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EU bows to pressure from banks; Market regulator decides against more disclosure for bonds

International Herald Tribune

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LONDON: -- The European Commission is rolling back a plan to provide greater protection to investors in the $15 trillion European market for corporate and government bonds, bowing to the biggest banks in the world and the financial regulator in London.

The commission, which is based in Brussels and proposes rules for the 25 countries in the European Union, indicated that it would allow banks to formulate their own price disclosure system, rather than requiring the same data for bonds as for stocks.

EU officials were rebuffed when the British Financial Services Authority, led by John Tiner, said it opposed any rules that would require banks to provide current prices or the value of securities they buy and sell. "High levels of transparency aren't always beneficial for market users," the Financial Services Authority, which oversees 70 percent of international bond trading, said Sept. 15 in a letter signed by David Lawton, the head of market policy.

When the United States made banks and brokers provide corporate bond prices in 2002, trading fees dropped by 50 percent. A similar rule in Europe could save investors as much as $10 billion a year.

"I'm not holding my breath," said James Gledhill, a fund manager at New Star Asset Management in London. "We'd like more transparency. There's no set official price at any time and those who hold that information guard it jealously."

More than $146 billion of European corporate and government bonds trade each day, twice as much as stocks in the region, according to the Center for European Policy Studies in Brussels. Unlike shares, which are listed on exchanges that display the price of each transaction, fixed-income deals are negotiated privately.

"Smaller guys like ourselves would benefit" from more information, said James Grayson, who manages a bond fund for Thesis Asset Management in Chichester, England. "We don't really have any transparency at all."

European Union officials have until July to draft new bond rules as part of a broader plan to reduce differences in securities regulations across the region. The EU said last week that it was getting advice from national regulators and a panel that includes representatives from BNP Paribas, Deutsche Bank, UBS and four more securities firms.

Charlie McCreevy, the former Irish finance minister who is now the European commissioner responsible for financial markets, will recommend rules on bonds next year. The commission already agreed that it would not force banks to provide more bond information, unless there were "no harmful side effects."

"Market sentiment is quite strongly to the effect that there are no or no significant problems, and that there are no proven market failures that would justify regulatory intervention," the commission said after receiving comments on its proposals from 59 banks, industry groups, exchanges and regulators.

London had fought off previous attempts to regulate the bond market. In 1999, the British government blocked EU plans for a 20 percent tax on interest income, arguing that the rule would prompt investors to move money to countries with lower taxes, like Switzerland and Luxembourg.

The Financial Services Authority does not see openness as "the problem or the answer," Lawton, the markets policy chief, said in Brussels last month.

"The concern on the side of the dealers is that if the details of their trades are published they will face greater risk," Tim Rowe, a Financial Services Authority associate responsible for markets policy, said last week. "Greater risk may mean that dealers will withdraw liquidity and clients won't be able to get trades done."

In Britain, only 1 percent of households are direct buyers of government bonds and fewer still own corporate debt, according to the Financial Services Authority. But 20 percent to 30 percent of families own stocks.

Italian regulators led the push for more disclosure of bond prices after a major default by Parmalat, the diary company. That, and the default by Argentina's government, cost more than 450,000 savers at least $15 billion, Financial Services Authority data show.

Individual investors in Italy have about 40 percent of their savings in bonds, according to Datamonitor of London.

Ensuring openness is a "moral duty," said Claudio Salini, head of market and economic research at Rome-based Consob, the government's securities regulator. "The market rarely suffers from greater transparency," he said last month at a conference in Brussels.

Manlio Pisu, a Consob spokesman, declined to add to Silani's remarks.

Italians struggle to get prices on the most-traded corporate bonds, like those sold by General Motors, said Stefano Cuccia, head of supervision at Milan-based TLX, a bond and stock market for individual investors.

"The typical situation in Italy is that a client goes to the bank and says, 'I'd like to buy such and such of General Motors bonds listed in Luxembourg that's traded all over the world,' and they don't find any kind of pricing for it," Cuccia said. More information can "enhance retail investors' confidence in the market," he added.

In the United States, corporate bond traders are required to post prices 15 minutes after every deal through the regulator NASD's trade reporting and compliance engine, or Trace. The system is responsible for reducing the amount institutional investors pay to trade bonds to $1.24 per $1,000 from $2.80, according Bloomberg data and a survey published in The Journal of Financial Economics.

"We would find similar results if transparency is imposed" on Europe's corporate bond market, said Kumar Venkataraman, a professor who lectures on portfolio management at the Southern Methodist University in Dallas and who was an author of The Journal of Financial Economics study.

Bond traders in Europe charge an average 53 cents per $1,000, according to the Center for Economic Policy Research in London. Cutting that fee to 27 cents would reduce annual commissions on bonds traded in Europe to about $10 billion

European fees already are lower because the U.S. market is dominated by five or six firms, while the European market has about 25 dealers that compete across national borders, a report by the Center for Economic Policy Research said.

The Securities Industry and Financial Markets Association in New York and at least 10 more trade groups have spent two years trying to fend off the proposal. Goldman Sachs, the most profitable securities firm, told regulators that imposing transparency was "unnecessary." Deutsche Bank, the biggest German bank, warned of "undesired" consequences. ABN AMRO said it could "damage" the market. Bloomberg LP, the parent of Bloomberg News that prices bond pricing, said the Financial Services Authority was correct in concluding that mandatory bond transparency was unnecessary in Europe.

Individual investors in Europe typically pay higher prices for bonds than institutions. HVB Group in Munich offered to sell the steel trader Klockner's 10.5 percent notes due 2015 to institutions for 118 cents on the euro, according to closing prices on Tuesday. Close Brothers Sydler in Frankfurt, which caters to individuals, was charging 121.5 cents for the same bonds. The difference cost 43 basis points, or 0.43 percentage point, in yield.

"Self-regulation isn't enough," said Fernando Zunzunegui, a professor of banking and securities law at the Carlos III University in Madrid. Zunzunegui wrote a response to the commission on behalf of FIN-USE, a group in Brussels set up by the EU to advise on financial consumer issues. "We propose introducing the regulations in the equity markets to other markets with adaptations to the specific structures of the markets."

By Steve Rothwell and Sebastian Boyd

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