

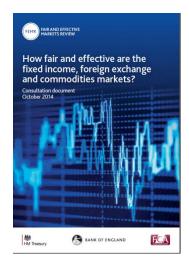
How fair and effective are the fixed income, foreign exchange and commodities markets?

January 20th, 2015

To encourage the free and frank exchange of views during this meeting, the FEMR Secretariat requests that all participants respect that this is a private event and ensure that communications regarding the content of this meeting are restricted to each participant's respective institution.

The consultation document

- Consultation organised around four key themes:
 - What 'fair and effective' means for FICC markets
 - Areas where the fairness and effectiveness of FICC markets may currently be deficient
 - Extent to which regulatory, organisational and technological changes post-crisis may address deficiencies in fairness and effectiveness
 - Further steps to help boost fairness and effectiveness in particular FICC markets



'Fair and effective' in FICC

Characteristics of effective markets

- i. Allow end-users, borrowers and end-investors to undertake transactions, including risk transfer and the channelling of savings to investment, in a predictable way.
- ii. Allow market participants to trade at competitive prices, set through a price discovery process reflecting the current end expected balance of supply and demand.

Characteristics of fair markets

- Clear and consistently applied standards of market practice market participants know what these are and have confidence that other participants will observe them.
- ii. Sufficient transparency for market participants to have common access to information and to verify that codes and rules are being applied consistently.
- iii. Open access for all, either directly or through open, competitive and well-regulated system of intermediation.
- iv. Competition on the basis of merit, reflecting equality of opportunity rather than equality of outcome.
- v. Participants behave with integrity and can be confident that they will not be subject to fraud, deception, misrepresentation, manipulation or coercion.

Framework for evaluating 'fair and effective'

	Potential source of vulnerability	Possible responses by			
		Market	Firm	Individual	Regulators/ Legislators
Structure	Market microstructure				
	Competition and market discipline				
	Benchmarks				
Conduct	Standards of market practice				
	Responsibilities, governance and incentives				
	Surveillance and penalties				

Specific issues in FICC markets - Structure

Market microstructure	 The Review considers whether structural features in specific markets may enhance or diminish fairness and effectiveness. For example: Fixed income – can corporate bond issuance be more standardised? Can new-issuance process be more transparent? FX – lessons learned from recent fx cases? Do structural vulnerabilities exist? What are the implications of increased internalisation? Commodities – is more transparency needed in OTC commodity derivatives markets?
Competition and market discipline	The Review asks if current competitive structures are vulnerable to misconduct, and whether better market discipline is a/the solution. For example: • Where do potential conflicts of interest arise in FICC markets? • Where could technological innovation improve competitiveness?
Benchmarks	 Having recommended additional UK benchmarks to be brought within scope of regulation, the Review asks what further industry/regulatory action is needed, especially at international level. What additional changes could be made in the design, construction and governance of benchmarks?

Specific issues in FICC markets - Conduct

Standards of market practice	The Review asks if standards of market practice are sufficiently clear, consistent and understood by participants so as to bolster fairness and effectiveness. In particular: • If there are real uncertainties, how should these be addressed? • What role can market codes of practice play? • Should there be professional qualifications for individuals? • Are there any financial instruments that should be brought more fully into the scope of regulation?		
Responsibilities, governance and incentives	 The Review considers how standards can be embedded in firms through governance and incentives. For example: Can performance assessment and remuneration structures be used more effectively to incentivise good conduct? What role can firms play in changing their attitudes to hiring, promotion and advancement? 		
Surveillance and penalties	 The Review considers what further measures are needed, at firm, market and regulatory level, to detect and punish misconduct. For example: Could more be done to encourage whistle-blowing? Could firms do more to punish malpractice, e.g. by shifting business away? Is there a need to widen criminal sanctions for misconduct? 		