

INTERCONTINENTAL EXCHANGE/TRAYPORT MERGER INQUIRY

Summary of hearing with Financial Institution A on 6 June 2016

Background

1. Financial Institution A said it operated with a [X] energy trading team in financial markets on exchanges for oil, coal, emissions, gas, and power products. It said it did not trade in physical products via over the counter (OTC) brokers.

Financial Institution A on ICE/Trayport

2. Financial Institution A said it used Trayport predominantly as a price-discovery tool as its key advantage was that it seamlessly combined prices from exchange and broker markets. It said although it only traded in the financial markets, it required access to the physical markets in order to inform its pricing strategy.
3. Financial Institution A said that it was not as reliant on Trayport as many other parties because [X] it used the technology for price-discovery, rather than execution. [X].
4. Financial Institution A said that it was considering the cost efficiency of moving to WebICE to trade ICE products [X]. It said it would, however, continue using Trading Technologies' platform for products not on WebICE, as the platform displayed an aggregation of prices from multiple exchanges.

Financial Institution A on competition for ICE/Trayport services

5. Financial Institution A said that it had concerns that ICE may seek to improve access to its products on Trayport to the detriment of competing exchanges, such as European Energy Exchange (EEX) and CME, notability in the power market where it had failed to gain market share. It said, however, this strategy would diminish Trayport impartiality and popularity and subsequently its value. It said ICE was unlikely to adopt a business model that devalued Trayport.
6. Financial Institution A said that Trayport held such a dominant position as the trading platform for gas and power, in terms of users and liquidity, and that there was a risk it might raise its prices. It said, however, that were Trayport to raise its price or limit its product offering, it would diminish its popularity and

subsequently its value. It said ICE was unlikely to adopt a business model that devalued Trayport.

7. Financial Institution A said it speculated that Trayport had found an equilibrium between charging the highest price possible without causing a meaningful shift in liquidity to alternatives. [3<].
8. Financial Institution A said that it did not consider the technological barriers for a rival to develop an alternative to Trayport to be too complex for exchange markets. If contractual arrangements made OTC brokers unlikely or impossible to switch to an alternative platform this would constitute a significant barrier to the emergence of an alternative trading platform.
9. Financial Institution A speculated ICE had historically resisted displaying its products on Trayport screens in order to promote WebICE as the main platform for selling gas and power futures. It said that this strategy was always going to fail because WebICE was limited to trading only ICE products, whereas Trayport had a breadth of pricing information across financial and physical markets. It said it was likely ICE changed their strategy when it acquired Trayport.
10. Financial Institution A said that Trayport was not as necessary if traders dealt only in products with high liquidity, on exchanges like NBP or TTF, as there were sufficient volumes on WebICE for traders to do without Trayport. It said that whilst Trayport and ICE may therefore be considered competitors in these niche products, overall the limitations of WebICE (i.e. only offering ICE exchange products) meant it did not compete with Trayport in most asset classes and products.
11. Financial Institution A said it did not know the details of Trayport's closed API business model but considered any technological barrier not as damaging to competition, provided its users' length of contracts were short enough not to prevent switching to an alternative model.

Competition for execution services

12. Financial Institution A said it used Trayport's Trading Gateway primarily for price discovery. It said the main execution platform it used was Trading Technologies' X_Trader to trade products across ICE, CME, NYMEX, CBOT and EEX exchanges. It said that X_Trader was not reliant on Trayport technology.

13. Financial Institution A said Trading Technologies was used more widely in the financial market, which, for historic reasons, was one reason why it used that platform for execution instead of Trayport.
14. Financial Institution A said that Trading Technologies was not suited for all energy traders as it only dealt with futures in the financial exchange markets, and was not suitable for traders requiring physical delivered trades.
15. [X]. It did not consider WebICE and X_Trader to be substitutable, as the WebICE screen was free and catered for a limited market (see para 10).
16. Financial Institution A said it thought liquidity could shift between trading venues over time. It said it welcomed the launch of new products into markets previously dominated by a single trading venue. It said firms typically took advantage of lower trading costs when new entrants offered reduced fees to incentivise traders to its trading venue, and the subsequent competition between exchanges that drove down fees. It said the shift in liquidity in the oil markets, from ClearPort in 2008 to CME and ICE, was an example of how exchanges competed in the long-term. Financial Institution A said liquidity shifted more easily if the products being offered by new entrants are standardised and identical to the incumbent ones.

Competition among OTC brokers compared to exchanges

17. Financial Institution A said that for some products, such as gas and power, there was little difference between the physical OTC brokered and financial exchange markets. It said that liquidity in the gas and power markets was split approximately in half between physical OTC brokered and exchange financial trading. It said that this balance of liquidity was a recent development within the last 3 years and that previously the gas and power markets were predominantly physical OTC brokered markets.
18. Financial Institution A said that exchanges compete with OTC brokered physical deals on underlyings where the relevant futures are physically settled. Interdealer brokers compete strongly among each other as they all offer the same service.
19. Financial Institution A said that participants in the power market typically used OTC when they wanted to physically settle the product, whereas those on exchanges settled by cash only. It is for this reason that firms (banks, hedge funds, etc.) who did not intend to receive the physical products operated on exchanges in the financial market, whereas utility companies who needed physical delivery used brokers.

20. Financial Institution A said it considered varying factors in selecting which exchange venue and which products it used, including; low transaction fees, exchange membership, and the incentive to reduce the amount of collateral required by buying and selling in a single exchange across product types, referred to as margin netting. Financial Institution A said the margin netting effect was strongest within a single asset class, but did have an effect across asset classes. Financial Institution A said that for this reason, it was more likely that a trader would be inclined to use the same exchange when trading power and gas. It said this effect was a more significant incentive over which exchange it selected than if Trayport were to prioritise on-screen a single exchange above others.

Financial versus physical settlement

21. Financial Institution A said that in the gas market participants were able to physically settle via brokers or exchanges, and therefore the difference between financial and physical markets were less pronounced than for power products.
22. Financial Institution A said emissions was physically settled similar to gas, on either an exchange or broker.
23. Financial Institution A said coal futures are settled similarly to power futures, by cash settlement on an exchange. Physical trades instead are arranged via an interdealer broker as they require a set of delivery related specifications to consider when trading coal.