MEDIA RELEASE

Dark Pools: Industry proposes a targeted response

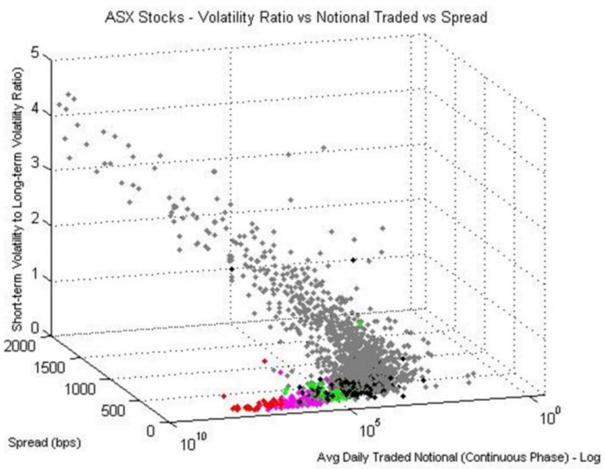
Leading AFMA member broking firms are growing increasingly concerned as ASIC moves towards finalising its approach to the regulation of dark liquidity. Dark liquidity is the term commonly used to describe ‘crossings’ where brokers match buy and sell orders before reporting trades to the exchange.

AFMA is concerned that the debate around dark liquidity in Australia has been trapped between calls for arbitrary thresholds. AFMA has proposed a more sensible way forward to meet the policy objective of preserving an efficient price formation process.

AFMA has developed a low-risk, world first, proposal for targeting a regulatory response to dark liquidity on a sound analytical basis. By comparing measures of price formation (volatility ratio and spread) against daily traded value for all ASX stocks, a picture emerges of where price formation may need protection and where it doesn’t.

The chart below illustrates these concepts using actual market data. The dots that sit low and close to the front in the chart below represent stable stocks that trade on low price spreads. There is no case for limiting dark liquidity in these stocks. The dots that sit higher and closer to the back wall show stocks that are more volatile and where price formation may be more problematic.

Price formation means the ability of the market to value shares and companies and is an important outcome of a well-functioning market.



Red: ASX50, Purple: ASX50-200, Green: ASX200-300, Black: ASX300-AllOrd, Grey: Outside All Ords
Time period: Q4 2011.

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The ASIC proposal in CP168 sets an arbitrary application of a $50,000 minimum for dark orders, a multiple of the average trade in dark liquid pools of around $10,000. Such an inflexible approach would stall these markets, stifle innovation and diminish the product offering of Australia's financial markets. As it is untargeted, it is an 'all or nothing' approach.

In comparison, AFMA's solution is targeted and does not inhibit innovation and market efficiency.

AFMA agrees with ASIC that protection of the price formation process should be the key policy objective in responding to dark liquidity, and our analysis has identified where it is in good shape. Where the case for intervention is made out, the industry supports limiting the migration of liquidity off-market in order to preserve price formation.

AFMA has now made its submission publicly available on its website at:
http://www.afma.com.au/submissions.html

Duncan Fairweather
Executive Director
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Notes for Editors:

The Australian Financial Markets Association (AFMA) is the leading industry association promoting efficiency, integrity and professionalism in Australia's financial markets and provides leadership in advancing the interests of all market participants. These markets are an integral feature of the economy and perform the vital function of facilitating the efficient use of capital and management of risk. Market participants perform a range of important roles within these markets, including financial intermediation and market making.

AFMA represents over 130 members, including Australian and international banks, leading brokers, securities companies, state government treasury corporations, fund managers, traders in electricity and other specialised markets and industry service providers.