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THE MARKET REFORM WATCH BULLETIN

Regulations: Fraudsters, Beware

Market Abuse Regulation

Over the recent years new financial instruments, technologies and trading platforms have emerged. New ways to manipulate them appeared alongside too, making regulators look for ways to damp them. The EU Parliament voted to endorse officially the Market Abuse Regulation (MAR) on the 10th of September 2013. MAR has to be in compliance with all statutes of MiFID II (which is expected in 2015) though, and may not be validated without it.

The MAR scope will cover all financial instruments, which are traded on the "organized" platforms and over-the-counter. Regulators will be able to access to the needed data to reveal market abuse. For these purposes, special systems shall be put in place to identify suspicious transactions.

Following the notorious denunciation of the London interbank lending rate manipulation, MAR shall address the benchmark manipulation scams to prohibit natural or legal persons from transmitting misleading information, providing false or deceptive inputs, or any action, which effectively manipulated the calculation of a benchmark. However, the competent authorities have been breaking their heads
over the efficient information disclosure procedures due to difficulty of proving that a benchmark manipulation took place and it affected the pricing of the involved financial instruments. Thus, prohibition of the benchmark manipulation has to be precise, and it must explain the sanctions that shall be imposed in such situation.

Under MAR, administrative sanctions are going to be quite punishing indeed.

Fines for the physical persons:
Insider dealing offence → at least EUR 5mln
Market manipulation → EUR 1mln
Remaining offences → EUR 500 000

Fines for the legal entities:
Insider dealing offence → at least EUR 15mln or 15% of annual turnover
Market manipulation → EUR 2.5mln or 2% of annual turnover
Remaining offences → EUR 1mln
In the case of recurring offences of market manipulation and insider dealing, supervisory authorities have a right to impose a permanent ban against any person. Yet, the proposed penalizing scheme is quite confusing, as according to the same regulation draft, the maximum fine shall be three times the amount of profits gained, or losses avoided.
This regulation shall compliment the existing Market Abuse Directive (MAD), aimed at increasing the investor protection and market integrity, and it will strengthen the provisions and rules of the latter.

Markets: Recovery of The European Repo

The EU Repo Council of ICMA has just released the results of its semi-annual survey of the EU repo market, which took place in June 2013.

The survey results showed:

The estimated repo market size is now EUR 6,076bn (EUR 5,611bn in Dec 2012) showing an increase of 8.6% in comparison with the December survey results. The size of the US repo market declined in the same period;

An increase in short-term repos (from 50.5% to 57.25%) is due to the higher repo rates (steepening money market yield curve → decreased risk);

Market share of the domestic trades increased (up to 30.7% from 29.7%), whereas trades with cross border counterparties declined (down to 29.3% from 18.9%) → one of the recovery indicators.

What are the reasons?

Banks return to the repo markets for funding on the back of the gradual completion of the emergency liquidity support provided to the market via the ECB's Long-Term Refinancing Operations (which has been divided into LTRO I and LTRO II) (LTRO I was EUR 489.19bn Dec 2011 and LTRO II was EUR 529.53bn Feb 2012);

The higher repo rates and greater market confidence attract lenders back to the markets, as ECB deposit facility pays 0.

Likely trend for the EU repo market

Recovery of the EU repo market over 6 months, totaling 64.8% (61.4% in Dec 2012) → LTRO repayments as the main driver.

It is likely that the EU repo market will continue to recover and expand its volumes due to increased lender activity on the LTRO contraction. Outstanding LTRO I is EUR 270bn and LTRO II outstanding is EUR 414bn at the moment. Next survey will take place in December 2013.