



LSEG RESPONSE TO THE FSB CONSULTATIVE DOCUMENT – FOREIGN EXCHANGE BENCHMARKS

INTRODUCTION

London Stock Exchange Group plc (LSEG) welcomes the opportunity to respond to the Financial Stability Board's (FSB) consultative document on Foreign Exchange Benchmarks issued on 15 July 2014.

LSEG has a long experience of providing neutral market services, and includes FTSE International Ltd (FTSE International) and MTS Next Ltd (MTS Next - a company 100% owned by MTS Spa.), which both operate and disseminate indices.

FTSE International calculates over 120,000 end-of-day and real-time indices covering more than 80 countries and all major asset classes, which serve the needs of the wide range of markets and market participants and investors.

MTS Next runs a number of indices that are independent total-return indices measuring the performance of the largest and most widely-traded securities in the Eurozone government bond market. These include the EuroMTS Index Range (ex-CNO Etrix), EuroMTS Inflation-Linked Indices, MTS Italy and ex-Bank of Italy index families.

Both FTSE International and MTS Next have established a reputation for transparent, robust, rules-driven index construction, overseen by an appropriate system of independent committees and/or industry experts.

In our response, we only deal with those aspects that are relevant to LSEG and not the majority of the wider points which we believe will be addressed more appropriately by other market participants and the regulatory authorities.

This submission represents the views and experience of London Stock Exchange plc, FTSE International, MTS Spa, LCH.Clearnet Ltd and other market operators and investment firms within the LSEG.



FEEDBACK DRAFT RECOMMENDATION

- 1. The group recommends the fixing window be widened from its current width of one minute. It seeks feedback from market participants as to the appropriate width of the calculation window.**

We agree that widening the fixing window will make manipulation more difficult. However, this must be balanced against the need for passive asset managers who track the index to be able to replicate the WMR fix by executing their foreign exchange trades during the fixing window; this will not be effective if the window is too long, such that the certainty of trading at or near the fixing prices is excessively reduced. Extending the window significantly could cause asset managers to use an alternative rate, which would defeat the purpose of improving the WMR methodology. Taking each of the concerns, one could consider setting a window as short as 2-5 minutes up to as long as 24 hours; LSEG suggests that further discussion with industry would be beneficial to understand the drawbacks and benefits in order to determine the optimum balance.

- 2. The group seeks feedback from market participants as to whether there is a need for alternative benchmark calculations (such as a volume weighted or time weighted benchmark price) calculated over longer time periods of up to and including 24 hours.**

LSEG agrees there is merit to using a volume weighted benchmark price (VWAP) or stylised VWAP as alternative benchmark calculations. For a VWAP calculation to be acceptable to market participants, LSEG agrees data should be collected from a wider range of trading platforms. In respect to a stylised VWAP the optimum weighting profile would require discussion and agreement with industry participants.

We believe using VWAP better reflects the “value” of a currency pair by taking into account the size of recent transactions and the size, or depth, of the order book for a currency pair. This, in turn, provides a reference rate that more accurately reflects the value of held positions and would provide an alternative benchmark calculation for live executions. We view an index of this nature as a better reflection of market value for a currency pair, and a better benchmark to measure currency pair executions against.

- 3. The group also seeks feedback from market participants as to whether the fixing windows should continue to be centred exactly on the hour (half hour) or whether the fixing window should close or start on the hour. Market participants**



should consider whether this view changes depending on the size of the window.

We do not have a strong view on this recommendation. It seems unlikely that such a change would greatly add to the credibility of the fix as exchange rates can be influenced by all types of news, not just news released by banks and agencies at fixed times.

- 4. The group proposes that WM investigate the feasibility of receiving price feeds and transactions data from a broader range of sources to further increase its coverage of the FX market during the fixing window, and should regularly assess its coverage as market structure continues to evolve. In that regard the group also proposes that in the short term, WM develop its methodology to utilise the transactional and quote information from both Thomson Reuters Matching and EBS, wherever both are available.**

We support the FSB recommendation. Increasing the number of execution venues, and, therefore, the amount of transactions and executable bids/offers from execution venues which underpin the WM/Reuters 4pm fix, will provide a fix that better reflects the value of a currency pair in the market. In this regard we agree with the FSB's commentary to this question 4, that considerations regarding the execution venues to include in the 4pm fix should include the size of executions on a platform, the nature of the participants on a platform, and the depth of the order book on a platform. We also suggest that the nature of the rule sets on a platform, such as the length of time that an order must be held open on a platform, further reflect the quality of an order book (i.e., the likelihood that a bid/offer at a certain volume is truly available for execution), and therefore the value of such order book for inclusion in the 4pm fix.

- 5. The group considers that, where central banks publish reference rates, it is the responsibility of each to set internal procedures. Central banks should at least take note of guidance from the IOSCO principles. However, where central bank reference rates are intended for transaction purposes, the group encourages compliance with the relevant IOSCO principles.**

We support the FSB recommendation that the IOSCO principles and policy guidelines based on good governance, sound methodology and transparency, should be followed by all administrators of indices used as benchmarks, including public bodies.



6. **The group supports the development of industry-led initiatives to create independent netting and execution facilities. However, it also is interested in seeking feedback from market participants on the development of a global/central utility for order-matching to facilitate fixing orders from any market participants.**

LSEG supports the concept of a central netting venue with residual trades being auctioned. However, it is not clear how such a venue can come into being of its own accord.

7. **The group recommends that index providers should review whether the foreign exchange fixes used in their calculation of indexes are fit for purpose.**

LSEG considers use of a mid-price to be appropriate for index valuation purposes. The use of a defined fix allows index managers to transact spot and forward transactions in such a way that the performance of their investment portfolios closely matches the performance of the index. It is not clear why an exchange rate calculated over a longer period should be any better for index valuation purposes. If the fix were to be redefined so that it is calculated over a longer window, LSEG would be concerned that the rate would be harder to replicate by those tracking the index. Where client demand is sufficient, FTSE is happy to calculate indices based on bids and offer prices for both the underlying assets and exchange rates.