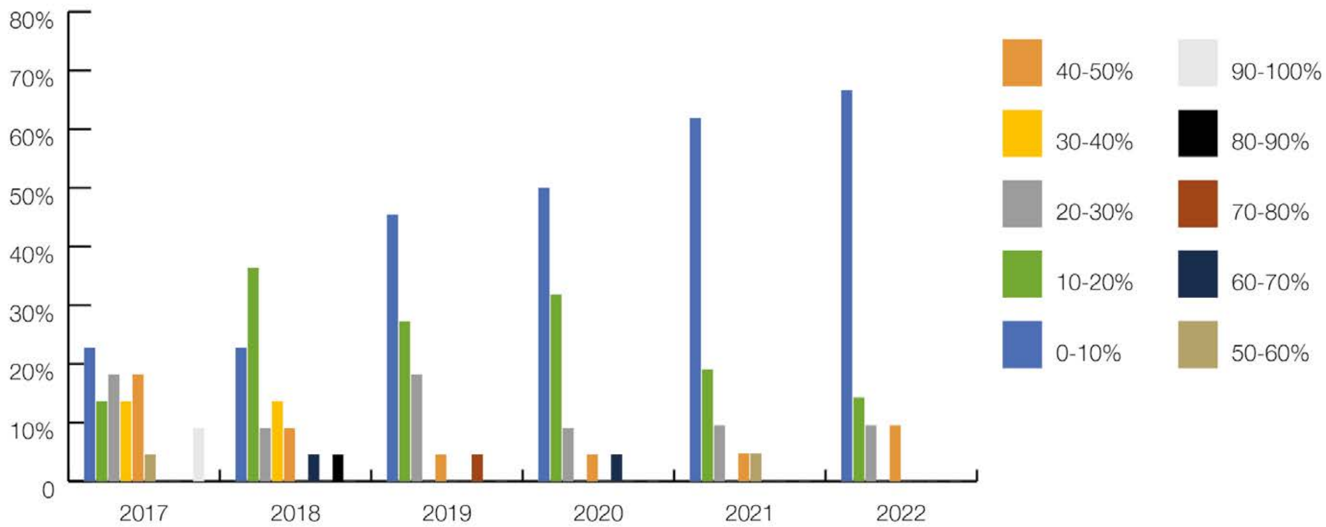


Cost

Respondents confirm that implementing MiFID II/R has been an expensive exercise. While comments suggest that trying to disentangle specific implementation costs from firms' overall IT budget is difficult, estimates indicate that for 2017 and 2018, in most cases, it was a significant proportion. Again, acknowledging the challenge of isolating specific cost allocation, the bulk of the spend appears to be related to complying with the various transparency obligations. While these costs appear likely to continue, the expectation seems to be that in the near term they will reduce as a share of firms' overall IT budget.

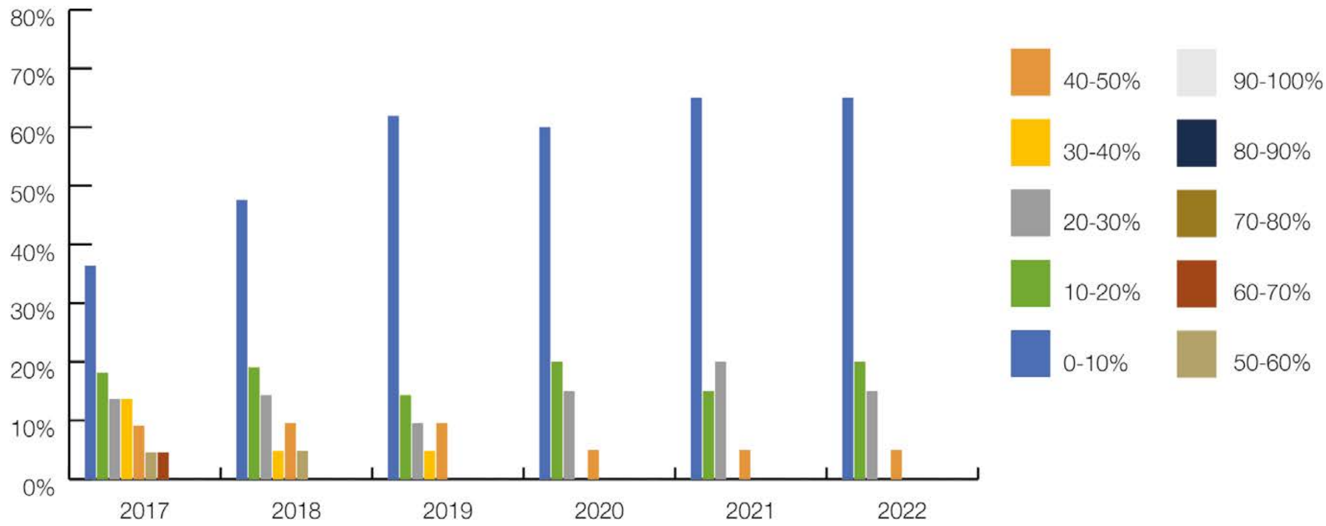
Q: What percentage of your firm's overall IT budget has been / will be allocated to MiFID II/R?

Figure 25 - % of IT budget allocated to MiFID



Q: What percentage of your firm's MiFID II/R budget was allocated to MiFID II/R transparency reporting purposes?

Figure 26 - % of budget allocated to MiFID II/R transparency reporting



Comments

Respondents also provided a range of comments with respect to their overall experience of MiFID II/R implementation from a secondary market perspective:

"Greater transparency in fees"

"Too expensive to implement."

"Retail investors informed better and execution is better for them."

"Too cumbersome and doesn't address the real issue which is the primary market structure and the ability to obtain data from trading venues."

"Building blocks for improved transparency in the future."

"Too many waivers and deferrals inhibiting true transparency."

"Prompted us to undertake more rigorous post trade execution quality reviews."

"No actual impact, just adding costs to the organization."

"Maybe the data will become useful in the future but nothing at the moment."

"Killed liquidity totally and there are no winners at all."

"Will force more people onto electronic platforms and encourage more buy side to buy side trading."

"Cost of implementation was large compared to negligible market change."

"Limited value pre and post trade transparency."

"Pushed trade efficiencies forward, embracing electronification of process. All to all more acceptable to some."

"Mostly the impact was neutral to detrimental. Mostly neutral."

III. Research unbundling[5]

Introduction

In October 2018, the Asset Management and Investors Council (AMIC), ICMA's buy-side committee, issued its second FICC Research Unbundling Survey.

The purpose of the survey is to help improve market clarity on this topic, identify remaining challenges, difficulties and outstanding issues in the implementation of the new MiFID II research rules and to establish progress compared to the first survey issued in 2017.

This survey is aimed at buy-side firms and focused on FICC research only.

27 firms responded to this survey.

In respect of types of firms, respondents classify as:

- 93% asset managers or investment funds; and
- 7% private banks.

In terms of AUM (expressed in USD) respondents are:

- 64% above $100bn;
- 21% between $10bn and $100bn;
- 11% between $1bn and $10bn; and
- 4% below $1bn.

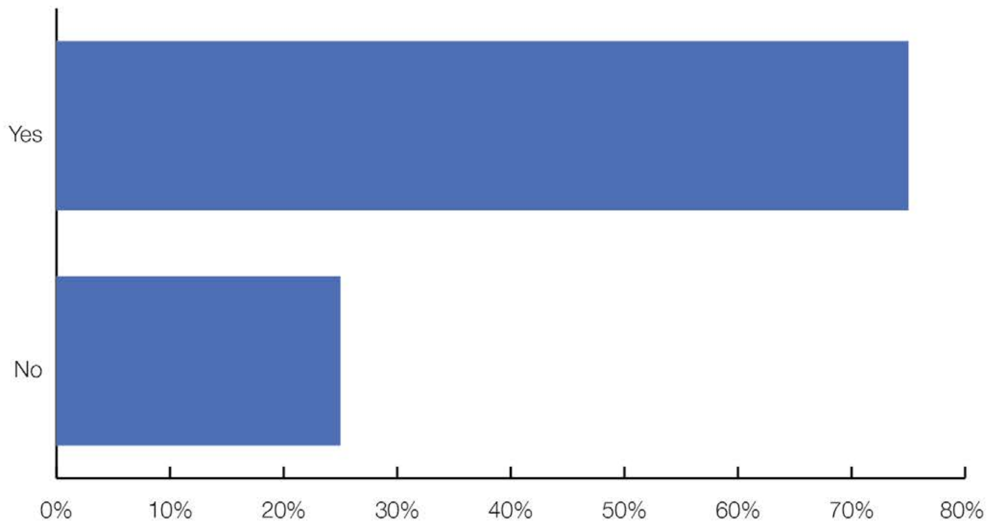
Geographically, the majority of respondents were based in the UK (39%) and Germany (21%). The remainder were from France, Switzerland, the Netherlands and other countries within the EU.

Deciding what is research

The majority of firms (75%) said that they have found it difficult to decide what research needs to be paid for and what can be classified as minor-non monetary benefits (MNMB) for which payment is not required.

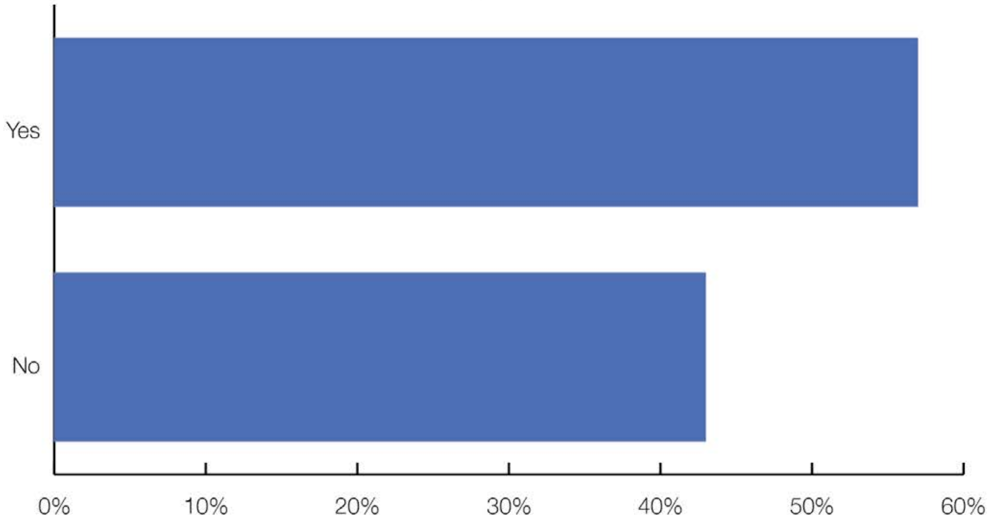
43% of the firms surveyed said that they have not received enough guidance from their national regulator or ESMA about the implementation of research unbundling for FICC research. This is down from 52% in November last year.

Figure 27 - Does your firm find it difficult to decide what research needs to be paid for and what can be classified as MNMB?



5 This section is extracted from the ICMA Asset Management and Investors Council (AMIC) FICC Research Unbundling Survey, published in November 2018.

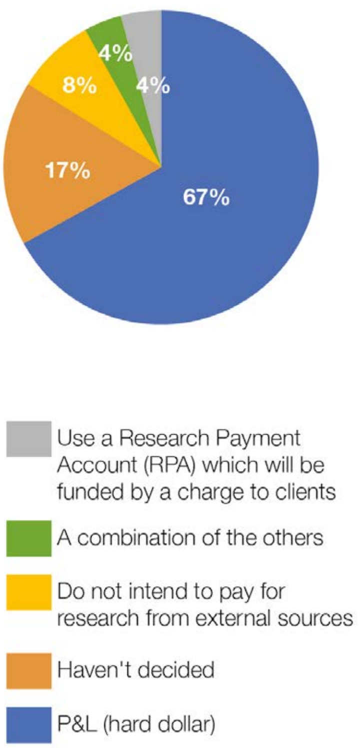
Figure 28 - Do you consider you have received enough guidance from the national regulators and ESMA on how to apply the new research rules?



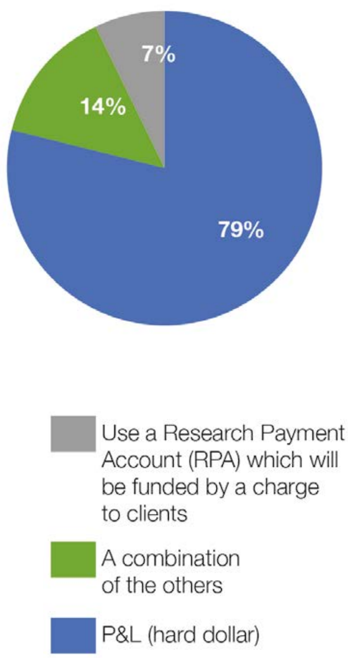
Payment for research

In line with recent market developments, the majority of asset managers intend to pay for research themselves. 79% of firms pay for FICC Research using their P&L, up from 67% last year. 7% intend to use an RPA funded by charge to clients, up from 4% last year and 14% intend to use a combination of the above, which is up from 4% last year.

Figure 29 - November 2017



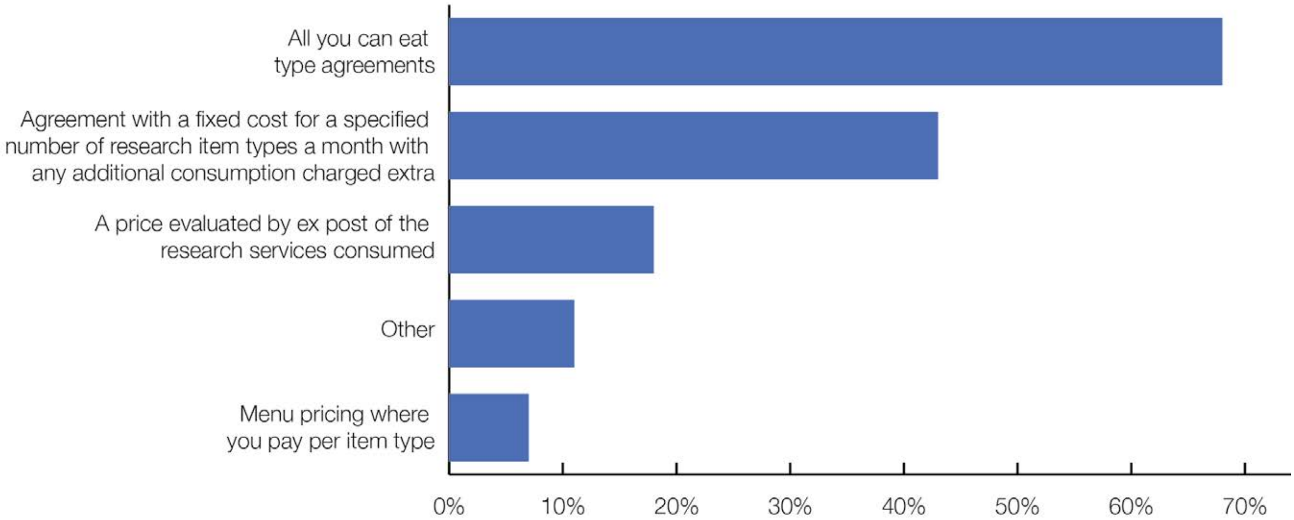
November 2018



Preferred type of research consumption

Firm preferences for type of research show most preferring 'all you can eat' type research agreements (68%) closely followed by agreements with a fixed cost but where additional consumption is charged (43%).

Figure 30 - What kind of research consumption has your firm signed up for:



Overall independent research providers do seem to get a larger slice out of the shrinking pie, which is in line with our survey results from 2017.

Figure 31 - All research providers

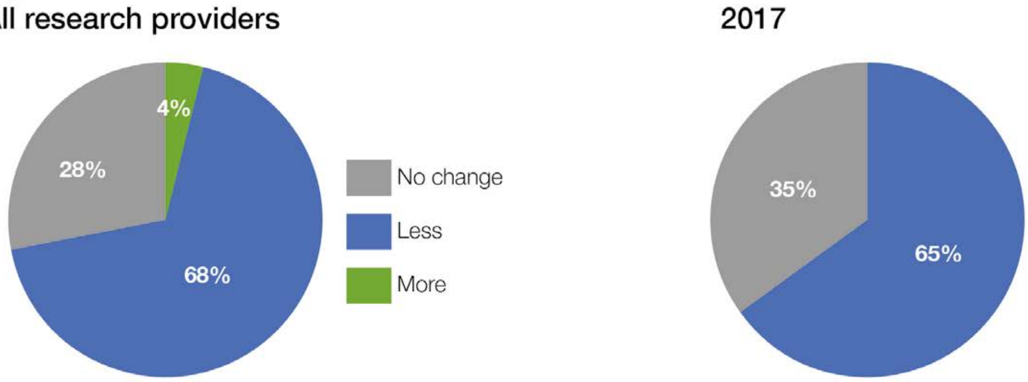


Figure 32 - Banks/brokers

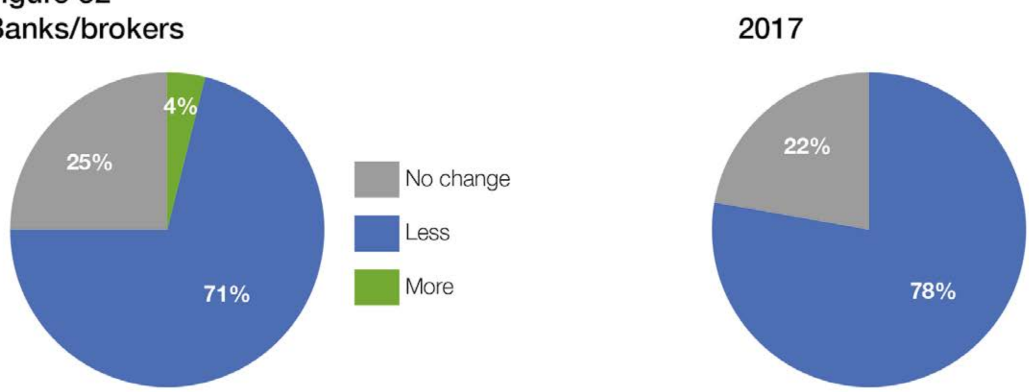
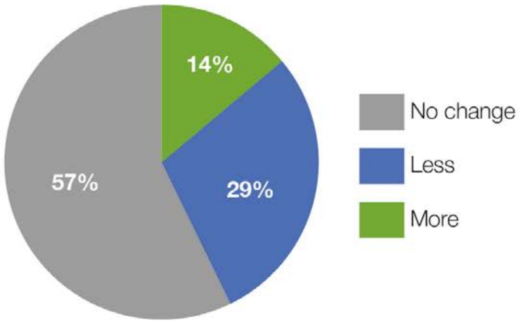
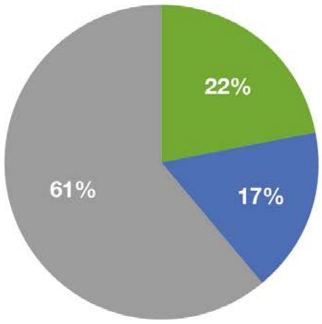


Figure 33 -
Independent research providers



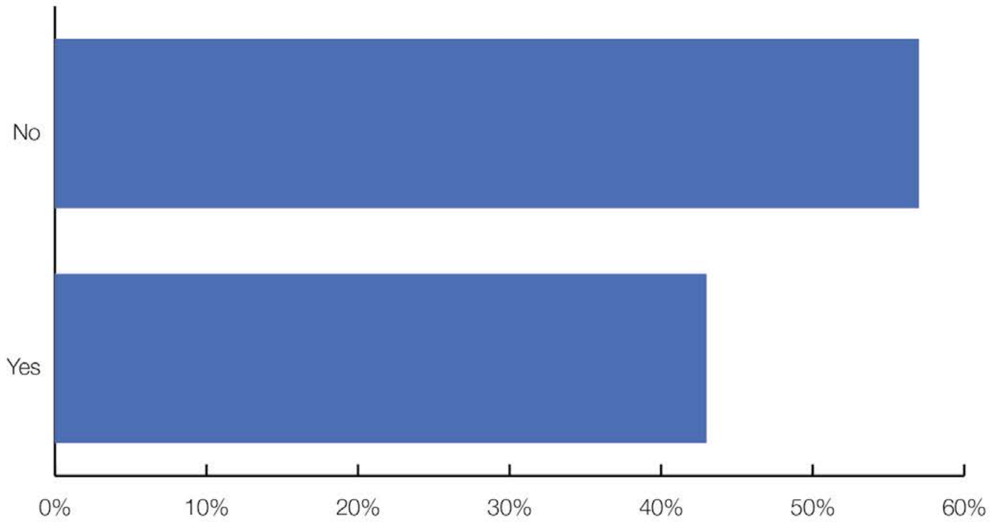
2017



Availability and breadth of SME FICC research

While a majority of the respondents who answered this question (57%) said that they have not noticed a decrease in the availability of SME FICC research, it is interesting that less than a year after implementation 43% said they have noticed a decrease. We expect this trend to continue as the reforms bed down.

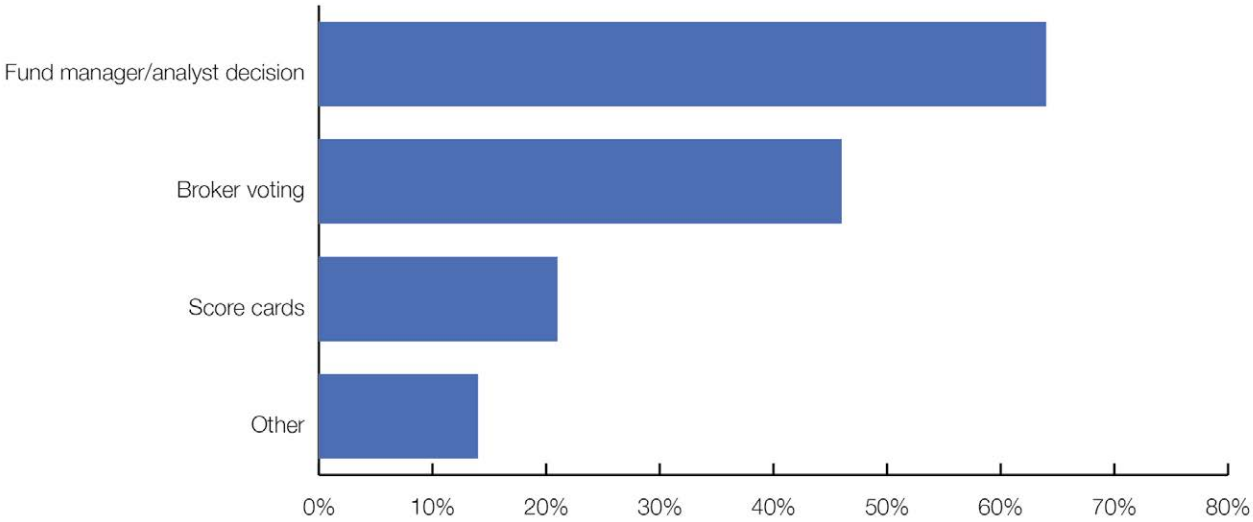
Figure 34 - Have you noticed a decrease in the availability and breadth of FICC research for SMEs?



Establishing the value of research

The majority of respondents (64%) said that the fund managers and analysts have a big say in deciding the value of research, with broker voting also being used by 46% of respondents.

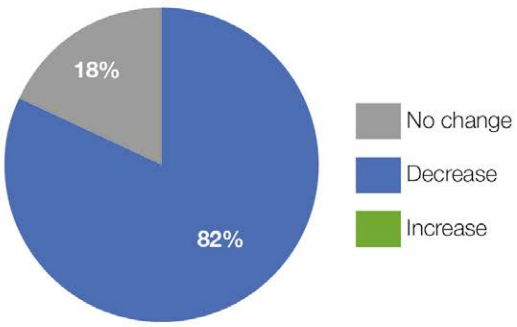
Figure 35 - How does your firm establish value of research and how it meets the objectives of the funds?



Changes in the number of FICC research providers

As expected, the majority of respondents (82%) said that they are using a smaller number of research providers, with the remainder (18%) noting no change. This is very much in line with last year's survey where 83% of respondents expected to use a smaller number of providers and 13% expected no change.

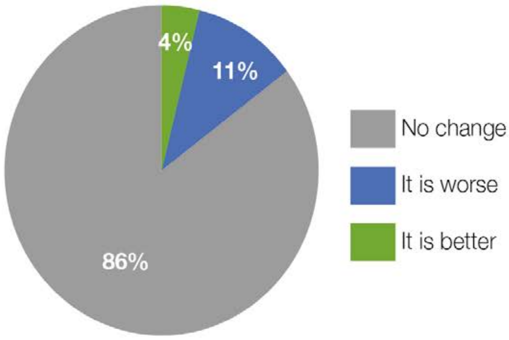
Figure 36 - How has the number of providers whose FICC research you consume changed?



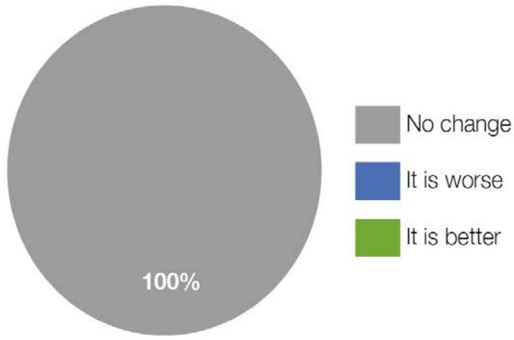
Quality of FICC research

The vast majority of respondents said that the quality of FICC research has not changed, with 86% in respect of research from banks/brokers and 100% for independent research providers. Only a few believe the quality of FICC research from banks improved (4%). This shows a significant shift from last year's expectations, where 32% participants said they believe research will get worse, while 14% said they believe it will get better.

Figure 37 -
Banks/brokers



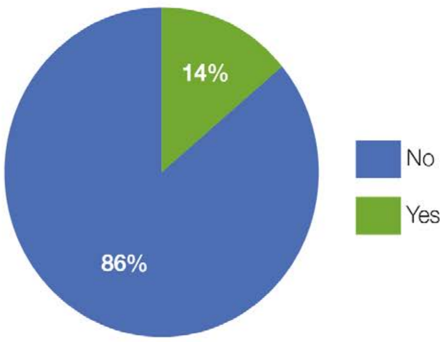
Independent research providers



Impact on fund performance

The majority of asset managers are confident that the reduction in the number of FICC research providers does not have a negative impact on their funds' performance. 86% of respondents said they are not concerned about this scenario, showing a potential oversupply of research.

Figure 38 - Are you concerned that the reduction in the number of FICC research providers used has had or will have a negative impact on fund performance?

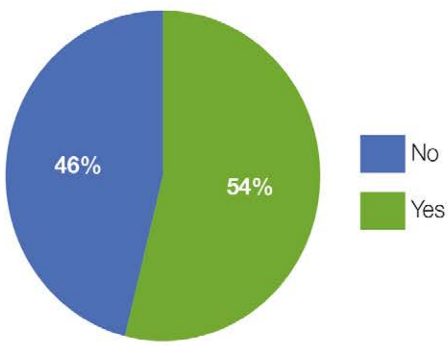


Attitude to investor roadshows

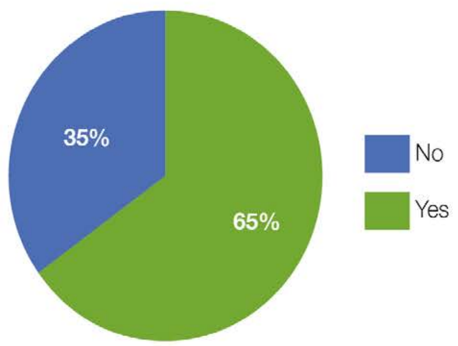
The majority of respondents (54%) said they have changed their attitude to and participation in investor roadshows as a result of the new rules, while 46% said they have not.

The majority of respondents who answered yes above, also said that the reason for the change relates to difficulties in deciding which type of roadshows can be considered minor non-monetary benefits and which should be paid for (65%), while 35% said their change in attitude is due to other reasons.

Figure 39 - Since the MiFID II rules came into effect, has your attitude to/participation in investor roadshows changed?



Does this change relate to difficulties in deciding which type of roadshows are MNMB and which should be paid for?

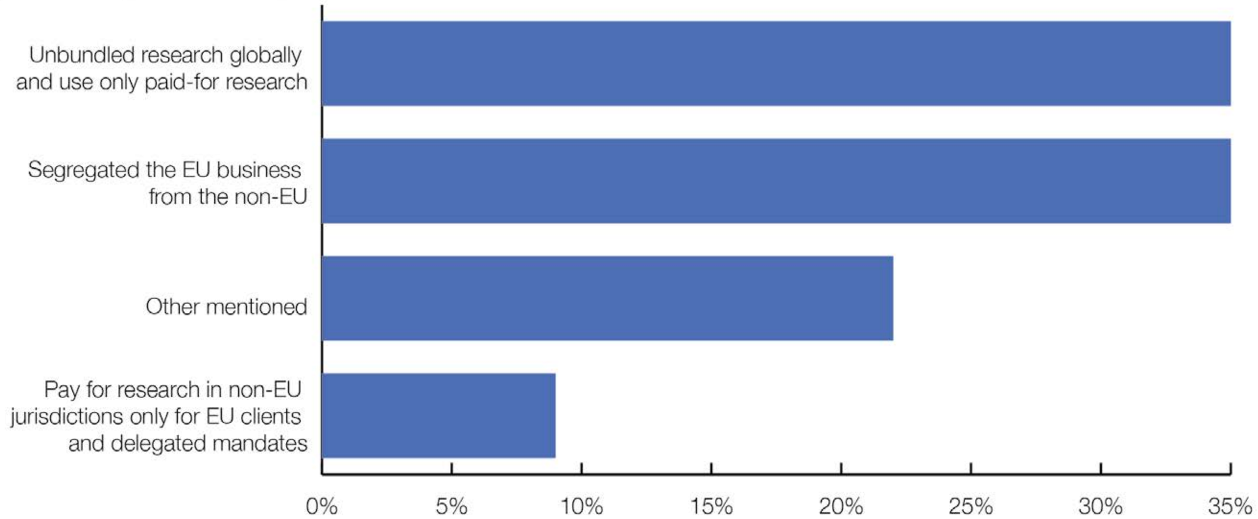


Approach to conflicting rules on non-EU FICC research

Respondents' approach to tackling the conflicting rules around FICC research globally seems to be equally split between unbundling research fees globally (35%) and segregating the EU and non-EU businesses (35%).

Our 2017 survey showed that the majority, 64% of firms, were planning to unbundle globally and only 7% of firms were planning to segregate EU and non-EU businesses. The significant change in firm attitude to the business segregation model may reflect that the costs and complexities of segregating their businesses geographically outweigh the costs and complexities that come from unbundling globally.

Figure 40 - If your firm has activities outside the EU, how have you tackled the potentially conflicting rules on research?



Comments

Many provided us with very helpful additional comments on the emerging market for unbundled FICC research which we want to take the opportunity to reproduce below:

"Paying for research has increased the total cost for clients and for our company as it did not change the spreads."

"The price discovery process in FICC is much more immature in comparison with the equity research market."

"Lack of clarity from the regulator from a FICC perspective has made valuation non uniform across the industry."

"Clearly a developing market. No standardised value proposition across sell-side firms, and a big discrepancy in rates versus quality. This will adjust over time as buy-side firms more deeply assess the quality of what they are paying for and make cuts where this is misaligned. Also, as firms are continually squeezed on management fees, they may face downward pressure to trim the research budget - I believe there is still significant room to consolidate."

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