MFA

March 6, 2024

Via Electronic Mail: cp23-32@fca.org.uk

Stephen McGoldrick
Financial Conduct Authority
12 Endeavour Square London
E20 1JN

Re: Improving transparency for bond and derivatives markets: Consultation

Dear Sir/Madam,

MFA[1] appreciates the opportunity to represent the views of the global alternative investment industry in this written response to the Financial Conduct Authority's ("**FCA**") consultation paper on improving transparency for bond and derivatives markets (the "**Consultation Paper**").

MFA is fully supportive of the FCA's intentions to improve transparency in the non-equity markets, in accordance with the outcome of the Wholesale Markets Review ("**WMR**") and the FCA's commitment to strengthen the UK's position in wholesale markets, as outlined in its 2023/2024 Business Plan. As the UK regulatory regime evolves, MFA would encourage the FCA to continue to engage closely with the US and other international policy and regulatory leaders to ensure continued alignment of the UK market framework in a way that supports cross-border trading.

Context

MFA represents globally active hedge funds supporting a policy environment that fosters growth in efficient, fair and transparent capital markets. Many of MFA's members are headquartered in the US and nearly 40 percent of MFA members have offices in the UK. Many MFA members trade actively in both equity and non-equity instruments on a range of UK trading venues as well as on an "OTC" basis with UK investment firms. Some of our members are headquartered in the UK, others that are not UK-headquartered have FCA authorised entities in their groups and may be directly subject to the requirements of MiFID II as onshored in

[1] Managed Funds Association (MFA), based in Washington, DC, New York, Brussels, and London, represents the global alternative asset management industry. MFA's mission is to advance the ability of alternative asset managers to raise capital, invest, and generate returns for their beneficiaries. MFA advocates on behalf of its membership and convenes stakeholders to address global regulatory, operational, and business issues. MFA has more than 180 member fund managers, including traditional hedge funds, credit funds, and crossover funds, that collectively manage over $3.2 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time.

the UK, and a third set of non-UK members transact solely on a cross-border basis and so are affected by the UK's regulatory regime indirectly.

Our responses to the FCA's questions focus on: (i) the scope of the proposed regime; and (ii) the framework for, and calibration of, waivers and deferrals. We have set out our responses to the relevant questions in the Annex hereto.

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MFA appreciates the opportunity to provide these comments to the FCA in response to the Consultation Paper. If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact the undersigned at jhan@mfaalts.org or Jeff Himstreet at jhimstreet@mfaalts.org.

Respectfully submitted,

/s/

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MFA

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ANNEX

CHAPTER 4. SCOPE OF THE NEW REGIME

Q1 Do you agree with maintaining the current scope of the transparency regime for bonds based on whether they are traded on a trading venue? If not, what do you recommend the scope should be?

MFA Response

MFA supports the FCA's proposal to maintain the current scope of the transparency regime for bonds. MFA notes the continued application of a broad transparency regime for bonds would contribute to a more efficient price formation and support the FCA's planned UK consolidated tape for bonds.

Q2 Do you agree that the transparency regime should focus on the classes of derivatives subject to the clearing obligation? If not, please explain why?

MFA Response

MFA agrees that the mandatory transparency regime for derivatives should focus on classes of derivatives that are sufficiently standardised and liquid as to benefit most from increased transparency.

To that end, MFA would encourage the FCA to limit the scope of Category 1 derivatives to OTC derivatives that are subject to the UK trading obligation, pursuant to Article 28 UK MiFIR, being a more liquid subset of derivatives subject to the UK clearing obligation.

MFA notes that derivatives which fall outside the scope of the UK trading obligation are considerably less likely to be standardised and liquid, and thus requiring transparency measures to apply to such instruments may not necessarily help price formation. Nonetheless, MFA expects the liquidity of derivative contracts and the number of market participants trading certain types of derivative contracts to fluctuate over time. Consequently, MFA encourages the FCA to continually assess the liquidity of derivatives subject to the UK trading obligation generally with a view to ensuring that derivatives which are sufficiently liquid are categorised as Category 1 instruments and made subject to mandatory transparency requirements.

Q3 Is the current level of transparency in FX derivatives and single-name CDS adequate? If not, should a subset of them be included as Category 1 instruments?

MFA Response

MFA agrees that FX derivatives and single-name CDS should be excluded from Category 1 instruments.

Q4 Do you agree with excluding FRAs, basis swaps and OIS and Fixed-to-Float swaps with reference index other than EURIBOR, SONIA, SOFR, €STR and FedFunds – from the list of Category 1 instruments? If not, please explain why.

MFA Response

MFA agrees that such instruments should be excluded from Category 1 instruments.

Q5 Do you agree with including iTraxx Europe Main and iTraxx Europe Crossover as Category 1 instruments? If not, please explain why.

MFA Response

MFA agrees with the inclusion of iTraxx Europe Main and iTraxx Europe Crossover as Category 1 instruments.

Q6 Do you agree with our proposal to bucket swaps by tenors? If not, please explain why.

Q7 Do you agree with our proposal to include spot and forward starting swaps within the same tenor bucket? If not, please explain why.

MFA Response

MFA disagrees with the FCA's proposal to include spot and forward starting swaps within the same tenor bucket. MFA believes that such swaps should be included within different tenor buckets as the liquidity in forward-starting swaps is much lower than that in spot starting swaps.

Q8 Do you agree with our proposed scope of Category 1 instruments for OTC derivatives? If not, please explain why

MFA Response

As explained in response to Question 2, MFA believes the scope of Category 1 OTC derivatives should be limited to derivatives subject to the UK trading obligation, as a more liquid subset of derivatives subject to the UK clearing obligation. Further, since instruments beyond the 30Y tenor point are significantly less liquid, as demonstrated by Table 5 in the Consultation Paper, MFA would suggest limiting the tenor of Category 1 OTC derivatives to 30Y.

Separately, MFA notes that all structured finance products, emission allowances, and derivatives (not falling within Category 1), will be categorised as Category 2 instruments.

Transactions in Category 2 instruments will be subject to transparency requirements, where traded under the rules of a UK trading venue, but the calibration of the transparency will be left to the trading venue. That is, trading venues will set the appropriate large in scale ("**LIS**") thresholds and length of deferrals for Category 2 instruments, and in turn be able to determine the appropriate level of transparency for such instruments.

MFA strongly believes that transparency requirements should apply broadly and across all relevant asset classes. While recalibration of relevant waivers and deferrals is appropriate in order to simplify the regime (for example, by removing the SSTI), MFA does not believe that it would be appropriate to grant trading venues full discretion over the calibration of the transparency regime for Category 2 instruments.

MFA is concerned that granting trading venues such discretion would negatively impact the transparency of Category 2 instruments. MFA notes that neither the Consultation Paper nor the draft MAR 11 rules currently require trading venues to consult trading venue members when calibrating the transparency requirements for Category 2 instruments.

As such, MFA is concerned that different trading venues may set different transparency requirements for the same or similar Category 2 instruments. Hence, at a minimum, MFA would suggest that a requirement be added to MAR 11 for trading venues to consult members prior to finalising the LIS size thresholds and length of deferrals for Category 2 instruments.

CHAPTER 5. FRAMEWORK FOR WAIVERS AND DEFERRALS

Q9 Do you agree with our proposals for, and waivers of, pre-trade transparency? If not, please explain why.

MFA Response

MFA supports the FCA's proposals to simplify and recalibrate the pre-trade transparency regime for non-equity instruments by limiting the scope of the regime. To that end, MFA supports the removal of (i) the current "detailed" pre-trade requirements for voice and RFQ systems, and (ii) the related SSTI waiver, and the waiver for instruments for which there is not a liquid market.

Q10 Do you support our objective of enhancing price formation by prioritising the prompt dissemination of price information? If not, please explain why

MFA Response

MFA supports the objective of enhancing price information by prioritising the prompt dissemination of price information, provided the need for enhanced transparency is balanced with the need to ensure market participants can execute large trades without the risk of the market moving against them.

MFA notes that too short deferrals and/or inappropriately calibrated waivers can lead to information leakage which would be to the detriment of liquidity providers (impacting their ability to hedge) and therefore may have a negative impact on pricing offered to buyside firms and more generally increase the costs of providing liquidity, as the FCA acknowledges on page 111, para 87, of the Consultation Paper.

Q11 Do you agree with our approach based on the dissemination of trade-by-trade information as opposed to aggregation of trades? If not, please explain why.

MFA Response

MFA agrees that post-trade information should be published on a trade-by-trade basis subject to appropriate deferrals/waivers/volume cap. The prompt dissemination of trade-by-trade information would help ensure market participants have access to granular and precise trade data, which is critical for informed decision-making and should contribute to more effective price formation.

Q12 Should package trades be granted a minimum of a 15-minute reporting deferral to allow for the complexity of booking such trades?

MFA Response

MFA supports a short technical deferral of 15-minutes for package trades, given the inherent complexities involved in executing and booking such trades. A short technical deferral would allow market participants adequate time to accurately record and report the details of package transactions as close to real time as technically possible.

Q13 Are there types of transactions other than packages that should benefit from a deferral irrespective of their sizes?

Q14 Which of the two models do you think can give better calibration of deferrals for bonds and derivatives?

MFA Response

MFA supports a modified version of Model 2, incorporating the volume cap mechanism but with extended deferral periods for large in scale trades. MFA considers end-of-day ("**EoD**") price and size disclosure, even with a volume cap, inadequate. Specifically, MFA is concerned that EoD price and/or size disclosure would lead to information leakage (for example, with respect to trades above the volume cap, EoD price disclosure may allow market participants to deduce the trade size and direction) and thus expose liquidity providers to undue risk. This, in turn, would result in deteriorated pricing for the largest trades, as EoD deferral is an insufficient timeframe for liquidity providers to effectively manage their risk exposure.

As such, MFA believes Model 2 should be modified to give better calibration of deferrals for bonds and derivatives.

CHAPTER 6. REAL-TIME TRANSPARENCY AND CALIBRATION OF DEFERRAL

Bonds

Q15 Do you agree with the factors used in grouping bonds?

MFA Response

MFA agrees with the factors used in grouping bonds.

Q21 Do you agree with our proposed thresholds for bonds transparency in Option 1?

MFA Response

As explained in response to Question 14, MFA supports a model with a single LIS threshold with a volume cap. As such, MFA does not agree with the proposed thresholds for bonds transparency in Option 1.

Q22 Do you prefer the Option 2 approach, wherein for trades between the thresholds both price and size are published at EOD rather than after 15 minutes and 3 days respectively?

MFA Response

As explained in response to Question 14, MFA believes the proposed EoD price and size deferral for trades above the Option 2 LIS threshold is too short for bonds. Such short deferral would, in MFA's view, result in information leakage, and have a negative impact on pricing offered to buyside firms. As such, MFA prefers a modified version of the Option 2 approach, wherein trades above the LIS threshold but below the volume cap would benefit from a longer price and size deferral than the EoD disclosure the FCA proposes.

Q23 Do you prefer the Option 2 approach, wherein for trades above the upper threshold prices only are published at EOD rather than our proposal to publish both price and size after four weeks?

MFA Response

As explained in response to Question 14, MFA is concerned that EoD price disclosure, even with a volume cap, would lead to information leakage and thus expose liquidity providers to undue risk. As such, MFA prefers a modified version of the Option 2 approach, wherein trades above the upper LIS threshold would benefit from a longer price deferral than the EoD disclosure the FCA proposes.

MFA

Q24 If all prices are to be published by EOD then when, if at all, do you think the size of trades larger than the upper threshold should be published?

MFA Response

MFA does not believe that the size of trades larger than the upper threshold should be published.

MFA notes this approach aligns with equivalent CFTC and FINRA transparency rules for block trades in the form of volume caps, where for transactions above the cap the actual size of the trade is never published (other than by indicating that the transaction is above the applicable volume cap).

OTC derivatives

Q25 Do you agree with the approach and methodology used to set the thresholds and the length of deferrals (for derivatives)?

Q26 Do you agree with the proposed deferrals and associated thresholds in the 2 models (for derivatives)?

MFA Response

As explained in response to Questions 14 and 22, MFA believes the proposed EoD price and size deferral for trades above the Option 2 LIS threshold is too short for derivatives. Such short deferral would, in MFA's view, result in information leakage, and have detrimental impact on pricing offered to buyside firms. As such, MFA prefers a modified version of the Option 2 approach, wherein:

- trades above the LIS threshold but below the volume cap would benefit from a longer price and size deferral than the proposed EoD disclosure; and
- trades above the upper LIS threshold would benefit from a longer price deferral than the proposed EoD disclosure.