

## **INTERCONTINENTAL EXCHANGE/TRAYPORT MERGER INQUIRY**

### **Summary of hearing with NASDAQ on 1 June 2016**

#### **Background**

1. NASDAQ said that it supplied exchange commodity derivatives offerings for power, gas and carbon emission markets, along with clearing services.
2. NASDAQ had its own proprietary software, which facilitated trading on its exchanges.

#### **NASDAQ on Trayport**

3. NASDAQ said that Trayport was a provider of software, which facilitated the trading of energy commodity derivatives. It said that its arrangements with Trayport were particularly important for their operations in continental Europe.
4. NASDAQ said it had two connections with Trayport:
  - (a) a direct route to NASDAQ's Electronic Trading System (ETS) allowing traders using Trayport to access the market prices directly on NASDAQ's exchange and execute through Trayport; and
  - (b) NASDAQ was using Trayport's GV Portal software, as a result of which brokers using Trayport could list NASDAQ products directly on their Trayport broker screens and use Trayport's straight-through-processing (STP) for exchange and clearing.
5. NASDAQ's ETS was a back-end software/ matching engine, which could be accessed through use of NASDAQ's own front-end, Trayport's Joule/Trading Gateway and/or an alternative third party front-end provider should that be the preference of the customer.
6. NASDAQ said it paid a fee to Trayport for providing access to its clients; NASDAQ paid a combination of fixed and variable yearly fees to Trayport dependent on the number of connections.
7. NASDAQ said that Trayport charged exchanges to obtain access to customers (e.g. traders) and charged customers for access to different exchanges and trading venues. In theory traders could use alternative platforms provided by other Independent Software Providers (ISVs), but

NASDAQ believed that the strength of Trayport primarily lied in the number of customers it could reach through its aggregated front-end screen:

Joule/Trading Gateway by giving access to multiple exchanges and trading venues including brokers, and both exchange and cleared liquidity as well as OTC non cleared liquidity. In NASDAQ's view, Trayport was unique in its ability to bundle all price information from multiple venues into one hub and, in this sense, there were no practical alternatives to reach the same amount of information and liquidity.

8. NASDAQ said that Trayport was essential to compete in the European energy markets (for example, the German, continental and UK power markets) and for all the gas hubs in Europe, a very high number of the trades go through Trayport.
9. NASDAQ said that the proportion of trades it received through Trayport in its continental power offering (consisting mainly of German power market for the time being) was a bit lower than one would see on other trading venues, as NASDAQ has many traders also using other systems due to its history where they mainly focus on Nordic power. However, for other continental exchanges and brokers connected to Trayport, NASDAQ believed their volume of trades received through Trayport to be substantially higher.
10. NASDAQ also believed Trayport's strong position in the market allowed it to charge a higher fee than other ISVs were able to charge in the European energy markets due to their strong position and amount of information they can provide.

## **NASDAQ on competition for Trayport services**

11. [X].
12. [X].
13. [X] NASDAQ said if it wanted to operate and expand further into the European energymarket, particularly on the European power side, NASDAQ would need to use Trayport. [X].
14. NASDAQ said it would be straightforward for the merged entity to create a more complex technical infrastructure, slow upgrades or only allow certain methods of connection, if their intention was to create barriers and to make it more difficult for other exchanges to compete with ICE.

## Competition for exchange services

15. NASDAQ said that they viewed ICE as a direct competitor, in particular in the European energy exchange markets.
16. NASDAQ said that it competed directly with ICE on the European energy market. NASDAQ listed the Nordic power market more than 20 years ago, and was the first exchange to list emissions contracts. However, NASDAQ only started listing their German power contracts in approximately 2006 and had a re-launch of that approximately three years ago. In addition, NASDAQ had launched several other new European energy markets, both on gas and power, including the UK where they had also won a power market tender together with Nord Pool Spot in 2010 (N2EX).
17. NASDAQ said that ICE was the biggest commodity exchange in the world and was involved in most asset classes. [X], NASDAQ said that ICE had recently launched various new power markets and was looking to enter the European energy market on a larger scale. NASDAQ believed that this was a reasonable rationale for the transaction, that in order to compete in new markets ICE would also need to be connected and to give access to Trayport for these power markets.
18. NASDAQ said that NASDAQ and ICE competed in the emission market. NASDAQ was the first exchange and clearinghouse to list emission products under the EU Emissions Trading Scheme when it was introduced. As a first-mover, they held a strong position and had good volumes in the market. However, NASDAQ said that when ICE entered the market it was able to take a majority of the liquidity in a very short time frame due to their wider distribution capability and having already established connections with most of the big banks, utilities and trading communities. NASDAQ said that these connections also related to the high levels of infrastructure investment costs and a firm's existing connections, if you had those connections in place from beforehand it was a lot easier to move liquidity away from one market place to another, especially in emerging markets where liquidity was not set and typically a majority of the liquidity will be OTC driven and non-cleared.
19. NASDAQ said that, using the German power market as an example, a majority of the market volume was traded bilaterally OTC non-cleared (three to four years ago approximately 25% of trades were cleared, whilst 75% was non-cleared), the trend has been moving towards moving towards clearance during the last couple of years (approximately 50:50 today).
20. [X].

21. NASDAQ said that there had also been developments in terms of competition between OTC and exchange trading as there had been significant changes within the market. Specifically, banks had exited the commodity energy space and been replaced by new businesses entering the market who were not as focussed on OTC trading. In addition, this created opportunities for the clearing volumes to grow.
22. NASDAQ said that, in the European energy market there was a preference for many financial traders to trade and clear financially settled contracts rather than physically settled contracts in the OTC space, as the latter requires larger investments in infrastructure and the ability to set up credit lines, etc. However NASDAQ noted that, the utility part of the market has, in general, been more focussed on retaining parts of the OTC business in the physical trading pattern due to history, competition and collateral costs being lower in the non-cleared environment.
23. NASDAQ said that the extent of competition varies by asset class. For example, based on Trayport's 2015 figures, the emissions market was almost 99 per cent cleared, while in the UK gas market, approximately 44 per cent was bilateral non-cleared and the remainder was cleared.

## **Competition for clearing services**

24. NASDAQ said that the story for clearing services was very similar to that for the exchange market. NASDAQ itself only offered clearing services on exchange listed contracts in the European commodity space. NASDAQ was strong in the Nordic power market due to its historical position in that market.
25. NASDAQ said that it would be an advantage to had a large position within various asset classes at a European-wide level, as the typical investor interested in a diversified portfolio would see it as beneficial to had access or to be able to place most of their positions in one clearinghouse due to the benefits of infrastructure costs and for the possibility of offsetting between the various asset classes reducing the overall cost.
26. NASDAQ said that the key factor for where you choose to place your cleared trades relates to where liquidity was held. This tended to create a barrier as to where a trader could shift clearing volumes. [✂].
27. NASDAQ said that a key component of competition was an exchanges level of distribution, and Trayport could be very important for exchanges to increase the level of their distribution towards brokers for OTC clearing. It was very important for exchanges that brokers had direct access to their clearinghouse

through the Trayport facility. NASDAQ also noted that another key factor was the level of fees you charge for clearing.

28. NASDAQ said that whilst it was costly to maintain infrastructure, that the costs of the STP link was not a significant factor. In addition, there were alternatives to the STP. For instance, NASDAQ said they had an open access solution that allows brokers to choose between various ways of reporting their trades to NASDAQ's exchange and clearinghouse. However, NASDAQ said there were some advantages with Trayport's STP link in terms of convenience.
29. NASDAQ said that it considered that the number one factor for choice of clearing venue was liquidity. For markets where liquidity resided with venues listed on Trayport, without connectivity to Trayport it would be close to impossible for an exchange and clearinghouse to attract trading volumes in the European energy markets.
30. [✂].
31. NASDAQ said that there were other possible mechanisms through which the merger entity could disadvantage competitors. For example, the technical infrastructure was highly important, both in terms of access and in terms of features, including the time of implementation of updates. The merged entity could provide ICE with a better technical solution, or, a first-mover advantage in adaptation of systems. For example, if Trayport were to make significant changes in the way exchanges connected or how trades will be reported or orders were routed, it would be very easy for Trayport to create barriers for competitors. NASDAQ therefore believed that Trayport should not be allowed to make changes to their system post-merger for some time. Further, the amount of information provided through Trayport could give ICE significant benefits in terms strategic decisions. As such, it was important that data from other exchanges and brokers were not accessible to ICE.
32. [✂].

## **Concluding remarks**

33. NASDAQ said that it was crucial to ensure equal treatment of Trayport customers if the acquisition should go through. NASDAQ said that it was important to ensure that ICE does not prioritise itself post-merger, creating barriers to entry for other exchanges and market places in the form of pricing, technical infrastructure features and connectivity. In addition, it was important that data was treated confidential and that ICE do not get access to other venues data.

34. NASDAQ said that, in its view, it was crucial to understand the importance of Trayport to the European energy space and the disadvantages for good competition if the merged entity were to use its position to disadvantage others.