Cboe®

OUR VISION FOR
EU EQUITY MARKET STRUCTURE REFORM

Cboe Europe is the largest truly pan-European equities exchange by market share and value traded, offering trading in securities from 18 markets. Through our exchanges in the Netherlands (Cboe NL) and the UK (Cboe UK) we operate a range of equity trading mechanisms to allow our clients to trade in a way that suits them. We operate Europe's largest Approved Publication Arrangement (APA) for the reporting of OTC equity trades and also offer low-cost European equity market data and benchmark equity indices.

We will be expanding our presence in Europe with the launch of a new equity derivatives exchange in the Netherlands in September 2021, initially offering futures and options on six of our major European equity indices. This exchange is based on an improved market model, which is designed to be attractive to new and existing participants and grow Europe's derivatives market overall.

Since our inception in 2008, Cboe Europe has helped to promote investor choice, competition and innovation in Europe's equity trading and clearing landscape – bringing significant benefits to all market participants, particularly end investors.

We believe that a range of trading mechanisms is essential to support a range of trading strategies and market conditions and help make Europe an attractive global marketplace.

SUMMARY

Our overall experience with the implementation of the MiFID II framework since 2018 has been a positive one and we believe it has enhanced equity market transparency in many areas, to the benefit of end investors. Any proposed changes as part of the MiFID II review should adhere to a 'do no harm' principle, particularly as they are taking place against the backdrop of the challenges presented by the ongoing Covid-19 pandemic.

As a general point, we believe the ability to execute trades efficiently directly impacts investment strategies and, therefore, the performance of pensions and other savings plans. In our view, the promotion of choice and competition at all stages of the execution value chain is fundamental to an efficient trading ecosystem. That includes a range of execution options with levels of transparency that support different trading models and market conditions, with a competitive market for execution services by intermediaries, supported by a robust best execution regime to ensure that buyers and sellers are brought together efficiently. This ensures that investors receive the best possible outcome.

Recent market volatility has served to highlight the strength and resiliency of the eco-system that exists and the benefit of having a range of execution mechanisms. Any proposed enhancements or changes to this market structure under the MiFID II review needs to be justified in terms of better outcomes for the end users of markets – investors and issuers. The review must not be used to reverse the progress that has been made over the past decade to open up European capital markets and to prevent them from continuing to progress.

OUR KEY RECOMMENDATIONS FOR THE MIFID II REVIEW ARE AS FOLLOWS

- **Bring the vision of a European consolidated tape to reality**, to allow for better informed investors and support price formation by providing a single reliable view of completed transactions;
- **Improve post-trade transparency and reporting**, to ensure that data is accurate and appropriately flagged, and addressable activity more easily identified;
- **Maintain trading venue competition**, through a healthy eco-system of complementary execution mechanisms, including all waivers and the SI category;
- **Removal of the Double Volume Cap regime**, which has introduced cost and complexity and delivered no clear benefit to end investors;
- **Preservation of midpoint executions**, for all order sizes and irrespective of execution channel;
- **Retain the open access provisions**, to ensure open, competitive financial market infrastructures remain a fundamental building block of European capital markets;
- **Address growing closing auction volume**, which presents a systemic risk to the orderly running of markets and highlights the nature of these events as single points of failure.

BRINGING A EUROPEAN CONSOLIDATED TAPE TO REALITY

We believe investors are best served when they can easily observe the best market prices and that the most efficient mechanism to achieve this is via a consolidated tape. A European consolidated tape has not emerged to date because of the high costs to acquire data from all sources, making it expensive to obtain a single, reliable view of market prices.

We have long advocated a European consolidated tape and believe it would, among other things, serve as an efficient, low-cost mechanism for investors to access real-time data and would help drive participation in the equities market, particularly from retail investors; aid best execution monitoring and transaction cost analysis; and broaden distribution of data for all European companies across Europe and to the rest of the world – including small and medium-sized enterprises (SMEs) – in a consistent format, helping to encourage further financing and growth and in support of Capital Markets Union.

With that in mind, we believe the key features of a European consolidated tape are as follows:

- A real-time post trade feed, aggregating transactions from all market
- A real-time pre-trade feed – aggregating the top five best bids and offers from all markets aggregated into a central pre-trade feed
- All venues to provide data to consolidated tape providers free of charge
- A revenue-sharing model for contributing venues based on market share

IMPROVE POST-TRADE TRANSPARENCY

While data quality and post-trade transparency for equities has improved significantly under MiFID II, there is room for improvement. A significant issue faced by market participants is the identification of addressable and non-addressable liquidity, and we believe this could be resolved by improved reporting.

We believe additional guidance and enforcement is required to ensure that OTC reporting obligations, including accurate flagging of transactions, are applied consistently. As our Approved Publication Arrangement (APA) handles around 75% to 80% of all equity APA reports, we think particular consideration should be given to providing guidance on the required flags for: Give-Ups/Ins; exercising of derivatives contracts; riskless principal transactions; and equity capital markets (ECM) transactions.

We also think post-trade transparency could be enhanced for systematic internalisers by printing the name of the SI operator on the post-trade tape. Given that larger trades where the systematic internaliser is exposed to significant risk are subject to an appropriately calibrated publication delay, we don't believe identifying SIs once published should discourage liquidity provision.

MAINTAINING VENUE COMPETITION

European investors today benefit from an unprecedented level of choice when it comes to trading mechanisms. This includes both multilateral systems such as lit and dark order books, periodic auctions, and block trading mechanisms, as well as bilateral mechanisms such as systematic internalisers. This diversity is a strength of the European eco-system, not a weakness, and it should be maintained at all costs. Having access to a range of

trading mechanisms is essential to support different trading strategies, investment objectives and market conditions. It has also been proven to deliver better execution outcomes and make Europe an attractive global marketplace.

The focus of regulators should be on maintaining a healthy eco-system of complementary execution mechanisms which operate on a level playing field, rather than simply removing them.

Any decision to restrict venue choice in order to boost trading on lit markets would have to be based on evidence of harm being caused to end investors and the price formation process. Cboe believes no such evidence exists and that arbitrarily forcing trading onto lit markets would increase volatility and prevent investors from gaining access to venues offering price improvement combined with reduced market impact.

In particular, we strongly oppose further requirements for reference price waiver venues, and periodic auctions, as discussed below.

RPW Venues: Reference price waiver venues are used to satisfy investor demand for urgent, low-impact midpoint executions, which are often the result of larger orders being broken up into smaller pieces and spread throughout the day so as not to adversely move prices. Opposition to these venues comes exclusively from other exchanges based on commercial interest. Market participants, including end investors, are almost unanimous in their support for these venues.

Their use is already restricted under the double volume cap mechanism, denying investors the ability to achieve low-impact, midpoint executions. Taking 2019 as an example, if investors who traded on reference price waiver books at the midpoint were forced instead to trade at the European Best Bid or Offer (EBBO), we estimated it would have cost them nearly €500 million in spread cost and market impact. If this option was taken away, or further restricted, now that markets have become volatile, these costs would be much higher.

A proposed arbitrary minimum size for reference price waiver activity would artificially constrain the ability of intermediaries to execute these orders in the most efficient way and, crucially, deny these orders the opportunity to be matched by multiple liquidity providers who may not individually be able to execute in larger size.

It is highly unlikely that restricting activity on reference price waiver books to larger orders only would help promote market transparency and price formation. Lit venues are often regarded by investors as venues of last resort given their high levels of market impact, so orders would be executed via OTC execution channels or held until the end of the day for execution in closing auctions. None of these outcomes would be beneficial for transparency and price discovery.

Periodic Auctions: Innovation in execution venues was one of most successful outcomes of MiFID II, including the emergence of periodic auctions, new large-in-scale systems and request-for-quote platforms. Periodic auctions, in particular, have proven themselves as highly-valued, price forming mechanisms helping firms to trade in a way that reduces market impact and delivers better execution outcomes.

Cboe Europe operates the region's largest periodic auction, an innovation we created in close consultation with market participants and regulators to provide an execution alternative that minimizes price impact, reduces the impact of speed by prioritising size, and allows for the possibility of price improvement.

While we understand the MiFID II review represents an opportunity to enshrine in legislation conclusions that the European Securities and Markets Authority reached in 2019 with respect to periodic auctions, we believe no evidence of investor detriment exists to justify different conclusions or materially different regulatory action on the platforms at this time. ESMA received a large amount of feedback from a broad range of market participants and, on that basis, ESMA was able to conclude that minor enhancements were required to FBAs.

Proposed full order book transparency for periodic auctions, when run alongside continuous trading, would indicate the direction of trading interest/market pressure and potentially influence other trading mechanisms. This would result in unnecessary order, cancel and replace activity as participants strive to minimise their information leakage.

REMOVING THE DOUBLE VOLUME CAP (DVC) MECHANISM

While we recognise the effort and associated cost of implementing the DVC regime, we believe the caps should be removed in their entirety rather than arbitrary alterations made to the current thresholds. The DVCs have introduced cost and complexity and delivered no clear benefit to execution performance and end investors. We believe there was no damage to price formation demonstrated to support their introduction and they already impose additional costs on investors seeking to achieve midpoint execution.

We would support removal of the DVCs altogether and believe this would go a long way to achieving ESMA's stated aim of simplifying the currently complex pre-trade transparency waiver regime in Europe.

PRESERVING MIDPOINT EXECUTIONS

Since MiFID II's introduction, the validity of the midpoint as an acceptable price point for execution has been questioned, primarily because of its compliance with the tick size regime, but others have also questioned its price forming credentials. On the latter point, Cboe is of the view that price formation occurs whenever a buyer and seller agree to a transaction, irrespective of the design of the platform. On the first point, this is particularly the case for trades where the spread is a tick or an odd number of ticks wide, and a midpoint execution would result in an off-tick execution.

The tick size regime was implemented to prevent venues from allowing tiny price increments to allow quotes to achieve price priority over other quotes and venues without offering any meaningful economic improvement to the terms of the trade. It was not intended to prohibit mid-point executions and Cboe believes regulators should put this uncertainty to bed once and for all and clarify that the mid-point is a protected price point, for all sizes of order and irrespective of venue type, as part of the MiFID review. It is accepted globally as a fair execution price and is extremely beneficial to investors by reducing the spread cost. European markets, and its investors, would be materially harmed should the ability to execute at the mid-point be constrained.

In our view, a midpoint execution is just as valid an expression of a view on price as the use of any other multilateral system. On a reference price wavier system, for example, market participants know the inputs and take a positive decision to trade there.

OPEN ACCESS

We believe that open competitive financial market infrastructure should remain a fundamental building block of European capital markets.

Open access has been widely adopted in European equities clearing in recent years, allowing market participants choice over their clearing provider, irrespective of which venue they use to trade. Prior to this, national European exchanges operated vertical silos for cash equity trading and clearing services, forcing users to hold separate collateral pools with each exchange/clearing house across the region. Interoperability injected competition amongst equity clearing houses and created significant efficiencies and lower post-trade costs for banks, brokers and investors across Europe.

An open access model across the trading, clearing and settlement lifecycle in exchange-traded derivatives would potentially extend significant costs efficiencies compared to the current situation. The vast majority of European derivative exchanges operate a vertical model, combining exchange and clearing services in a single group, which makes it difficult for competitive venues to emerge and can result in inefficiencies at the post-trade layer.

ADDRESS CLOSING AUCTION VOLUME

In Cboe's view, the increase in closing auction volume is creating a systemic risk to the efficient and orderly running of equity markets in Europe and is a situation which is detrimental to end investors.

Closing auctions by their nature work best as a single, centralized event, meaning there is no desire for competing, price-forming closing auctions; however, that hands significant pricing power to the primary exchanges that run auctions and renders them single points of failure. Clearly this arrangement is not conducive to encouraging competition within the marketplace and seeking to provide best execution to end investors. Furthermore, it also weakens the resilience of European markets in the event of outages on primary exchanges, leaving investors unable to achieve closing prices in affected securities.

Another particularly concerning aspect of increased closing auction growth is its impact on price volatility. Auctions attract flow that is not necessarily driven by the desire to achieve the best possible price – e.g. large portfolio rebalances and transitions. This means that the auctions are subject to supply and demand characteristics that have very little to do with the underlying value of the instrument. Investors may be losing out on best execution that could have been achieved earlier in the trading day, as orders are held back to the closing auction.

We believe European regulators should assess the systemic risk posed by increasing closing auction growth, and in particular how the resilience of the market can be improved in the event of primary market outages.

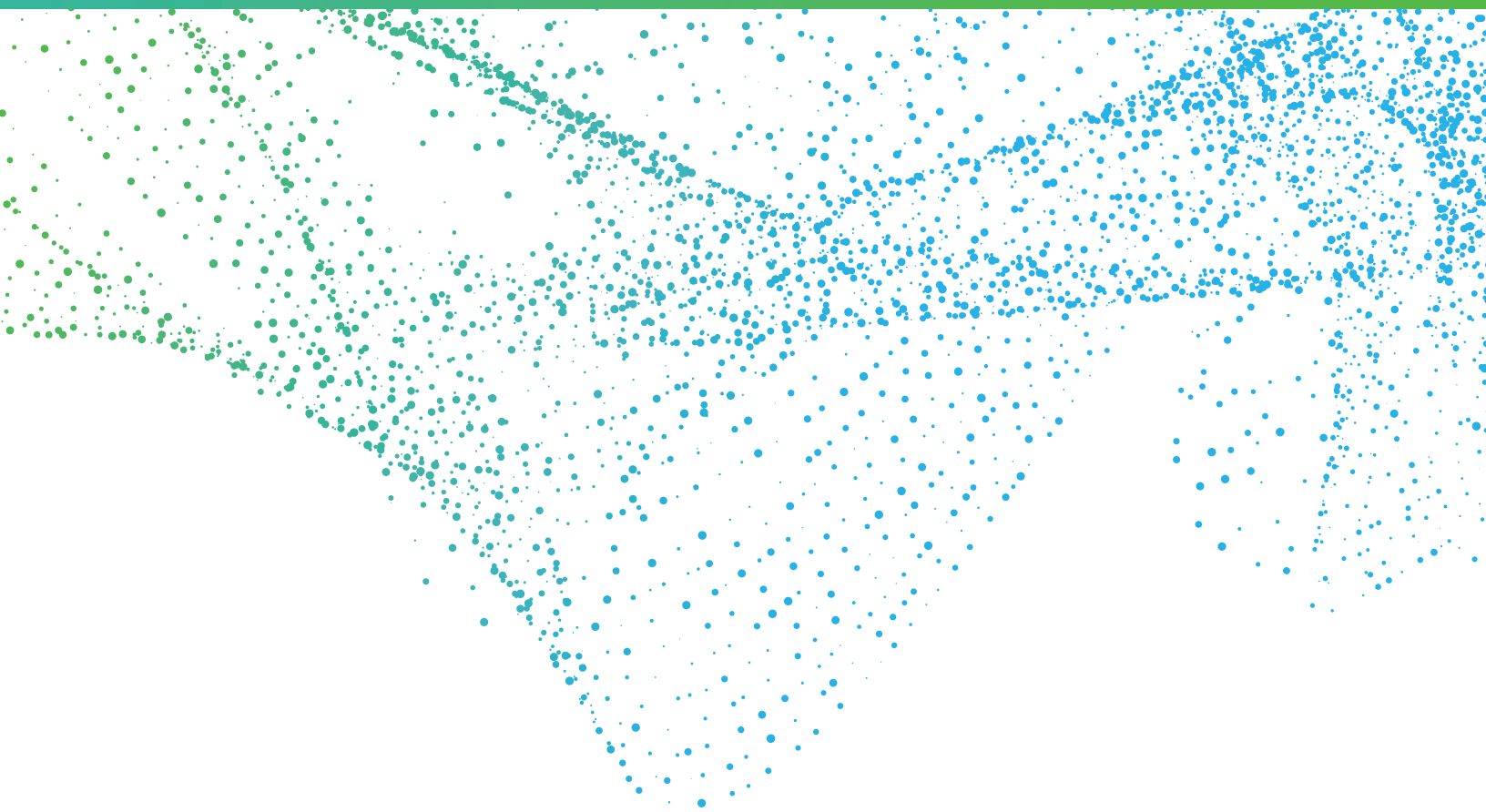
ABOUT CBOE GLOBAL MARKETS, INC.

Cboe Global Markets (Cboe: CBOE) is one of the world's largest exchange holding companies, offering cutting-edge trading and investment solutions to investors around the world. The company is committed to defining markets to benefit its participants and drive the global marketplace forward through product innovation, leading edge technology and seamless trading solutions.

The company offers trading across a diverse range of products in multiple asset classes and geographies, including options, futures, U.S. and European equities, exchange-traded products (ETPs), global foreign exchange (FX) and volatility products based on the Cboe Volatility Index® (VIX® Index), recognized as the world's premier gauge of U.S. equity market volatility.

Cboe's subsidiaries include the largest options exchange and the third largest stock exchange operator in the U.S. In addition, the company operates one of the largest stock exchanges by value traded in Europe and is a leading market globally for ETP listings and trading.

The company is headquartered in Chicago with a network of domestic and global offices across the Americas, Europe and Asia, including main hubs in New York, London, Kansas City and Amsterdam. For more information, visit www.cboe.com.



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