GL NET FORUM

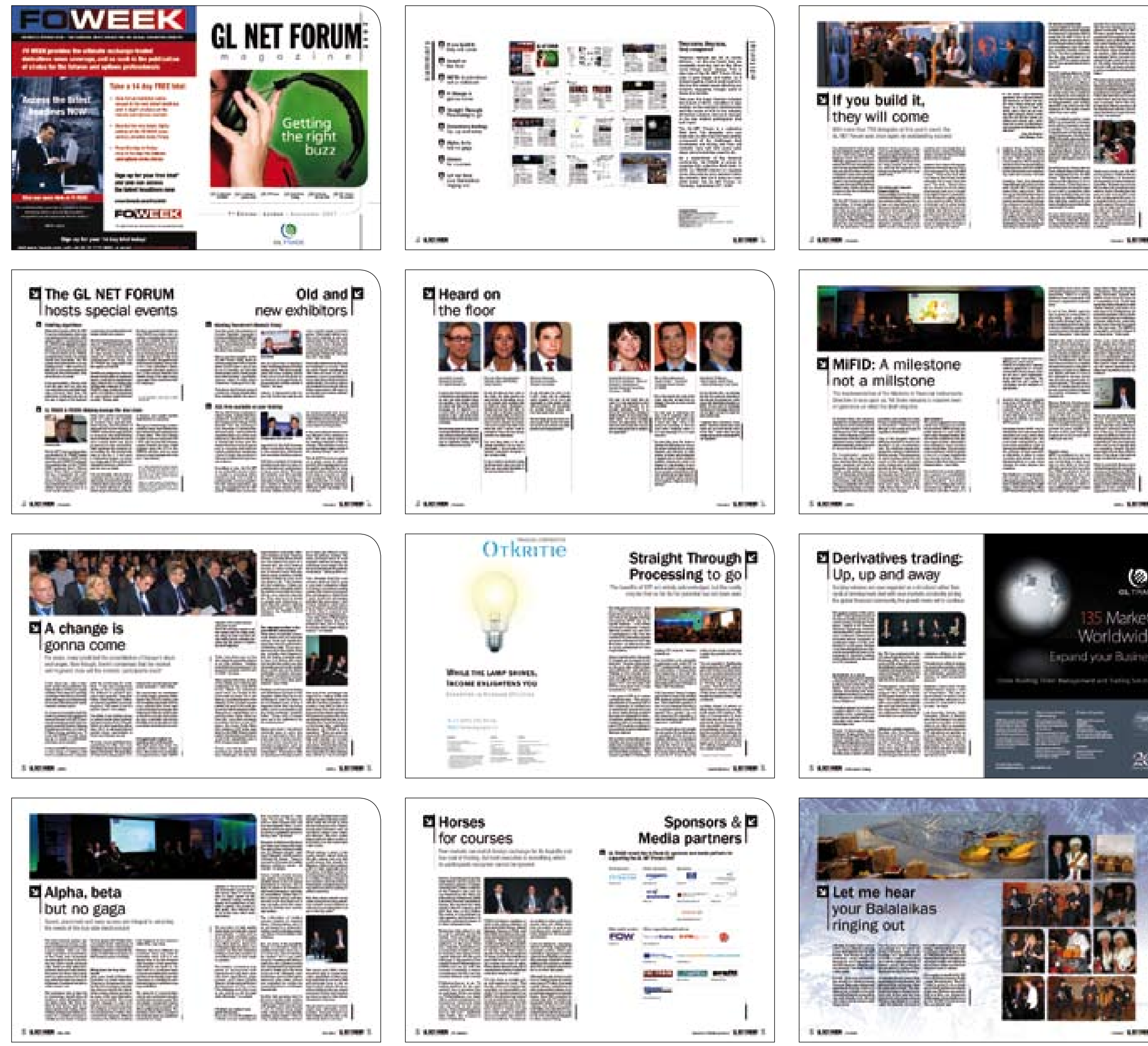
magazine

2007

7TH Edition - London - September 2007

GL TRADE

summary



editorial

They came, they saw, they conquered

Financial markets are full of contradictions – on the one hand, they are constantly evolving, but on the other, some things never change. This is also true of the GL NET Forum. Every year, it gets bigger and better, as it brings together market participants to discuss the latest issues affecting our industry; frequently, though, many of these are familiar.

This year, the major themes included the impact of MiFID, the effect of algo trading on the market's infrastructure and the levels of STP in the industry. All familiar subjects. But what changes is the way market participants deal with them.

The GL NET Forum is a collective think tank. The delegates who saw what was on offer may not have entirely conquered all the challenges their businesses are facing, but they will certainly have left with some solid ideas about what they need to do.

As a stakeholder of the financial community, GL TRADE is proud to organise this collective think tank. In 2008, GL TRADE intends to organise more discussions and debates within the industry. Save the date for our main 2008 event: the GL NET Forum, on Thursday, September 25th, 2008.

GL TRADE Publication
GL TRADE Group Communication & Marketing
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Graphic Design: Marc Letellier
Cover credits: AbleStock.com

If you build it, they will come

With more than 750 delegates at this year's event, the GL NET Forum was once again an outstanding success

You almost had to feel sorry for the 35 exhibitors at the 7th GL NET Forum, held once again at The Brewery in the City of London. Officially, registration for the event started at 8.00 am. But delegates were turning up before this and as they sat down for their coffee and croissants, many were joined by exhibitors, who were supposedly meant to be erecting their stands. This year, the buzz at The Brewery started early, lasted all day and carried on into the cocktail party in the evening.

The GL NET Forum is all about networking. It brings together participants from multiple markets from around the world to discuss the hottest issues that are impacting their industries. This year was no different. Delegates seized the opportunity to continue the discussion of familiar themes from previous years, such as the likely impact on the European equity landscape of the Markets in Financial Instruments Directive (MiFID), as well as what for many people are new topics, such as the acceptance of foreign exchange (FX) as a true asset class.

The final path towards fragmentation

The possibility that the European markets will fragment after MiFID now seems widely accepted. So it was not surprising to see a throng of people around Chi-X's stand for the entire day. The company, which is an example of one of the new multilateral trading facilities (MTFs) predicted to emerge in the post-MiFID world, is already up and running and it is beginning to attract some volume. Delegates clearly wanted to find out what all the fuss is about.

Graham Dick, Head of European Business Development at Chi-X, was impressed by the GL NET Forum. "This is the first time I've been to the Forum myself, although Chi-X was here last year," he said. "Since then, we've moved on from being what people saw as a concept that might bring in competition to the European equity market to very much a reality. The level of interest we've seen today around the stand has been incredible. But the Forum is not just about presenting our story, it's a chance to catch up with old friends and find out what is going on elsewhere. It's been a very good day," he added.

"It's (the Forum) a good networking opportunity. We've had some interesting discussions on MiFID and how the whole trading landscape might change. It's a chance to meet old friends, talk to them and see what they think is going on. There's a mood here this year that the markets are shifting more towards algos, which raises lots of issues. It's interesting to hear how people are intending to deal with these."

Gary John-Baptiste, Sales Manager, Fortis

Andrew Pryer, Vice President EMEA Execution Sales at Merrill Lynch, was also pleased by what he saw. "We've seen a good, mixed audience. We've had good feedback from the presentations, particularly the ones about MiFID, which clients felt were enlightening, clear and concise," he said.

Similarly, Gary John-Baptiste, Sales Manager at Fortis in London, said: "It's (GL NET Forum) a good networking opportunity. We've had some interesting discussions on MiFID and how the whole trading landscape might change. It's a chance to meet old friends, talk to them and see what they think is going on. There's a mood here this year that the markets are shifting more towards algos, which raises lots of issues. It's interesting to hear how people are intending to deal with these."

FX moves mainstream

It is impossible to mention every exhibitor and quote each delegate. The financial community that attends the GL NET Forum is expanding. It has moved away from its exchange-traded origins and now increasingly also includes the over-the-counter markets (OTC). The first conference of the day was dedicated to the issues of STP in capital markets. FX was represented in force this year.

Three FX trading platforms, FXall, FXMarketSpace and FXCM, exhibited at the Forum. All of them have strengths in different market segments, providing niche services for distinct client bases. For years many have predicted FX would move on to a single exchange. But it has thrived despite its fragmentation, and looking ahead FX may well provide the blueprint for the equity market, rather than vice versa.

The FX market's position under MiFID is somewhat confusing, but it will be impacted one way or another. "For us, being at the Forum this year is a first step given our FX background. We think that MiFID will create opportunities as investors are forced to look at how they manage their FX exposure, so it's useful to get our name in front of potential clients outside of our traditional base," said Francois Nembrini, Managing Director of FXCM.

David Woolcock, Senior Director, Head of Bank Sales at FXall, was also impressed by the GL NET Forum. "This has been a great event and the Brewery is an excellent venue. FX has become a mainstream product and it's been good to talk to people from other areas and markets today and see what they are thinking about and hear what they regard as the hot topics. It really is a good networking opportunity," he said.

As ever, there was a solid representation from the emerging markets. Thomaz Brandão Teixeira, an associated broker at Brazilian securities trading and brokerage firm Socopa, pointed at the fact that the markets are now a global community. "It's (GL NET Forum) a great chance to meet people who are interested in new markets, such as Brazil's, which they aren't trading yet. Also, we can talk to other market players about their views and feelings on vendors, other markets and exchanges. We're now part of a global industry which is growing, so it's really important to stay in touch with as many developments as possible and being here helps."

The same views were expressed by Fahad Musaibeeh, Manager, Marketing/Client Relations at the Kuwait and Middle East Financial Investment Company (KMEFIC). "This is the first time we've been to the Forum and we have seen lots of people. We're the only broker here offering access to all the Middle East markets, and it's clear that there's a huge demand for this," he claimed.

Final word on this year GL NET Forum goes to Fabrice Proust, Vice President of Business Development at Swiss American Securities. "It's been a good show. We've seen both prospective and existing clients. We attended last year as well, and we felt it was worth coming again this year. It's a targeted forum and we know what to expect. It's a good show; the size is right and it's not so big that you simply get lost in foot traffic," he concluded. In other words, while all the exhibitors had worked hard and long, the day had proved extremely worthwhile.

The GL NET FORUM hosts special events

SHaPing algorithms

Before they headed off to GL NET Forum's cocktail party, there was one last important event for delegates to attend - was the launch of GL TRADE's new algorithmic (algo) trading product, SHaPE. Andrew Murray, Development Director for Core Products at GL TRADE, presented the product to invited clients and journalists. The VIP guests were welcomed in to a cosy meeting room – after receiving a little bit of red-carpet treatment. As they left the presentation, they all received a souvenir.

In his presentation, Murray said both the sell- and buy side are now using far more sophisticated algo products than they did previously. Analysing the rise of the use of algos in the financial community, he mentioned the role hedge funds have played.

Almost from the beginning of algo use, GL TRADE has played a part in the game with the provision of GL TACTICS, its current product for algo trading. But now, the needs for customization and sophistication are rising, and GL TRADE has responded with the launch of SHAPE.

"SHAPE was designed so that both the sell- and buy side can create and deploy customized sophisticated algos. Next to the 14 existing standardized algo created by GL TRADE, SHaPE's open architecture allows quick and efficient development of user-defined sophisticated models." Murray said.

He then presented the features that SHaPE provides: fast execution; managing the exponential rise in market data, plus a comprehensive and full set of programmes. A brief demonstration showed how easy it is to use an embedded algo and then modify and deploy it. The combination of safe, straightforward JAVA-based scripting, along with a C++ code generation option to maximise execution speed is one of the unique features that SHaPE brings to the algo trading capacities of the system in which it is deployed.

For more information, contact your GL TRADE business unit.

GL TRADE & FISERV: Helping manage the deal chain

Peter Keane, FISERV

The GL NET Forum was the perfect opportunity for GL TRADE Capital Markets Solutions (CMS) business line and FISERV to present their partnership. As GL TRADE CMS business line's Global Head Farid Naib explained, the two companies are both very strong in their respective areas of operation, which gives the partnership the potential to deliver financial services to a much wider audience.

Naib said clients increasingly want to reduce the number of vendors they operate with. Peter Keane, Vice President of International Product Strategy at FISERV added that rapid growth in crossover mix retail banking and wholesale derivatives products means there are good prospects for the partnership. Naib explained the greatest opportunities for the partnership were in the tier 2, 3 and even 4 institutional space, as there is a huge gap in the market for integrated services offered on a pay-as-you-go basis.

The partnership will provide a complete service across all instruments covered. Few systems currently allow corporate customers or bank officers to see the entire range of banking products or treasury and capital markets instruments in one place.

This type of technology solution will allow better client satisfaction and enhanced risk management of that client. "We have started to refer to this as horizontal STP – STP right across the treasury, capital markets and into retails systems using the STP in the SIERRA solution and our business process management solution," says Keane.

The GL TRADE Capital Markets Solutions business line was created after the acquisition of FNX in early 2007. GL TRADE CMS counts more than 50 clients (top tier and regional banks, private and retail banks, hedge funds, corporate treasuries), mainly in the USA and in Asia.

FISERV is a global leader in the provision of integrated, front-to-back office banking software solutions and services, particularly to tier 2 and 3 institutions and subsidiaries of multi-national banks around the globe.

Old and new exhibitors

Meeting Tomorrow's Markets Today

Over the years, the presence of Societe Generale Corporate & Investment Banking (SG CIB) has become a feature of the GL NET Forum. This makes the bank well positioned to comment on how the show has changed.

The SG CIB booth

"We've become regulars at the GL NET Forum. Partly, that's an acknowledgement of GL's market share, but it's also a good way for us to develop our sell side relationships and to meet people from other markets," says Patrick Lebouc, Head of Sales (Paris – Electronic Trading) at SG CIB.

For Lebouc, the Forum is more of a chance to meet potential rather than existing clients. He sees it also as a good way of staying in touch of developments in the wider market place. "We don't actually meet that many existing clients. That's not so much the point; for us, it's more of an opportunity for prospecting (for clients) outside of France," he says.

Lebouc is impressed with the way the Forum has cast its net over a wider range of participants. "What really strikes me is that we're starting to see new names here. For instance, there are brokers from Russia and various exchanges, such as from Luxembourg and Singapore, as well as the 'traditional' ones like the LSE," He adds

"It actually reflects nicely the way the business is moving. There are some 'exotic' exchanges on offer here and even for us, that presents a good opportunity to cross sell our products and form relationships. As well as attracting business from people like us, these newcomers still need to access the more mature markets," he concludes.

SGX: Now available on your desktop

The GL NET Forum continues to attract highly notable first time exhibitors, including this year the Singapore Exchange (SGX). Dominic Lim, the exchange's Vice President of Membership Development, Intermediaries explained that one of the main reasons for the SGX's decision to attend the Forum was the simple fact that it is such a good way to increase international market participants' awareness of what it does, the products it offers and initiatives it may have up is sleeve.

SGX representatives at the GL NET Forum

According to Lim, the GL NET is an essential service when it comes to providing direct market access. It is a web of participants coming together into the various execution venues. Lim explained the GL NET and GL TRADE were extremely important for the SGX because of the connectivity they provide to the exchange's derivatives and securities trading engines.

SGX has a number of business developments that it is keen for the international marketplace to know more about. The newest initiative was the recently launched proxy hosting for derivative markets. This allows prop traders to directly access the exchange's trading engine. Another initiative that has run for several months now is a restructured membership scheme to facilitate remote trading. This offshore membership has lower associated exchange fees.

In the past offshore banks were not allowed to be members of SGX. "We now allow banks to be clearing members of the exchange. This will allow banks to access the larger balance sheet of the clearing house," said Lim.

The GL NET Forum is recognised as a great venue to network and the SGX management even thought it worthwhile to bring local members of the exchange from Asia to London to meet new prospects. "We have taken the opportunity to invite two large local clearing members, DBS and OCBC Securities," Lim concluded.

Heard on the floor

Joackim Lantz,
Managing Director,
AG Capital Nordic AB

"I came to the Forum for the first time. It matched my expectations because we have met some potential clients and providers. Our brokers provide our clients with DMA to the Russian exchanges. So it's important to us to meet clients as well as systems providers to get a wide vision of the solutions to trade on the Russian stock exchanges.

"The best thing about the Forum is that it's an open exhibition and, at the same time, you have conferences where you can be focused on specific subjects, such as algorithmic trading. It's the mixture of both, which is good."

Fusun Hacieyupoglu,
Director, Sales and Trading,
Deniz Yatirim

"It's the first time we have come to the Forum. We came because we have worked on (providing) access to the Istanbul stock exchange with GL TRADE for 2-years. This project is finalised and we now offer DMA. So, we are here to introduce ourselves to the community. Now, we know we are on the right path. The Forum is the place to be to promote our product. I met a lot of people who didn't even know that such a service could be provided for Turkey. We have already exceeded our expectations.

"The best thing (here) is the very friendly atmosphere: it's not hard to meet people. …You can make a lot of business connections throughout a day. It's really fruitful.

"To me, in terms of electronic trading, it's the top event I have ever been to. There was very useful information in the sessions during the day."

Kleber Detoni,
Electronic Execution,
Schahin Securities

"It's the first time I've come to the GL NET Forum, but my company comes regularly. For us, it's a big opportunity to meet people and to show our products. We can present the Brazilian financial market and learn more about other markets.

"The best thing about the Forum is to meet people from around the world. We can focus our effort to reach DMA providers and trading platforms."

Isabelle Salomone,
First Vice President - Head of Business Development,
Société Générale Securities Services – PAREL

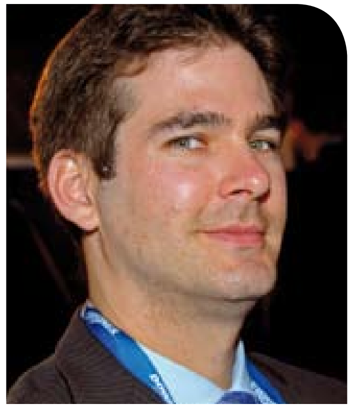
"This year, it's the fourth time we come. It's a big opportunity to meet our clients and prospects. It's an excellent networking event. To us the GL NET Forum is like a meeting of family members. It's less formal than other events. The Forum absolutely reaches our expectations. We have seen even more people than last year and we really appreciate the quality of the organisation."

Nico Nussbaumer,
Equity Trader – Technical Coverage Retail Clients,
DZ BANK

"This is my second time, here at the Forum. Last time, we were there as delegate. This year we have a booth as exhibitor.

"Our main goal is networking. We have a lot of customers who also attend the Forum. We want to get in touch with them. There is not always the possibility to find one event where everybody comes to. It's a big advantage for us to meet them here.

"The best thing about the Forum is definitely the networking. Our focus is the German markets but we are also implanted and interested in other markets. DZ Bank is representing itself in England and in North European countries. Because the Forum is in England, it's a big advantage for us to promote our bank in a foreign country. So, we can make connections here. We have reached both our expectations to meet the customers and to (discuss) B-to-B business. I hope we can do it next year."



Gerhard Fellner,
Global Equity Retail Sales – Sales Brokerage, Erste Bank

"It's the first time that I am attending this fair. The reason we came here is that we saw the program and conferences with interesting information on MiFID. We also came for networking. We have a lot of brokerage connections and we figure out that we could find new contacts here.

"I attended three conferences. About MiFID, I think the contents were quite active and you could feel the needs of the field. I learnt about the next changes we could see regarding MiFID and regulations."

MiFID: A milestone not a millstone

The implementation of the Markets in Financial Instruments Directive is now upon us. Yet there remains a massive level of ignorance on what the draft requires

As Anthony Kirby, who heads up regulation & compliance for banking & insurance at Accenture set the scene for the session on the key milestones for the implementation of the Markets in Financial Instruments Directive (MiFID), he explained many institutions are still astonishingly under-prepared for its arrival on November 1.

EU Commission research shows that the countries that have declared that they are prepared represent two thirds of European domestic and cross border equity trading, but only 30% of European bond trading. A number of countries admit they are not ready, with others saying there is a possibility they may not be. This includes large countries with significant financial services industries, such as Italy and Spain. Those countries that are not ready by November 1 will have to go through a two-stage process of regulatory forbearance.

One of the biggest impacts MiFID is predicted to have is the abolition of the concentration rule. The draft has already triggered the creation of alternative trading venues. The emergence of such trading platforms will result in the need for smart order routing and undoubtedly transform the way business is done in Europe. The incumbent exchanges may not admit it, but they are about to face the most competition for business they have ever seen. Some, especially those that are not in the top five, may struggle.

Size matters

The panel suggested that larger banks and players may benefit the most from MiFID as they are better placed to cope with the high costs of implementation. But second tier institutions will also have opportunities, especially if they manage to carve out niche areas of expertise. “It is not going to be a big bang. I think it’s going to be a 3- or 4-year transformation moving forward. What we will see in the short-term is some fragmentation,” says Kirby.

He predicts the market will then see a period of consolidation and the emergence of greater specialisation. Accenture asked 150 entities that will be impacted by MiFID how the directive will affect them in a tactical and strategic manner. Less than 15%, view MiFID as a strategic exercise. The vast majority, 85%, do not think of it in strategic terms. Amazingly at this late stage, 75% of buy-side firms still do not have a MiFID policy.

Highlights of the “final milestones for MiFID go-live” panel session

“It (MiFID) is not going to be a big bang. I think it’s going to be a 3- or 4-year transformation moving forward. What we will see is some fragmentation in the short-term,” says Kirby. “The market will then see a period of consolidation and the emergence of specialisation.”

Accenture found MiFID can be divided into four main areas: Best execution for every asset class; client order handling; pre- and post-trade transparency, and post trade operations, such as clearing and settlement. Although the concept of best execution is effectively in place in some countries and assets, its wider implementation is a new development for many players and countries.

The likelihood of fragmentation will provide some companies with great opportunities. Mark Akass, Chief Technology Officer at BT Global Financials Services, is forecasting more churn, which will make it necessary to increase bandwidth. There is a strong likelihood that connectivity will become a significant business issue.

“A lot of the MiFID opportunity is going to come down to plumbing…(and) getting the data centre strategy right. From a technologist’s point of view, this is about combining opportunity and big market changes and big market disrupters,” said Akass.

Perhaps the clear out-and-out winners will be technology providers. There could be demand for as much as 4-times bandwidth as is presently available, which not all providers will be able to deliver. Furthermore, the best execution provision is a market disrupter because it will make it necessary to trade in a different way. Banks will have to look at the alternative venues, which may provide an opportunity for newer entrants. “The experience of the US market shows us that we can expect a big increase in the number of players,” Akass pointed out.

Marcus Bullock, Development Manager for inter-dealer broker GFI in London, agreed, saying his company saw these events occur in the US as a result of similar regulatory impetus. Back in 2004, he said there was peak flow of 25,000 messages per second for price updates. By the end of this year, that peak is expected to be around half a million per second.

Flexible rules

MiFID compliance is not just about the implementation of new technology. It also goes right to the heart of how the sell-side services the buy-side. Paul Willis, explained that he sees best execution as a set of flexible rules, rather than a concrete prescriptive regime. “It’s an opportunity for firms to take a different approach to their client base,” he added.

Juan Carlos Nieto, Global Head of Business Development at Rabo Securities, argued that MiFID could even be seen as a competitive tool. Those that understand this will still have their clients dealing with them in a year from now. Furthermore, he posed the question of how do the second tier banks and institutions compete effectively, especially when most of the top tier is ready for the new rules. “It’s (MiFID) a competitive tool and a threat at the same time,” Nieto said.

Price, cost, execution, settlement, speed, lack of information leakage, these are just some of the parameters that impact best execution; depending on the nature of a transaction, these can even sometimes be contradictory. The need to trade without moving the market dramatically will determine sensitivity to price, for instance.

There are also big implications for the top 10 players from all this change, even if they are MiFID ready. Currently many of Europe’s domestic universal banks use one of the top 10 international brokers for DMA for their non-domestic trading. But some are now scrambling to become members of the new pools of liquidity that are emerging, despite the fact they might not even have DMA for some of the larger international major traditional exchanges.

There is a need for firms to have vertical integration for execution, clearing and settlement. Matteo Cassina, Head of Total Trader SM business at Merrill Lynch, finished the session by predicting that the larger brokers will increasingly be relied on as the conduit for the aggregation of trade flow.

A change is gonna come

For years, many predicted the consolidation of Europe's stock exchanges. Now though, there's consensus that the market will fragment. How will the markets' participants react?

A few years ago, only a maverick would have predicted the fragmentation of Europe's equity markets. Now, there is a growing consensus that this is precisely what will happen and fragmentation is one of the European equity markets' hottest topics.

So it was not surprising that the breakout session discussing the issue at this year's GL NET Forum was absolutely packed solid. As panel moderator Andrew Delaney, President and Editor-in-Chief of A-Team Group, pointed out, "It looks like MiFID is really shaping up to create a multi-tiered execution environment."

In the post-MiFID environment, a new range of trading platforms is predicted to compete with the exchanges for order flow. "I can see tremendous ability to move liquidity and it's difficult to predict who will be the winners," said Bob Fuller, Chief Executive Officer of nascent regulated exchange Equiduct. "We seem to be in a perfect storm," he added.

The ability of new trading venues to capture market share is already being proved by Chi-X. Hirander Misra, its chief operating officer, says Chi-X is capturing decent market share, particularly in Dutch and German stocks.

"The new venues definitely have something to offer. Our core principles are that we're cheaper, faster and smarter. The early signs of what we're seeing are 2- or 3-basis points of price improvement going upstream," adds Misra.

The newcomers are uninhibited by clunky legacy systems. Misra claims that Chi-X's trading platform is significantly faster and has more capacity than those used by the incumbent exchanges. But while most of the focus has been on the front end, the newcomers are also potentially introducing flexibility and competition in the post-trade environment as well.

A fragmented market of clearing and settlement?
This last point has been frequently missed when people have discussed the possibility of fragmentation after MiFID.

Highlights of the multiple liquidity pools panel session:
Pierre Gatignol, GL TRADE's chief executive said: "There are some big reasons for all brokers to try and help split liquidity, but a major one is to increase the value of execution."

Fuller says that even at this late stage the potential impact is not fully realised. "Clearing and settlement issues won't be apparent probably until the end of 2008," he says.

Misra agrees that there is likely to be a shake-up in clearing and settlement in the post-MiFID world. "When we embarked upon Chi-X, we looked at the post-trade process. As a new start-up, we looked at each of the existing CCPs (central counterparties). No such CCP could give us across CSD (Central Securities Depository) capabilities on a pan-European basis. What we then felt…was that wholesale providers did that in the OTC space. We chose Fortis Bank, who created a CCP entity, regulated by the DNB (Dutch central bank) in Amsterdam and that has cross-CSD capabilities and is 40% cheaper post-trade."

Those providing clearing services are aware that they face challenges, but also that fragmentation potentially offers opportunities as well. Clearing houses, including those which are considered as part of a vertical silo, are now seeking access to other trading venues. In the short term, that may lead to some confusion, but the market is likely to soon work out what to do. "The brokers will find solutions, if there are multiple pools of liquidity, which the market now believes there will be, on a case by case basis. They now have to invest in people and technology to get to the real cost for clearing and settlement," says Pierre Gatignol, GL TRADE's chief executive.

The information flow in the post-MiFID environment
Other areas of potential concern cover issues such as corporate actions, trade and transaction reporting and the publication of reference data. "If you get a takeover bid in the middle of the day, currently what happens is that the listing exchange gets to hear of it before the event and handles the orderly way that information goes into the market place. In the new world, that is potentially a problem, because the MTFs (multilateral trading facilities) won't have that (information)," says Fuller.

"Perhaps we'll see both listing and information go back to the regulator rather than be at the exchange in order for there to be a consistent view of how it happens rather than favouring really a semi-concentration role at a local exchange," predicts Fuller. "Those sorts of issues have yet to be understood by the market place."

Misra says that it should be relatively easy to solve the issue of information flow. But what may be of more concern is which price should be for reference purposes, such as portfolio revaluation and index composition. "If we were to offer an opening and closing auction, we'd likely get different prices from the primary market. The index providers have to work together with the industry; the exchange price might not be the true benchmark for portfolio revaluation," Misra points out.

Few disagree that the newcomers, such as Chi-X, pose a very real competitive threat to Europe's incumbent trading venues. But most would expect the exchanges to fight back. "I don't think the exchanges will take this lying down," said Octavio Marenzi, chief executive of Celent Communications. "I think they'll respond and they'll respond aggressively… once they start to think they'll lose market share, they'll do whatever they can to keep it. In private they'll admit they're scared," he added.

But even if the exchanges can respond by cutting tariffs and rolling out new, faster and more efficient trading systems, ultimately it may well be that it is their clients who will choose to fragment the market regardless. "We speak about the policy of the exchanges and the new pools of liquidity, but I feel that the key is on the broker side," said Pierre Gatignol, GL TRADE's chief executive. "There are some big reasons for all brokers to try and help split liquidity, but a major one is to increase the value of execution. If the brokers decide that splitting liquidity is good in the longer term for their business, they will do so," he concluded.

Straight Through Processing to go

The benefits of STP are widely acknowledged, but the reality may be that so far its full potential has not been seen

The delegates at the first conference of this year's Forum soon heard the answer to the question of how far straight-through-processing (STP) can go in capital markets – a lot further. As Octavio Marenzi, CEO of Celent pointed out, just 25% of participants in the over-the-counter (OTC) derivative markets are aware of the level of STP their firms have* - in other words, STP is not as widespread as many might believe.

Marenzi said that all too frequently IT budgets are focussed on the front end. "The back office is seen as the poor step child in financial institutions", said Marenzi. "Tellingly, in the complex derivatives markets, the largest group have very little STP. A small group, about 10%, felt that they had STP for more than 75% of their transactions," he added.

A key goal of STP is to reduce operational risks. "The primary impediment of achieving STP is the complexity of transactions or instruments. People are trying to force deals through systems that were not designed for them… Sometimes, getting the necessary budget in place to actually put in place STP projects continues to be a problem is some institutions," Marenzi claimed.

The problem is that although the benefits may be recognised, generally only a small proportion of IT budgets are dedicated to middle and back office operations. "That creates a problem in initiating and funding STP projects," Marenzi pointed out.

The panellists were generally in agreement with what STP is. "STP fundamentally started as the automation of transactions from beginning to end with the minimum of human intervention," said Peter Keane, vice president International Product Strategy at Fiserv CBS Worldwide.

ICAP Securities' Danny Corrigan said his firm's policy is to develop STP solutions and give it to clients free. This raised the question of how do you measure the return on investment (ROI) of an STP spend? "As a vendor, I go out and make the ROI argument, or help the institution make the ROI argument," said Farid Naib, Head of GL TRADE's CMS business line.

"You can break down the benefits into two parts. It's an elimination of operation al risk and an increase in efficiency. In operational risk, there's a cost to having a security fail. I know of one case where someone had a deep in the money option and they forgot to exercise it. It was about $2 million in the money, so that was a pretty big operational cost," he added.

"You can quantify it. Traditionally, when people put in STP, volumes grow. We've had one client where we put in an automated processing for a global network and we went from 40,000 tickets a day to 150,000 over the course of 2-years. The ROI is from the elimination of risk and the ability of the same number of staff to handle increased workflow," Naib continued.

Looking ahead, it seems unlikely there will ever be a single, multi-asset STP solution. The lack of homogeneity in financial instruments, as well as in standards and protocols make this impossible. However, STP is increasingly seen as the solution for a myriad of problems. As Naib concluded, there is still a lot of work to be done in numerous areas, but what is clear, is that STP still has a lot further to go in the capital markets.

* Research of Celent Communications

Derivatives trading: Up, up and away

Surging volumes are now regarded as a structural rather than cyclical development. And with new markets constantly joining the global financial community, the growth looks set to continue

The opening session of this year's GL NET Forum looked at some of the factors fuelling growth in derivative trading. Moderator David Myers, Partner in UK Financial Services & Technology Practices at Deloitte MCS, said recent surveys confirmed volumes have increased almost constantly at compound rates of 20% over the last 15- to 20-years. Perhaps most interestingly there has been a wide geographical basis to the increases in derivative trading, both in listed and over-the-counter (OTC) products.

Derivatives in a storm

"The interest and uptake in trading in listed derivatives is on the rise in Mexico and on the SGX," says Myers. There are a lot of growth stories surrounding the more established markets' exchanges, but Singapore and Mexico are boom stories too.

Derivatives appear to be in almost a perfect storm. For instance, volatility in the underlying contracts attracts attention and better education and ease of access encourages use.

Robert Fotheringham, Vice President, Trading at the Toronto Stock Exchange (TSX) says the exchange currently has a non-compete with the Montreal exchange, which has long had a monopoly on derivative trading in Canada. But this ends in March 2009 and the TSX has partnered with the US-based International Securities Exchange (ISE). Eurex recently took over ISE, which should widen the distribution capabilities of what is already the largest single-stock option exchange in the world. Not surprisingly, TSX is hoping to tap into this rich derivative seam.

Fotheringham says feedback from TSX's cash equity clients suggest they want to trade across asset classes on one platform. "An integrated exchange with cross asset-class capabilities and one that lends itself to the algorithmic capabilities of our customers is what has really motivated us to get involved."

Offshore: global markets

Dominic Lim, Vice President, Membership Developments, Intermediaries SGX, says growth changed dramatically once the exchange moved away from open outcry trading in September 2006. Now 90% of the exchange's derivative volume originates offshore, so direct market access (DMA) is vital.

"This (electronic offshore trading) has spawned proprietary trading participants, both hedge funds and individuals – speed is of the essence. So DMA is important," says Lim.

Guillermo Camou from Scotia Capital Mexico makes a similar observation. "We saw an improvement, in Mexico when the authorities allowed us to provide to customers direct access," he says.

Luis Acevedo Gomez, Chief Operating Officer of MexDer, says the exchange is focussing on product provision and innovation in an effort to penetrate local and international customers. OTC derivatives are another opportunity for the exchanges, at least in clearing space. Lim has identified that this is an area of opportunity for SGX believing there is the potential for a degree of convergence with the listed derivatives world.

Alpha, beta but no gaga

Speed, placement and easy access are integral to servicing the needs of the buy side electronically

The trend towards greater use of e-trading is becoming a key factor in determining what makes a good dealer. John Lee, the chief executive and publisher of The Trade, who moderated the final panel on how to service the buy side's needs electronically, made an early distinction between alpha and beta traders. The former are those that purely exist to make money from trading, while the latter are there to implement investment decisions at the lowest cost.

The consensus view is that better technology should allow all traders to place themselves in the alpha camp. But there are flaws to this theory. Take for instance smart order routing, which suffered widespread failure as a result of a sudden increase in volatility across assets in August. "So how smart is it? If it fails when you need it most," asked Lee. It seems that some routers lacked sufficient capacity to deal with the surge in data that took place in this frenzied period of activity.

What does the buy side need?

Jerry Lees, Head of Alternative Execution at Credit Agricole's Cheuvreux brokerage unit, said his firm is focussing on maintaining clean access for his clients, which means getting access to as many of the new alternative pools as possible. But most clients struggle to cope with this amount of access because of problems at their back end. He predicted that better interconnectivity between different venues pools will be something that happens in the medium- rather then near term.

Brokers will have different approaches. They may wish to internalise flow, but it is not always easy to do this electronically because of the speed the transactions are done at. So there will be a continued need for those specialists that can find and then cross liquidity. Lees said Cheuvreux is creating its own internal engine to optimise crossing possibilities.

The removal of concentration rules is seen as transforming the market place in many ways. But one largely unexpected impact is that fragmenting liquidity will affect settlement processes. The resulting back-office problems that arise are seen as a significant headache for many.

Highlights of "How to service the buy side electronically" panel session: Nick Garrow, Head of E-brokerage Sales at Calyon, pointed out that the statistical trading community requires an incredible level of data detail to operate. The provision of high quality, clean historical data is one of the areas which needs improvement.

The provision of high quality, clean historical data also needs improvement. "I mean tick by tick, full depth of market going back a year or even 18 months," says Nick Garrow, Head of E-brokerage Sales at Calyon, who pointed out that the statistical trading community requires an incredible level of data detail to operate.

The trading community now wants to incorporate both historical and real-time news into their algorithmic (algo) models, said Simon Rodda, Director of International Product Development at Dow Jones. "The challenge is to find a way to get clients to sift through data efficiently," he added.

I'll show you mine if you show me yours...

"If you try to work in isolation as a broker you are restricting the flow you have access to," said Lees. "If you say, 'I'll open my pool to other brokers who will rest their liquidity there,' you're going to find more opportunities to provide a qualitative service to the buy side," he added.

But again, limitations at the back-end mean may hamper this ideal. "The real problem is trying to settle into 20 different venues," said Sean Fitzgerald, Chief Executive of Broker AK Jensen. "Trying to connect to 20 venues, for smaller players, makes no sense – its overkill," he stated.

Future trends should encourage greater connectivity and if developments in the US repeat themselves in Europe, this is likely to result in an increase in algo trading strategies, especially as competition causes fees to fall. Lowering latency will also become more important and it may actually prove the major issue for brokers who service algo traders.

The collocation of trading servers remains an ongoing theme. Placing these next to an exchange's or alternative trading venue's matching engine can shave of vital milliseconds of latency.

But, as some of the panellists hinted, is collocation really everything it is made out to be, or is it more of a case of following the leader? "It's a very primitive way of dealing with latency," said Lees, who pointed out that risk management programmes should in reality be in the same venue as well. Ultimately, new technology, such as fibre optics networks, may make collocation redundant by cutting the connectivity time to exchanges dramatically.

Another fast growing trend is the rise of smart order routers. These are designed to interact with liquidity, not to directly seek it out. So where does smart order routing end and liquidity seeking algos begin? There is a big overlap between the two, said Lees. The latter tries to take liquidity without allowing others know while the former is more about taking previous history about best execution and using that to inform were orders are directed. The new routers being built will allow orders to be broken over the observable order books.

"What makes a smart order router smart? asked Garrow. His glib answer was one that made money. But despite his flippancy, Garrow had a serious point to make, especially about the issue of getting access to working larger orders efficiently. A corollary of these changes in the market's microstructure is that brokers and alternative trading platforms will be seeking to attract order flow.

But then where should smart order routing technology reside? Can brokers avoid conflicts of interest by providing their routers to the buy side?

The panel said DMA clients should be able to create smart order capabilities of their own but those that do not have DMA will obviously have to rely on their brokers. Vendor driven solutions might be the way ahead, but some of front-end vendors are slow to react to their clients' demands in this area.

The provision of broker-neutral algos may ultimately prove popular, because many buy-side traders will not wish to be effectively tied to a broker.

Horses for courses

Few markets can match foreign exchange for its liquidity and low cost of trading. But best execution is something which its participants recognise cannot be ignored.

As Dow Jones Newswire reporter Katie Martin set the scene for the breakout session on foreign exchange (FX), further evidence of the market's size was being released by the Bank for International Settlements (BIS). In its latest Triennial Central Bank Survey, BIS reported that daily activity in the FX market in April 2007 had risen to $3.2 trillion. The market is characterised by tight spreads, and because it is primarily a principal business, it is often commission free.

Technology has played a major role in opening up the FX market. This was reflected by the presence of three different platforms on the panel. FXall was originally established by a consortium of banks to cater for their buy side clients, Forex Capital Markets (FXCM) spotted a gap in the market at the retail level and FXMarketSpace (FXMS) was set up with the concept of inserting a central counterparty into the over-the-counter, bilateral cash market.

"FXMarketSpace is an FX trading platform for the cash market, but it operates like an exchange. When you trade on FXMarketSpace you trade with a central counterparty. It's anonymous. Everybody sees and can trade on the same prices. It has streaming prices and no last look," explained Jake Smith, the company's Head of Marketing.

FXMS is looking to capitalise on what is the democratisation of the market. Mark Warms, General Manager Europe at FXall, said that better buy-side access was a key development in the market's evolution. "With the opening up of EBS and Reuters (the market's two largest OTC spot brokers) up to the buy side, there's been a growth of an entirely new segment of clients, both at the institutional and retail level....who are looking to trade currencies for alpha. Those clients demand a new set of requirements in terms of what best execution means," he said.

FX has done a notable job at self-regulating itself. That though, does not mean better execution is not possible and while FX is largely exempt from MiFID, the directive has helped to focus attention on the topic. As Warms pointed out, the definition of best execution will vary from client to client, but just as in other assets, if required, price providers will need to show an audit trial. "Companies are putting in place policies to ensure they can define what best execution is and prove it to those who require it, and that's helpful for the industry," said Warms.

Francois Nembrini, managing director at FXCM, explained his company's policy, which was basically to aggregate a number of prices from liquidity providers. This generally resulted in clients dealing at the best price; whether alone this constitutes best execution is another discussion.

Ultimately though, there is a platform or trading venue for almost every type of FX client, from retail margin clients, institutional clients, quasi-market makers, on to government agencies and central banks. Since BIS compiled its volume data, the FX market has expanded further and with daily volumes now likely to be closer to $4 trillion, it is clear that FX is a market that should be big enough for all of its diverse participants to make a decent living.

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Let me hear your Balalaikas ringing out

Officially, it wasn't 'beer o'clock' until 5.30 pm. But it's a friendly crowd that attends the GL NET Forum, and thanks to various exhibitors, most notably the Singapore and Luxembourg Stock Exchanges, delegates got the chance to 'wet their whistles' a little earlier.

In truth, there was no need for any alcohol to loosen tongues. However, there was widespread agreement that the chance to share a few cocktails at the end of what had been for some a long day with friends, both old and new, was a very nice way to wind things down.

The Russian broker Otkritie sponsored the Cocktail by giving a Russian style to the evening. As a balalaika band provided some interesting and subtle interpretations of familiar music, the delegates and exhibitors continued their discussions into the evening.

One familiar theme unexpectedly re-emerged during the party. We all know what can happen when the pipes get blocked. This time, it was the surge in demand at the front end, in this case for beer, which led to a blockage out back. Perhaps surprisingly for a venue called The Brewery, the back office staff couldn't keep up, at least initially, with the demand. It could have been a tricky situation. But GL TRADE is the master at providing true front to back solutions and someone swiftly and efficiently solved the problem and the beer was soon back on stream.

Once again, an excellent GL NET Forum had been topped off with a great, informal party. The 2007 Forum is going to be a tough one to beat but plans are already under way. Markets are seldom dull and they are frequently challenging, which neatly sums up the GL NET Forum as well. See you all next year.