Secondary Market Practices Committee

Meeting of the ICMA SMPC, June 16th, 2020

The meeting was held virtually, hosted by Barclays, and chaired by David Camara (Goldman Sachs) and Yann Couellan (BNP Paribas AM)

Attendees (accepted)

David Camara	Goldman Sachs	(Co-chair)
Yann Couellan	BNP Paribas AM	(Co-chair)
Ruud Teeuwen	ABN Amro	
Kevin Rauseo	AQR	
Lee Sanders	AXA IM	
Gherardo Lenti	Banca IMI	
Umberto Menconi	Banca IMI	
Elyas Galou	Bank of America	
Aalok Gupta	Bank of America	
Colin Cooke	Barclays	
Andrew Dowsett	Barclays	
Chloe Griffiths	Barclays	
Arran Rowsell	BGC Partners	
Sander Schol	BGC Partners	
Andy Sinfield	BGC Partners	
Vasililki Pachatouridi	Blackrock	
Jennie White	Blackrock	
Andrei Serjantov	BNP Paribas	
MartinaBen-Shaul	CIBC	
Silas Findley	Citi	
Philippe Perot	Citi	
Chris Orr	Credit Suisse	
Richard Glen	Deutsche Boerse	
Alexandre Rogues	Deutsche Boerse	
Marco Ferrari	EFG Bank	
Goran Hoblaj	ERSTE Group	
Eric Heleine	Groupama AM	
Luca Rizzo	Groupama AM	
Sara Benjamin	ING	
Stephane Malrait	ING	
Barbara Zittucro	Intesa San Paolo	
Claire Davis	JP Morgan	
Kate Finlayson	JP Morgan	
Paul Glasgow	JP Morgan	
Claudia Gonzalez Cabanillas	JP Morgan	
Antony Baldwin	LCH Limited	

Angela Lobo	Morgan Stanley	
Philip Read	National Australia Bank Ltd	
Rahni Soliman	National Australia Bank Ltd	
Hakan Guney	Nomura	
Daniel Middleton	Oppenheimer Europe Ltd	
Mark Rowe	RBC CM	
Janet Wilkinson	RBC CM	
Vincent Grandjean	Santander	
Ricardo Goddard	Schroders	
Paula Alves	Société Générale	
Sylvie Bonduelle	Société Générale	
Mathieu Casadevall	Société Générale	
Louise Drummond	Standard Life Investments Ltd	
Johan Wijkstrom	Swedbank	
Neil Treloar	Tradition	
Christoph Hock	Union Investment	
William Martin	Westpac	
Zameer Mukhida	Westpac	
Liz Callaghan	ICMA	
Gabriel Callsen	ICMA	
Arthur Carabia	ICMA	
Godfried De Vidts	ICMA	
Lee Goss	ICMA	
Andy Hill	ICMA	(Secretary)
Rene Karsenti	ICMA	
Paul Richards	ICMA	
Martin Scheck	ICMA	
Rowan Varrall	ICMA	

Minutes

The Co-chairs thanked everybody for joining remotely in what was now becoming the 'new normal' for meetings. Since the last meeting in March we had seen, at least for recent times, unprecedent volatility and dislocations in the European bond markets. However, the market adapted quickly to working remotely, while central bank intervention had been critical in stabilizing markets and restoring investor confidence. The SMPC was therefore grateful that Liz Vaz Cruz from the ECB's Market Operations Team could join the meeting to discuss the ECB's purchases of corporate bonds under its Corporate Sector Purchase Programme (CSPP) and the recently launched Pandemic Emergency Purchase Programme (PEPP).

1. ECB corporate bond purchases under the CSPP and PEPP

*Discussion with **Lia Vaz Cruz, Team Lead, Market Operations at the European Central Bank***

Overview

The ECB felt that the overall secondary corporate bond market structure was working well following central bank intervention.

CSPP/PEPP

The ECB explained that its corporate bond purchases needed to be assessed in light of the broader package of measures, including sovereign purchases (under the PSPP and PEPP), Targeted Long-Term Refinancing Operations (TLTROs), and changes to collateral eligibility. The extension of corporate bond purchases to include commercial paper is also an important consideration, which was a response to companies' challenges with cash flows in the initial wake of economic lockdowns.

In terms of market impacts, the ECB is aware that the scale of purchases under the new CSPP envelope and PEPP is significantly greater than previously, noting that in the first two months it purchased on average more than €10bn of bonds, which is more than in the previous years of the CSPP. However, the ECB remained sensitive to impacts on market liquidity and pricing and was focused on market axes rather than looking to leave the street short.

This was also a consideration in the decision to make purchases in the primary or secondary market. After the increase in the APP envelope and the introduction of the PEPP, there were a lot of offers in the street, which favoured secondary purchases. As the market turned, and particularly as we saw a surge in new issuance, primary market purchases became more relevant. But there is no pre-set quota or target for the split between primary and secondary market purchases, and this will continue to be driven mainly by market dynamics and liquidity conditions.

Through facilitating the ability for more corporates to raise capital in the bond markets, the CSPP/PEPP is helping banks indirectly, freeing up their balance sheets to support other activities. The ECB judged the existing range of instruments and the current policy stance as appropriate in light of prevailing economic and market conditions.

Discussion

The Group discussed the IG market performance during the covid-19 crisis, including observations highlighted in ICMA's recent report.[1] It was noted that during the peak of the volatility there had been a marked shift from e-trading to voice, but otherwise, the overall trend for market electronification and automation has continued. Some commented on the wider use of protocols beyond traditional request-for-quote (RFQ), in particular portfolio trading. It was also suggested that other markets, such as equities and FX, continued to function well due to a high level of automation and algorithmic trading, while credit struggled due to a lack of real-time data required to support auto-quoting. It was commented that a contributing factor to the shift to voice in response to high volatility is also a function of how corporate bond market liquidity is created, and the limited capacity of dealers' balance sheets in the face of significant one-directional flows.

Conclusion

The Co-chairs again thanked the ECB for taking the time to join the meeting, and for the very helpful and engaging discussion. It was also noted that his was the third time in recent years that the ECB had joined the SMPC to discuss its purchase programmes, and it was hoped that this engagement between the SMPC and the ECB would continue.

2. Regulatory updates

a) Bond market transparency

Liz Callaghan (ICMA) updated the Group on ICMA's recent regulatory submissions related to bond market transparency.

ESMA

On June 12, ICMA submitted its response[2] to ESMA's consultation paper on MiFID II/ MiFIR review report on the transparency regime for non-equity and the trading obligations for derivatives. ICMA's response focused on post-trade reporting, rather than pre-trade, which is not seen as overly relevant. The response proposes a level 1 change to create a harmonized EU deferral regime, which protects liquidity providers and investors and is consistent with CMU goals. Importantly, any harmonization of deferral regime should not be uniformly set at the lowest level of available post-trade transparency thresholds under MiFID II/R. Instead, the uniform deferral regime should be based on the existing MiFID II/R deferral regime experienced by most market participants today. However, industry participants

[1] The European investment grade corporate bond secondary market & the COVID-19 crisis (May 2020)
[2] See: https://www.icmagroup.org/assets/documents/Regulatory/MiFID-Review/ESMA-Transparency-CPRESPONSEFORM-Final-ICMA-submission-12-June-2020-150620.pdf

should be allowed, as an exception, to set up agreements whereby transparency levels are set at higher levels of transparency exposure than the uniform post-trade MiFID II/R based transparency regime across the EU (for example Denmark).

The response also recommends the creation of an industry body to Independently verify bond liquidity and threshold data output with ESMA's: The Data Advisory Group. The 'DAG', would consist of industry operational level experts, including trading venues, APAs, data providers, sell-side banks (global and EU headquartered), Institutional Investors (global and EU headquartered) and intermediaries. In addition, the 'DAG' should make sure the APA representatives are from the top APA providers as listed on ESMA's website, as those data repositories should have the most accurate data sets.

Finally, the response suggests that the best transparency regime is one that is not overly complicated or overengineered and in fact is a transparency regime that works for all market participants in practice. To this end it proposes investigating IG/non-IG based large-in-size thresholds (without applying size-specific-to-the-instrument thresholds), as this could potentially prove to be a better and more workable transparency regime, that is easier for both industry participants and regulators.

European Commission

On May 15, ICMA submitted its response[3] to the European Commission MiFID II/R review consultation paper on the review of the MiFID II/MiFIR regulatory framework. The relevant secondary market elements to which ICMA responded included: general questions in relation to bond markets, consolidated tape for EU bond markets, post-trade transparency, best execution reporting, research unbundling, multilateral systems, non-discriminatory access to bond markets, and digitalization and new technologies.

Consolidated tape

In April, ICMA submitted and published its final report on an EU Consolidated Tape for Bond Markets[4] which had been prepared at the request of the European Commission.

The report highlights the potential benefits of a consolidated tape (CT), proposes principles that should underlay its data ownership and design, and discusses possible governance structures. It also provides an analysis of FINRA's Trade Reporting and Compliance Engine (TRACE) and draws on lessons learned from the US's journey. It further emphasizes that data quality is a top priority for the establishment of a CT.

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[3] See: https://www.icmagroup.org/assets/documents/Regulatory/MiFID-Review/MiFID-review-CP-ICMA-response-2020-05-15-180520-secondary-version.pdf

[4] See: https://www.icmagroup.org/assets/documents/Regulatory/MiFID-Review/EU-Consolidated-Tape-for-Bond-Markets-Final-report-for-the-European-Commission-290420v2.pdf

Discussion

It was noted that a CT could be helpful, particularly from the perspective of measuring trade execution quality. Not only would it support explanations to investors why a trade was executed at a particular price, but also why some transactions could not be executed. It was added that a CT would also be useful for risk management.

However, it was also pointed out that the considerations for a bond CT are very different to those for equities, and that from a best execution perspective factors such as the size of a trade and the application of a dealer's balance sheet also need to be factored into a price, and that this cannot necessarily be comparted with the last reported print.

Members agreed that while the benefits of an EU CT for bonds are clear, the calibration is extremely important.

b) CSDR Settlement Discipline

Briefing

Andy Hill updated the Group on ICMA's ongoing work related to CSDR-SD implementation, in particular that related to mandatory buy-ins (MBIs).

Delay to 2021

The proposed delay to implementation to February 1 2021, submitted by ESMA in February, was approved by the European Commission in May 2020, this is currently awaiting further approval by the European Parliament and Council, with the objection period ending on August 27.

ICMA communication with the European Commission

In May 2020, ICMA, on behalf of its members, wrote to the European Commission and ESMA outlining the industry concerns related to timely implementation of the CSDR mandatory buy-in provisions. The letter highlighted the ongoing lack of regulatory clarification required by the industry to facilitate successful implementation, as well as asking the authorities to review the design and application of the buy-in framework in light of recent market events.

Also, in May 2020, ICMA discussed the points outlined in the letter on a call with the European Commission. The Commission confirmed that in recent weeks it had engaged with numerous industry bodies and individual firms expressing similar concerns. The Commission further indicated that they were aware of the potential consequences on pricing and liquidity in benign market conditions and were also considering how this would play out in a scenario of market stress. They suggested that they would be reviewing CSDR-SD as part of their post-COVID-19 assessment of market regulation.

Implementation

Through its CSDR-SD Working Group, ICMA continues to engage with members to prepare possible revisions to the ICMA Buy-in Rules, which would provide members and other industry users with (i) a contractual buy-in framework that can be initiated in the event of a settlement fail and completed before the CSDR MBI is required; and (ii) a contractual framework to help support execution of the MBI process in the event that this is required. ICMA intends to consult on the proposed revisions later in the year.

Discussion

Members felt that given the serial shocks of covid-19, then Brexit, the implementation of MBIs in early 2021 is likely to have seriously negative impacts for markets. It was also flagged that this point was completely missed by the EU High Level Forum on the Capital Markets Union, whose [Final Report] had been published the previous week. It was asserted that if the objective of CMU is to help foster SME's, then we should be looking to develop Europe's capital markets, making them attractive to both investors and issuers, not drain them of liquidity. Members felt that this point should be central to ICMA's advocacy on MBIs.

3. FinTech update

Update

Rowan Varrall (ICMA) updated the Group on ICMA's various FinTech initiatives, particularly as they related to ICMA's secondary market work.

ICMA's FinTech Advisory Committee (FinAC), met on May 26. At that meeting, special guests Joseph Noss and Patrick Armstrong, members of the FSB Secretariat, provided an update on some of the latest aspects of the FSB's work in relation to FinTech, notably on implications of BigTech in finance and lessons learnt from emerging markets, the use of RegTech and SupTech, as well as the potential implications of Covid-19.

In other news, ICMA was preparing its response[5] to the European Commission Consultation on a new digital finance strategy for Europe / FinTech Action Plan.

Other recent regulatory engagement included the ECB FinTech task Force meeting (May 4), the Swiss National Bank (April 8), and the Bank of England (May 5) to discuss the BoE's consultation on Transforming data collection from the UK financial sector.

Finally, members were updated that ICMA was in the process of formalizing the collaboration with ISDA and Regnosys to extend the CDM to repos and bonds.

[5] Submitted on June 25. See: https://www.icmagroup.org/assets/documents/Regulatory/FinTech/ICMA-Response-to-EC-Consultation-on-a-new-digital-finance-strategy-for-Europe-FinTech-Action-Plan250620.pdf

4. AOB

There were no other points of business. The co-chairs thanked everybody again for joining in these busy and testing times, and hoped that everybody remained safe and well. The next meeting of the SMPC would be on **September 15**, and it was reasonable to expect this to be held virtually.

Key calendar dates

Subject to change in light of Covid-19 developments

ICMA Asset Management and Investors Council (AMIC): First lessons of the COVID-19 crisis for the asset management industry
18 June, 11-12pm CEST

Bond market post-trade transparency and the consolidated tape – a conversation
23 June, 3.30-5pm CEST

Prepared by Andy Hill (June 2020)
Updated September 2020