

e-FOREX

transforming global foreign exchange markets

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Re-engineering workflows

- regulatory reporting of OTC FX derivatives

From desktop to API

- increased demand for e-FX Option platforms

FX On Exchanges

- ICE, ISE, JSE, OSE

Expert Advisors

- customisation from bespoke FX trade strategies

FOCUS on High Frequency FX

- trading opportunities meet new technology

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Welcome to

e-FOREX

transforming global foreign exchange markets



SUMMER 2011

In this edition we have tried to examine the work that FX market participants are going to be facing over the coming months in preparing for new requirements that all OTC derivatives are reported to Trade Repositories (TR). These new regulations are going to have a big impact on existing post-trade and back office processes with significant implications for the associated technology that underpins the way these operations are conducted on a day to day basis.

It's still too early to try and guess how many TR's will ultimately emerge to serve the needs of the FX market and to predict which business models will succeed. There are a number of complex issues involved including the ownership of TR's and their jurisdictional coverage and physical location. However, it would make sense to try and avoid having too many as the more fragmented they are the less likely it is that they will effectively deliver what the regulators are looking for. A smaller number means that each will have bigger trade databases that can be more comprehensively monitored for market surveillance purposes.

The Global FX division at AFME is currently running some architecture group sessions to examine the logistics of a FX Trade Repository and to explore whether the industry can avoid completely re-engineering existing processes within the banks and stop the market having to deal with multiple interfaces. There are many other issues that need to be addressed. For example, some regions have restrictions on data movement and these will have to be overcome to get a truly global Repository,

One organisation that has geared up to meet the incoming OTC regulations and position itself to meet the new reporting needs of FX market participants is REGIS-TR. Their Deputy Managing Director, Thilo Derenbach believes that people need to start thinking about connecting to a Trade Repository now, even though the regulation is not yet finalised. He anticipates a run on Trade Repositories and CCPs from participants in 2012 and argues that IT staff will need time to set up infrastructure and mapping rules to allow the customer's in-house data to be transferred to the Trade Repositories. His advice is that market participants should take a decision on which Trade Repository and CCP they will use by Autumn this year and start technically, functionally and legally connecting to those service providers to ensure adequate project phases for testing and back-loading all the existing transactions to the Trade Repository.

We will come back to this topic in the Autumn when there is more clarity. In the meantime we hope you enjoy this edition of the magazine.

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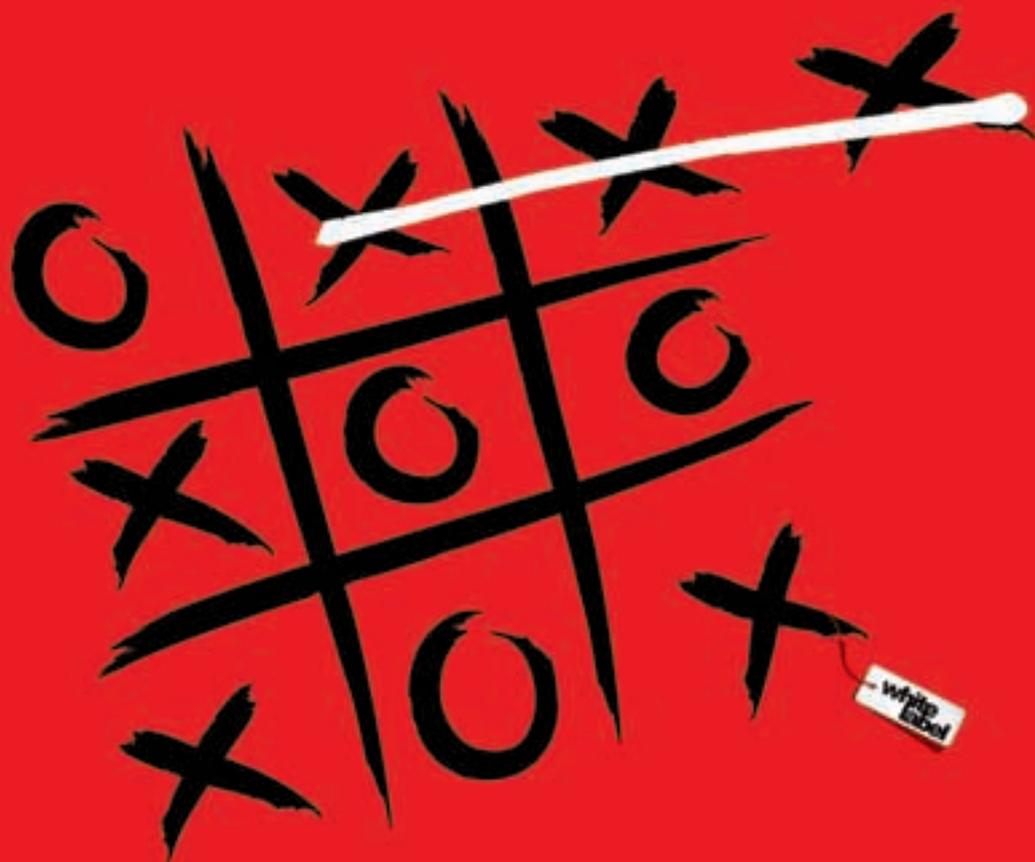
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High Frequency FX
Trading opportunities meet new technology



No sweat
Transitioning to the MT5 platform



Back office & clearing connectivity
New services for FX

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Hello
My trading objective is

execute faster

Hello
My trading objective is

*match 3rd party
benchmark*

Hello
My trading objective is

lower transaction costs

Hello
My trading objective is

*keep large trades
confidential*

Hello
My trading objective is

*minimize
market impact*

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best execution
strategy

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Nordea launches CNH trading

Nordea has added the Chinese offshore Renminbi, CNH, to its suite of tradable currencies. Launched in April, the currency is also available for e-trading on the bank's electronic trading platform, e-Markets.

Head of Global FX, MM and Commodities Trading for Nordea Markets, Kenneth Steengaard, said the quick adoption of CNH after its release as a convertible currency at the end of 2010 was a 'natural step' in the bank's strategy for emerging markets authority in the region.

"Adding CNH to our broad range of emerging currencies gives customers a cutting-edge opportunity for managing Chinese FX exposure. Nordea offers great strength for customers interested in emerging markets and our ambition is to be recognised for our solid commitment in this area," says Steengaard.

eSignal 11 offers new features

The new version of eSignal features a significantly improved intuitive, user-friendly interface that allows users to focus entirely on market analysis and trading. It also offers a wide range of customization options, including ease of access, themes, object-based charting and more.

The latest features, such as chart trading and the ability to program partial or fully automated position management strategies, give traders choice and seamless connection to their broker's trade order platform. Free Forex strategies are available and a glimpse into the education the company offers in addition to its products and services can be found at : www.esignal.com/offer/forex

Cloud Trading Technologies moves to the cloud with Microsoft Azure

Cloud Trading Technologies proven suite of applications including on line trading, risk and portfolio management and complex pricing areas of FX and other OTC markets are now available on the cloud using Microsoft's Windows Azure Cloud technology platform.

Howard Tolman, Director says that "Cloud delivery mechanisms will revolutionise these markets by greatly reducing the cost of ownership, making distribution quicker, easier and more efficient and providing total scalability in what are massively volatile markets. This advent of cloud technology will dramatically alter the market dynamics reducing barriers to entry and making previously unprofitable lines of business viable."



Howard Tolman





The hottest emerging markets - all tied up

Now trading offshore renminbi - CNH

At Nordea we're proud to be the markets authority in Nordic and Eastern European currencies, and with the addition of CNH in our growing bundle of new emerging currencies we deliver on our promise to give customers the finest global markets experience.

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Nordea's vision is to be a Great European bank, acknowledged for its people, creating superior value for customers and shareholders. We are making it possible for our customers to reach their goals by providing a wide range of products, services and solutions within banking, asset management and insurance. Nordea has around 11 million customers, approx. 1,400 branch offices, a leading net banking position and a total market capitalization of EUR 26 billion. The Nordea share is listed on the NASDAQ OMX Nordic Exchange in Stockholm, Helsinki and Copenhagen.

Gold-i launches Position Keeper



Tom Higgins

Gold-i has launched the Gold-i Position Keeper, a dashboard which helps MetaTrader brokers to fully understand their exposure to the market on a real time basis. Displaying profit and loss as well as position, the Gold-i Position Keeper provides small and medium sized brokers with the level of informed data which is normally only available to institutional brokers.

Tom Higgins, CEO of Gold-i comments, "The Gold-i Position Keeper is a truly unique product which provides MetaTrader users with a real time overview of their position. Larger brokers have only been able to access this information by building expensive back office systems. Now, with the Gold-i Position Keeper, all MetaTrader users can have access to the same level of management information. It's a superb, cost effective tool, particularly for brokers who don't want to cover all of their trades in the market" Brokers can customise the look and feel of the Gold-i Position Keeper interface to ensure it displays the information which is important to them.

E-trading pioneer launches Ogg Trading



David Ogg

David Ogg, founder and former CEO of both Hotspot FX and LavaFX, has announced the launch of Ogg Trading LLC, a provider of advanced execution solutions to the global financial services community. The new venture will leverage Ogg's well-documented success within the foreign exchange markets to bring a host of technological innovations to the FX market and beyond. "Best execution standards in FX are not where they need to be and have consistently lagged behind other markets. When traders calculate the cumulative effect of not achieving best execution they realize this has a major impact on their bottom line. It is our mission at Ogg Trading to bring new profit-enhancing tools and technologies to market that will allow participants to gain execution capabilities that are not available to them in today's marketplace, and we're very excited about that." says CEO David Ogg.

Oanda launches News Overlay feature

Oanda has recently launched a news overlay feature that allows traders to watch for important economic announcements and events that affect their forex trading from within the fxTrade forex trading platform.

Traders do not need to switch windows or access separate web pages in their browser or consult economic calendars to use the

feature which is available from fxTrade Practice accounts. These accounts allow traders to practice currency trading risk-free, under real market conditions. OANDA's forex demo account is free of charge and never expires. Traders can sign up at fxtrade.oanda.com/learn



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FINANCIAL



Claus Nielsen

Saxo Bank launches ForexTrading.com

Saxo Bank has announced the launch of ForexTrading.com which will offer retail investors a select range of FX crosses and CFDs with variable spreads, as low as 0.8 pips. The new service operates on a low cash-funding only basis and provides investors with a range of basic functionalities designed to make FX trading flexible and straightforward.

Claus Nielsen, Head of Markets at Saxo Bank, said: "Saxo Bank will continue to cater for high-net-worth and institutional traders who increasingly demand usability,

mobility, performance and service when executing online trades and orders. At the same time, this new offering will appeal to Forex and CFD traders who are price sensitive and do not require a personal service, but still want the ability to utilise an online trading platform like SaxoTrader." The minimum initial deposit when opening an account with ForexTrading.com is \$2,000 or equivalent and no interest will be paid on funds on deposit. ForexTrading.com will offer an English support service and only supports retail trading accounts.

Varengold Bank FX Trading Challenge

e-Forex is partnering with Varengold Bank FX for this year's Varengold Bank FX Trading Challenge. Participants in the event will be competing with virtual capital over a set period of time (1st September, 2011 to 30th November, 2011) to achieve the best risk-adjusted performance for their free Varengold demo account. The three most successful competitors will receive up to 1 million USD AuM (Assets under Management) which they can use for live Forex trading and will also be offered coaching and excellent support. Participation in the challenge is free of charge and involves absolutely no risk. Traders can register now at www.trading-challenge.com

Alpari launches Mini FX options

Spinning off the launch of Alpari FXOptions in February of 2011, Alpari (US) has expanded their product array by launching smaller FX options contracts for introductory traders. With the new FX options mini account, Alpari clients can get started trading spot and FX options from one margin account with a reduction in minimum trading volume from 1 standard lot (100K) to 1 mini lot (10K) and a minimum deposit requirement of \$2,000. Powered by FX Bridge Technologies, Alpari FXOptions features StrategyOptimizer™, a powerful modeling tool with a customizable interface allowing trading directly from charts, comprehensive reporting, a full order book, and complete risk management tool suite. Alpari FXOptions pricing is provided from top-tier liquidity providers on 20+ currency pairs.





Quasar eFX

Pricing and decision engine for single and multibank portals,
Liquidity management with Aggregation, Autohedge & Algorithmic execution

Pohjola Bank choose Quasar eFX from Aphelion

Aphelion has announced that Finnish Pohjola Bank has chosen Quasar eFX to provide pricing and autotrading on multibank portals as well as Aggregation and Autohedging on the Interbank market.

“Our objective is to service our customers better with faster responses to their RFQs and even more competitive prices” Says Mikko Räsänen, Head of

Foreign Exchange and Money Markets “Partnering with Aphelion and implementing Quasar will open up new possibilities to the bank and enable us to compete with the top Nordic banks. We will start by servicing our clients on the multibank portals FXall and 360T but we are looking to add more multibank portals as well as our own single bank portal as well.” Says Jarmo Koukonen, Head of FX and MM, Sales and Trading.

Dukascopy Bank launches Silver trading accounts

Dukascopy Bank SA has announced the launch of Silver (XAG/USD) trading accounts. The minimum trading amount is 50 units (ounces). With an increment of 1 unit (ounce). Trading hours during summer time are from 22.00 GMT Sunday till 21.00 GMT Friday with a daily one hour interruption at settlement time (from 21.00 GMT to 22.00 GMT).

Synergy FX announces new service

Synergy FX, which operates as a straight through processing broker, has announced a comprehensive new service for forex traders with multi-bank liquidity, straight through processing and mobile trading signals at competitive rates.

“We’ve invested heavily in our technology. Through our multi-bank price feed, we receive a deep source of liquidity from the world’s largest banks, allowing us to provide interbank pricing to all traders. Our clients take peace of mind from the fact that we have no dealing desk. With no dealer intervention and straight through processing, trade execution is super quick,” says Executive Director, Piers Cracknell.

smartTrade Technologies completes CME Group connectivity

SmartTrade Technologies has announced the certification to CME Group for FX Futures using the smartTrade Technologies LiquidityConnect™ component. The addition of FX futures from CME Group will enable organizations to benefit from accessing and trading on the liquidity provided by CME Group in their FX Futures product suite. CME Group FX futures contracts are listed by and subject to the rules of CME. The connection to CME Group was done in the FIX/FAST protocol. FIX/FAST is the basis for CME Group's market data distribution and offers reduced latency at both average and peak message rates. The smartTrade Technologies LiquidityConnect™ is a highly configurable trading-connectivity platform that natively supports FIX, FIX / FAST and bespoke protocols for quick time-to-market connectivity. The CME Group connector for FX Futures will be added to the smartTrade Technologies LiquidityConnect for FX product group which has over 22 FX connections.

Portware adds to Portware FX

Over the past 18 months, Portware has added several key features to Portware FX. Many of these enhancements address the company's growing list of long-only asset manager clients, who are increasingly focused on execution quality and deep workflow integration.

For example, Portware has integrated FX algorithms from several leading FX dealers, including Citi, Credit Suisse, Deutsche Bank and JPMorgan Asset Management, while enhancing its suite of embedded execution strategies. The system also includes extensive netting and aggregation technology, as well as full support for restricted broker lists and internal compliance rules. Portware also recently introduced FXLM, the company's new post-trade FX TCA and analytics package that gives clients greater insight into their execution performance.

DealHub selected for Quantum FX

DealHub (Option Computers Ltd) have been selected to provide the QuantumFX Institutional platform (powered by Alpari Companies) with a real-time and intuitive mechanism that will allow the monitoring of customer trading



Peter Kriskinans

activity, limits and utilisation across QuantumFX and other integrated customer facing trading venues. The DealHub Limit Monitoring Module is extensible to a wide range of trading venues and offers real-time web enabled reporting to allow customers to monitor and view trading activity, margin activity and profit & loss. The solution provides detailed real-time analysis and reporting of customer dealing activity across all integrated venues via DealHub trading connectors, including real-time monitoring of PB customer credit utilisation and maintain, call and close-out limits for margin customers with deep data filtering and real-time alerts. Peter Kriskinans, Managing Director of DealHub commented, "DealHub is used globally by many of the markets most active FX trading organisations to support low latency and high throughput e-trading and we are delighted to have added QuantumFX and the Alpari Companies to that list".



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GAIN Capital launches GTX Direct

GAIN Capital Holdings, Inc. has launched GTX Direct, a new prime brokerage service offering for its electronic communications network (ECN) for institutional and high net worth investors. GTX Direct allows qualified investors without an existing FX prime brokerage relationship to leverage GAIN Capital's central clearing facilities in order to access the liquidity available in the GAIN GTX marketplace. "GTX Direct addresses the needs of individuals and institutions who are looking for a more diverse pool of liquidity," said Vincent Sangiovanni, chief operating officer, GAIN GTX.



Vincent Sangiovanni

"Now, clients can leverage GAIN Capital's longstanding FX trading relationships to trade on all prices in the GTX marketplace, whether from participating banks or other clients, with the added advantage of a short account opening process."

Vantage FX offers MetaTrader 4 for Mac

As readers know the Metatrader 4 is a dynamic and adaptive trading system allowing the user to focus on the automation of trading strategies and systems. The trading terminal has long been associated with the PC and has had limited application on other Hardware platforms like Mac. Now Vantage FX in conjunction with CodeWeavers offers clients

the ability to use Metatrader 4 on a Mac. CrossOver is a technology that bridges the gap between PC and Mac. Users can install the software and run their favourite windows based programs in Mac or Linux. As Metatrader 4 was built for the windows environment, the CrossOver technology allows for full integration and the running of automated trading systems.



TraderTools introduces LightFX™ Pricing and Aggregation service

TraderTools has partnered with Citi's Prime Finance to offer LightFX, a fully-disclosed, relationship-based FX pricing and aggregation service. The prime-based, hosted service represents a cost-effective alternative to traditional ECNs, which execute FX trades anonymously and charge both liquidity takers and providers. With LightFX, liquidity takers receive relationship pricing at significantly reduced upfront and operational cost. Liquidity providers, which are not charged for the service, deliver full transparency and benefit from the ability to differentiate themselves from their competition. Several liquidity providers have already signed up, enabling more liquidity at more competitive pricing.

TraderTools' CEO Yaacov Heidingsfeld said, "The market is demanding fully-disclosed, relationship-based pricing and we – and Citi's Prime Finance – are listening."



Yaacov
Heidingsfeld

GAIN THE FX EDGE

With **Quasar eFX** single- and multibank autotrading with liquidity aggregation, autohedge and algorithmic execution.



QUASAR INCLUDES

FX Auto Trader
Liquidity Management
FX Pricing & Rate Engine
Single Bank Portal
Limit Order Management
Mobile Trader

APHELION'S KEY VALUE PROPOSITION

is based on the monetary value Quasar brings through its unprecedented speed combined with superior tooling to express and manage your business models. Providing an end-to-end automated trading solution connecting to any multibank portal balancing on the largest liquidity pools in a single trader view.

EUROPE

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NEWS

Integral launches Cloud-based platform for FX

Integral Development Corp. has announced the launch of FX Cloud™, enabling the full life cycle of FX, available in the cloud, as services hosted by Integral. The services are available now to trades initiated on the Integral network and will be rolled out in the coming months to “off-network” trades, opening the services up to all industry market participants. FX market participants and the businesses that serve them, have access to all the tools they need to be successful, pick what they need to build their own proprietary solutions, and do so on a shared open platform.



Harpal Sandhu

“Providing affordable access to the FX market to an ever wider variety of businesses has been at the core of Integral’s success to date,” said Harpal Sandhu, CEO, Integral Development Corp. “With the release of FX Cloud, we are now offering the broader market access to the full life cycle of FX at a cost level never before achieved. This is the future of OTC trading services.”

TMS Brokers plans to launch new service

After the introduction in 2003 of the TMS Direct platform and then in 2009, of GO4X, which is based on MT4 technology, TMS Brokers will launch the first FX based service provided by a Brokerage House in Poland for physical currency delivery.

“We carefully observe the Polish segment of FX associated with physical delivery and are just about to launch our own, advanced transaction system, which will be designed mainly for retail segment, however we would also expect small Polish companies to use it and take advantage of a better conditions than those offered by most operators in Poland. In addition, with the attractive spreads and transfers on-line, clients will be able to plan their future transactions and currency payments, which is of particular value for borrowers who pay off the mortgage denominated in foreign currency, especially in CHF,” says Piotr Mierzwiński, Head of marketing at TMS Brokers S.A. TMS Brokers has been listed on the Polish stock market – NewConnect, since January 2011.

AFX Capital appoints Ricardo Onófrío Dytz as Sales Manager

AFX Capital, a global provider of online Forex trading services, has announced the appointment of Ricardo Onófrío Dytz as Sales Manager effective immediately. Mr. Dytz has joined the London-based team of AFX Capital which focuses on Western European, Northern and Southern American sales and market analysis. His main responsibilities will be the sales team management and office operations. Mr. Dytz was recently working for ActivTrades as an expert in Spanish and Portuguese markets. He has achieved a high level of success in establishing relations with IBs and Money Managers from Latin America, Spain and Portugal. In as little as 2 years Mr Dytz managed to expand the market, increase the company's presence and market share. He went from Sales Associate to Senior Sales Manager with a team of personnel covering the Portuguese and Spanish Desk.

"We are very proud to have appointed Ricardo Onofrio Dytz as the Sales Manager of the London office," – says Mario Persichino, the Global Business Developer of AFX Capital Markets. "His professional skills and experience in the industry will help the company increase our international market share. AFX Capital considers investment in new professional staff an important aspect of its globalization strategy, which also improves the company's reputation in the financial market".

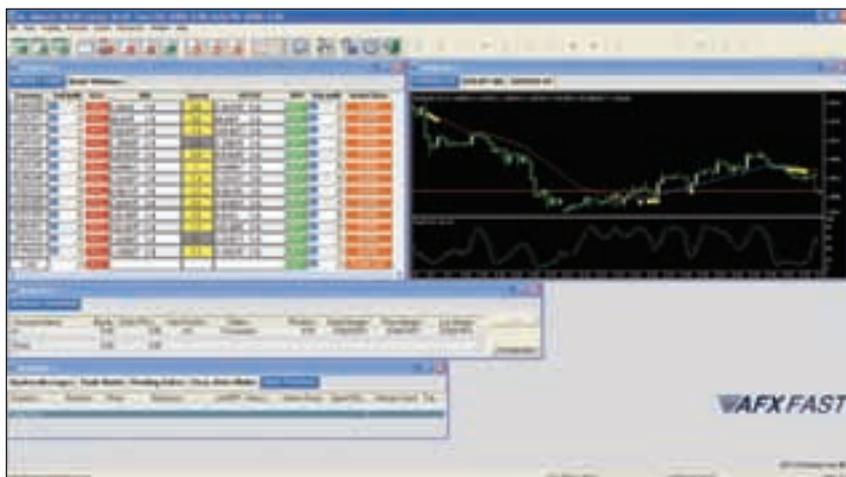
"I have a strong belief in the great range of products, the liquidity available on the platforms, and most importantly the level of professionalism of the support team and a great potential of growth in the near future of AFX Capital", said Mr. Dytz. "The company has proven constant

Ricardo Onófrío Dytz



growth with establishment of its offices in Cyprus and UK and a branch in Italy, looking at the nearest opportunity of opening further European offices and branches. I am delighted about this opportunity and looking forward to successful and productive work together with AFX Capital."

AFX Capital is an online Forex broker which offers access to all Global Markets using one integrated account with a complete product offering including Forex, Metals, Oil, Commodities, Indices and more. Customers have a choice of 5 leading platforms including the recent addition of institutional trading platform AFX FAST, which offers a professional trading environment.



AFX FAST Platform



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eases
import
tariff
concerns

superderivatives

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controls cost of
overseas shipping

**DUAL
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high-speed superhighways

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Correcting market imbalances and minimising over-regulation

Concerns that associated costs to introduce centralized clearing (CCP) of non derivative currency contracts may impair market participants, in particular the 'buy side' to preserve the ability to obtain economic pricing for currency risk management, were justified. Not to mention that CCPs would have increased concentration risks, as countless transactions would have had to settle through a few clearing houses.

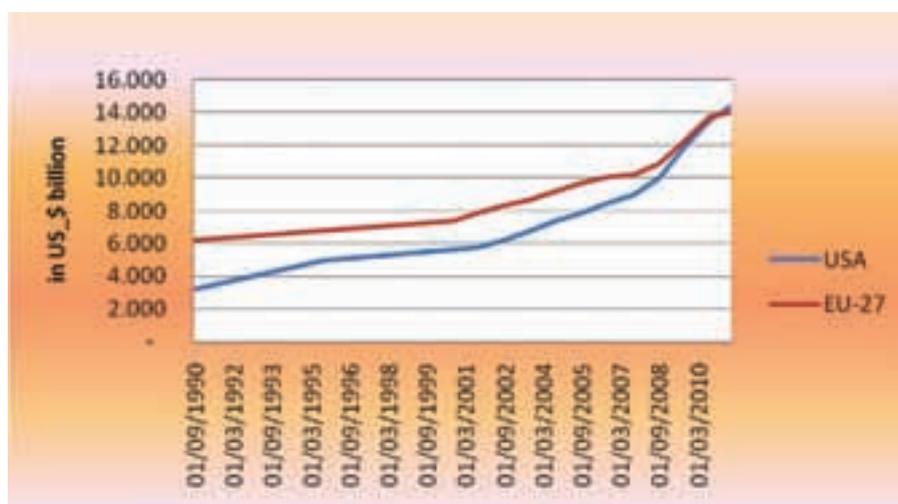
Furthermore, we agree with the logic underpinning the decision by the US Treasury in recognizing the unique factors of the Foreign Exchange market and the difference between FX Forwards / Swaps and other credit derivatives. The fixed terms of physical settlement, their short term nature and well functioning settlement process, have ensured that the FX market has continued to function continuously and efficiently throughout the market turmoil of the past three years.

We all recognize and support the effective progress achieved in the elimination of Settlement Risk, which has been achieved with the introduction of CLS Bank and other similar payment versus payment (PVP) settlement systems. In fact, the chairman of the Federal Reserve FX Committee noted that 'the committee has observed that the availability of the CLS was a key contributor to the robust functioning of the foreign exchange market during the recent period of financial market disruption.'

The recently announced 'proposed determination' by the US Treasury Department to exempt foreign exchange forwards and swaps from sweeping new derivatives rules, specified under the Dodd-Frank Act was welcomed by both financial and non-financial groups, alike. ACI regards this development as fundamental for the sustainability and effective function of stable and liquid (cash) markets.

Manfred Wiebogen
President ACI, The
Financial Markets
Association.

Recently, Stephane Malrait, our Chair of the ACI Foreign Exchange Committee commented *'Given the global nature of the FX markets and the challenges (operational, potential for arbitrage and otherwise) that could arise from geographical and cross-border regulatory inconsistencies, we do hope that the European regulators, in the first instance, will align themselves to this announced 'proposed determination' and recommend an exemption of foreign exchange forwards and swaps transactions from mandatory clearing.'*



Government Debt

I can say that all market representative bodies, AFME, ICMA, CME, ACI etc. endeavour in their work, not to “hard-sell” any position but rather to explain to regulatory entities the best practice standards for further well functioning markets. From our side, it can be said that Central Banks and Regulators do understand most of the concerns brought forward by banks, but the political pressure to change is enormous.

ACI World Congress

On May 26th – 28th, ACI held our 50th World Financial Markets Congress in Budapest with a large contingent of more than 500 participants from 56 different countries. The list included a large number of Central Bankers and Supranational representatives from the Hungary, Romania, Serbia, Czech Republic, Slovakia, Austria, Banque de France, India, Sri Lanka, Denmark, Germany, Poland, Australia, Sweden, Netherlands, the BIS, ECB, IMF and even SAFE (State Administration Foreign Exchange – China) participating in the meeting.

Some of the statements given by officials were fairly open minded and some, came as a surprise. Aiming at the other part of regulation, Basel III and its liquidity consequences, a Central Bank Board member stated that ‘the role of the banks is not to finance public debt but to finance the economy’. In a similar manner, the conclusions of representatives from the BIS and ECB when speaking in their personal capacity confirmed that ‘...there could be room for maneuver but it is to the banks to come up with initiatives and proposals’.

My opening remarks at the congress were aimed towards fairness vis-à-vis banks and their respective traders. Too many times and with little hesitation they have become blamed and criticized for nearly any mishap (financially or economically) that occurs.

Referring to the US debt situation, now reaching USD 14.400 billion, traders are obliged to protect their customers’ interests and their positions. This debt will twice cover the distance to the moon if it had to be piled up in one dollar bills on top of each other (!) and that is a distance of about 360.000 kilometers. But did you know that although the population is significantly larger, in aggregate, the 27 EU countries have a similar amount of debt.

Again, traders cannot turn a blind eye to this mount of debt and it has to be reflected, when quoting market prices or advising their clients. It is their obligation to deliver fair prices that mirror anticipated market movements in line with the interpretation of politics and macroeconomics.

So going forward, my approach would be to focus more on the original source of recent market and trade imbalances, instead of targeting banks and risking unforeseen consequences with (over) regulation. At the end of the day, the FX market has an unmatched track record of self regulation.

Measurements of over-regulation bear the risk of protectionism by preventing small and medium sized participants to grow. Let us not forget, the crisis started with AIG, Fannie Mae and Freddie Mac, didn’t it?

Re-engineering OTC FX Derivative workflows to meet new regulatory reporting obligations



By Frances Maguire

Whilst there is still uncertainty as to whether Europe will follow the US in exempting swaps and forwards from mandatory clearing requirements, it has been clearly stated by the G-20 leaders that all OTC derivatives contracts should be reported to Trade Repositories (TR). This was reaffirmed in June 2010 when the leaders met again and pledged to speed up the implementation of measures that will “improve the transparency and regulatory oversight of OTC derivatives in an internationally consistent and non-discriminatory way.”

Until the final Dodd Frank rules are released by the US Commodity Futures Trading Commission (CFTC) in July, it is still not known what kind of implementation time the industry will be given, although G20 has indicated the end of 2012 as a deadline.

EMIR

The European Commission has adopted the European Market Infrastructure Regulation (EMIR) to address issues relating to OTC derivatives, central counterparties and Trade Repositories, which will

work with the new MiFID (II), which focuses on execution and will specify the products to be covered by both sets of regulations, expected to take effect at the end of 2012, under the newly created European Securities and Markets Authority (ESMA).

However, EMIR is still a draft and not expected to be finalised until later this year, and then passed on to ESMA to make the final rules. Other G20 countries are also pushing forward, with the Hong Kong Monetary Authority into consulting on Trade Repositories. How these all interact with each other is an area that will need careful work over the coming years.

James Kemp, Managing Director, Global FX Division at the Association for Financial Markets in Europe (AFME) and its partners, SIFMA in the US and ASIFMA in Asia – says that while a number of asset classes have either started, or historically had, central warehouses for some of their data, particularly credit and rates, most pressing for FX is that under Dodd-Frank, these reporting rules will encompass all FX transactions, except spot. Even if FX swaps and forwards are exempt from clearing, there is still a requirement for FX swaps, forwards, options and NDFs to report to a Trade Repository.

There is already some debate about how many Trade Repositories there should be. Although there is nothing, in terms of competition, to limit the number, from an FX perspective, to maximise oversight capabilities, the Global FX Division expects regulators to prefer as few Repositories as possible because of the operational challenges and the need to have less fragmented data to oversee.

Kemp says: “There is nothing to say there cannot be a number of Repositories but it is probably more practical to have less rather than more. The US rules will soon set out the criteria for setting up a swap data Repository and, in the long run, we might expect market forces to move towards one main global Trade Repository”

Building a TR for FX

Representing 22 of the largest FX banks, the Global

FX Division has initiated a process to try and identify a provider of global Trade Repository services, enabling different suppliers to propose to the industry how they can build a Trade Repository for FX. He says: “This doesn’t mean it will be the only one and there may be local and regional ones as well, but everyone can see the sense that the fewer there are, the better a regulator would be able to make use of them, because they want to be able to look across as big a trade database as they can for surveillance. So, we are working with the industry to help meet these regulator time-lines. The more fragmented that Trade Repositories become the less the goal is met, as the

level of oversight the regulators have is reduced.” In terms of building several for geographical regions there are concerns about data being seen in different jurisdictions and there are differing privacy laws for data that will need to be overcome but this is going to have to be done at international level. “There are some regions that have restrictions on data movement so we are going to have to overcome those to get a truly global Repository,” says Kemp.

The Global FX Division is running some architecture group sessions at the moment to discuss the logistics of a FX Trade Repository. “Because it is a whole new area, there is a chance that the industry can streamline



the technology and do it once, rather than have, for example, multiple interfaces. We don't want to re-engineer various processes within the banks. There is a trade off to be had in re-using as much as possible - if we can piggyback on existing systems we can capture the trade flow from the different messages that already exist.

Kemp says: "It is huge undertaking. A Big Bang approach probably won't work – it will be too much – so we are going to have to have some kind of phasing and then look at the different services and how the data is integrated by the regulators as well as the real time aspect of the reporting."

Contenders

CLS, thought by some as a natural provider of such a Repository, has decided not to pitch to become a global FX Trade Repository. A spokesman for CLS says: "The design and building of a Repository of such a scale and extent is neither CLS' core business, nor our area of expertise. CLS remains committed to evaluate an appropriate role with regards to the FX TR and will collaborate with other interested industry participants on this to satisfy new regulatory requirements."



James Kemp

"It is huge undertaking. A Big Bang approach probably won't work – it will be too much – so we are going to have to have some kind of phasing and then look at the different services and how the data is integrated by the regulators as well as the real time aspect of the reporting."

The US Depository Trust & Clearing Corporation (DTCC) confirmed that it has jointly responded to an RFP from AFME with Swift to build a Trade Repository for FX.

A DTCC spokesperson says: "We understand AFME is running a process reviewing potential providers, so it wouldn't be appropriate to elaborate at this time. In general, we believe we have a design that can support multiple asset classes. After the review process has concluded, a provider may have firm plans in terms of establishing and operating an FX Repository."

Also involved in the pitching process is REGIS-TR, which was jointly launched by Bolsas y Mercados Españoles (BME) and Clearstream in September 2010.

Thilo Derenbach, Deputy Managing Director of REGIS-TR, describes the European Parliament's recent agreement concerning central counterparties and Trade Repositories in Europe, as "one very important step towards the goal of materialisation of the regulation in Europe". Once the European Parliament and the European Council have agreed the terms for OTC regulation, hopefully this summer, it will be put forward to the European Commission to be made law.

Reporting and clearing

Derenbach says: "The logic is clear. If the regulators want transparency and insight into the OTC derivatives market and if they want to understand which types of trades are being used and which firms have exposure to other participants in the European environment they will need to have position information of all OTC product types including FX products. It could be argued that FX products should be out of scope for clearing but from a regulatory perspective it makes sense to have them included in the reporting requirements so that regulators will have a clear and complete picture of the trading activity in the OTC derivatives market in Europe."

REGIS-TR is a co-founded and co-owned company run by two well-known European market infrastructures, Iberclear, a subsidiary of Bolsas y Mercados Españoles (BME) and the Spanish CSD, and the ICSD Clearstream Bank. It was launched at the end of last year for the collection of all types of OTC position data and a number of customers are already live for IRS. Another key difference between reporting and clearing is that while it is only banks and investment firms that will be obliged to fulfil the incoming OTC trading and clearing requirements, all firms, including corporate financial firms will have reporting obligations for commodity derivatives.

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According to Derenbach REGIS-TR's business model is very flexible and open, and differs from other existing business models because it has been developed around the incoming OTC regulation. He says: "We understand that all market participants will have to comply with the regulations, not just the bigger banks and corporates but any type of market participant trading OTC derivatives, and we have built our solution accordingly. There are very different needs and pain-points depending on the size, type and trading activity of the respective firm. We have established a business model for all types of market participants and covering all OTC derivatives. We will have all the products covered and will be able to accept all types of position data, from any type of market participant in Europe, well before the end of 2012."

Value added services

REGIS-TR, being fully operational for IRS already, will be able to accept all types of OTC derivatives except CDS products by the end of this year and extend its coverage to credit default swaps before the end of 2012.

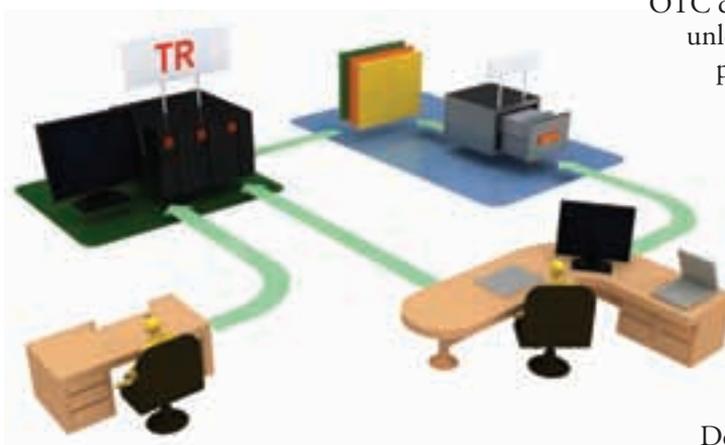
Derenbach adds: "In the meantime, from the beginning of 2012 to the end of the year, we will use this time in parallel for the development of value added services such as collateral management services, transaction reporting according to MiFiD and other services that will help participants deal with the additional regulatory costs that will materialise."

With the MiFiD II review underway, REGIS-TR intends to apply to be a so called 'Authorised Reporting Mechanism' so that REGIS-TR can not only report position data to ESMA but also transaction data to the national regulators, according to the MiFiD rules. "This will mean that market participants will not be obliged to open yet another reporting channel but use REGIS-TR for both reporting regimes."

Another element REGIS-TR wants to provide is value added services such as allowing members of Clearstream Banking the option to use alternative

collateralisation sources to cash. One of the prime alternatives is the securities collateral that members hold in Clearstream Banking and by linking Clearstream's collateral management system and REGIS-TR it will allow participants to use their securities collateral to securitise their OTC derivatives transactions directly out of Clearstream Banking.

Derenbach says that reporting for FX instruments has been conceptually developed and is currently being built into the system, with launch expected in late August/early September. He says: "With this launch we will be able to service the majority of the volumes market participants have. Many market participants are very concentrated in their OTC derivatives activity in IRS and FX products. It is usually a mix of these two and seldom do they also trade CDSs or further commodity OTC derivatives for example unless they are rather large players. This is why we have started with IRS and FX first so that we can cater well for the majority of participants prior to the materialisation of regulation."



Choice of Trade Repository

Derenbach believes the choice of Trade Repository will depend upon the type of market participant, their know-how and their activity profile. He says that two business models for Trade Repositories are emerging: one offering services for the larger banks and a more flexible model that caters for firms of all sizes, with different individual needs and concerns in terms of cost, connectivity, and legal and networking requirements.

There is also the issue of whether large organisations will choose a reporting entity for each asset class or want to access a single Trade Repository for the reporting of all their OTC derivatives transactions.

He adds: "The cost of compliance with regulation will depend on the structure market participants have. Many participants in the industry, particularly on the corporate side, are not used to such interfaces to regulators or CCPs and in the future will have to have interfaces to Trade Repositories. Nor do all corporate



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Powering Institutional FX



“It could be argued that FX products should be out of scope for clearing but from a regulatory perspective it makes sense to have them included in the reporting requirements so that regulators will have a clear and complete picture of the trading activity in the OTC derivatives market in Europe.”

customers and financial institutions have access to electronic matching platforms for OTC derivatives.”

Strategic decisions

Whether firms decide to set such link up to a Trade Repository separately or use the joint matching and reporting solution provided by REGIS-TR, Derenbach says will be a strategic decision that will influence the final cost of compliance to the participant.

Market participants in FX derivatives will have to decide whether to use a single Trade Repository or pick-and-choose from several providers. He says: “It is most likely they do not only trade FX swaps. They will have a choice of Trade Repositories and whether to connect directly to such a Repository. REGIS-TR offers access for all participants, regardless of size. They can connect through a low volume package, have a direct relationship but outsource trade reporting, or not interact with a Trade Repository directly at all but outsource the reporting of the position details completely to their counterparty.”

While it is expected there will be less than ten Trade Repositories across all asset and product classes, in total, in Europe, it is expected that there will only be a maximum of three, for FX reporting. “We believe in competition and it makes sense to have competition in this field as it allows for innovation,” Derenbach says.

He cites the collateral management services as an innovation that has grown out of competition, as well as the opportunity to double up and use a single Trade Repository for compliance with both EMIR and MiFID II or have transactions matched in the same environment where the reporting of the position takes place, as examples of where competition could increase the efficiency of the market and reduce business, operational and legal risks.

The clock is ticking

But Derenbach emphasises that time is running out and that participants should not delay their preparations in respect to regulatory compliance much longer even though the regulation is not finalised yet. He says: “By Autumn this year, market participants should have taken a decision on which Trade Repository and CCP they will use and start technically, functionally and legally connecting to those service providers to ensure adequate project phases for testing and back-loading all the existing transactions to the Trade Repository, in line with the draft regulation.”

Live contracts are likely to have to be back-loaded into a Trade Repository before the regulation becomes effective on 1 January 2013. This should be one of the biggest concerns for market participants. “We anticipate a run on Trade Repositories and CCPs from participants in 2012 and IT staff will need time to set up infrastructure and mapping rules to allow the customer’s in-house data to be transferred to the Trade Repositories. To avoid such bottleneck situations participants should foresee sufficient time to set-up their relations with TRs and CCPs,” he adds. However, despite the fact that an AFME spokesman says it will be “months, not weeks” before the outcome of the pitch is known, Derenbach stresses that time is short and that market participants need to start thinking about connecting to a Trade Repository now.

He says: “We are not talking about plain vanilla instruments only, particularly in the FX area and this means that possibility not all transactions will easily be transferred from in-house systems to the Trade Repositories. Possibly TR’s will need to enhance their systems initially and on an ongoing basis to be able to cater for all bespoke contract structures, which could equally delay the input process of position data.”

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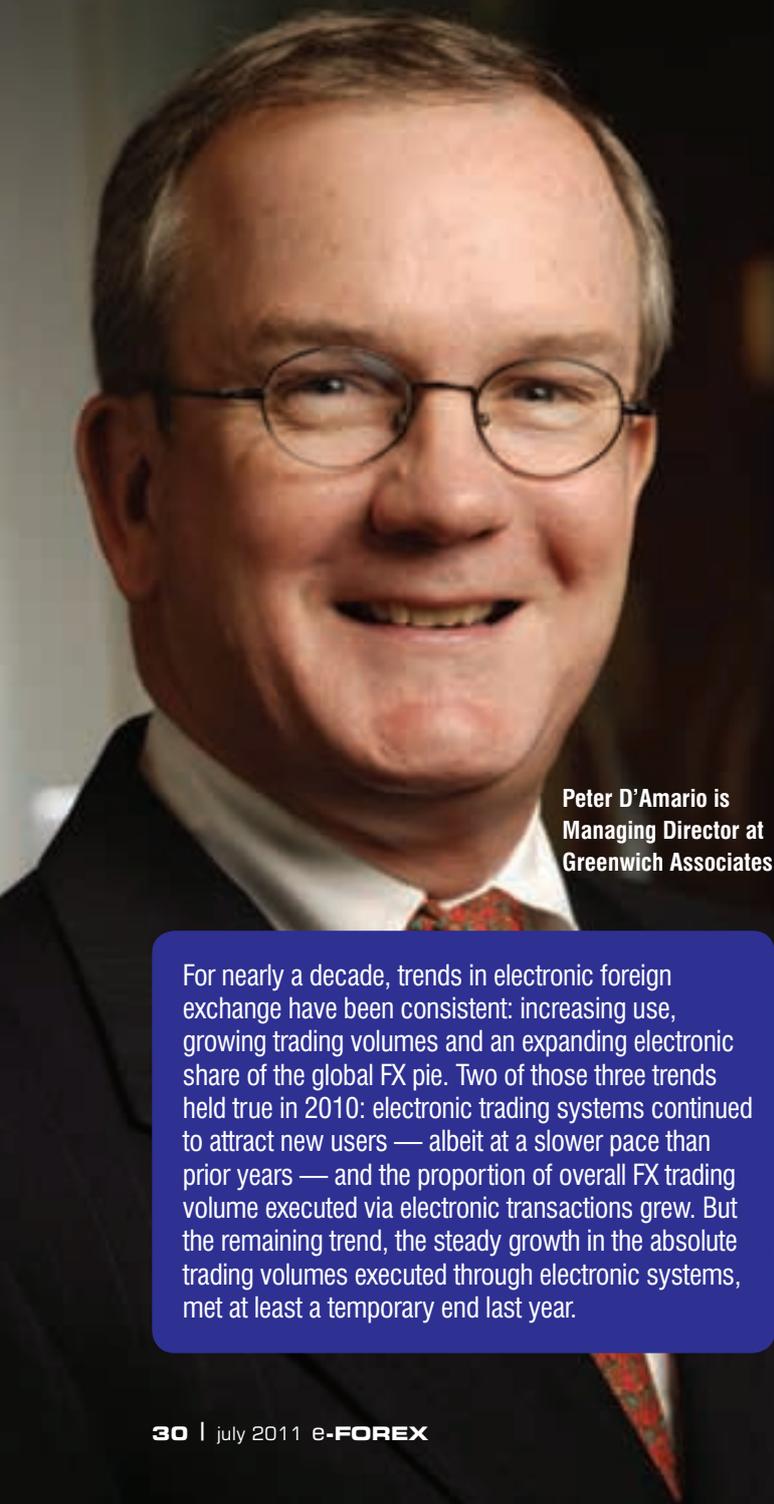
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In slowing market, E-trading systems capture FX trading share



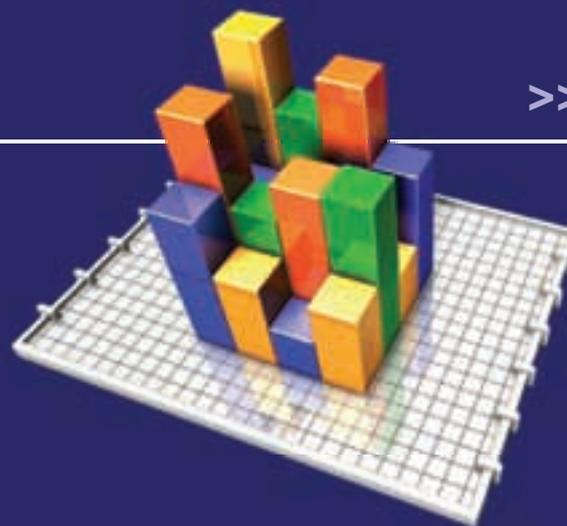
Peter D'Amario is
Managing Director at
Greenwich Associates

For nearly a decade, trends in electronic foreign exchange have been consistent: increasing use, growing trading volumes and an expanding electronic share of the global FX pie. Two of those three trends held true in 2010: electronic trading systems continued to attract new users — albeit at a slower pace than prior years — and the proportion of overall FX trading volume executed via electronic transactions grew. But the remaining trend, the steady growth in the absolute trading volumes executed through electronic systems, met at least a temporary end last year.

Greenwich Associates tracks overall foreign exchange trading volume among a universe of 1,563 end-user corporate and institutional customers; volume figures cited in the research exclude Tomorrow-Next Day (Tom/ Next) and other short-dated rollover trades. On this basis, the research results show that global foreign exchange trading volume declined approximately 13% from Q4 2009 to Q4 2010. However, the picture looks much different when Tom/Next transactions are allowed into the mix. Trading volume in Tom/Next and other short-dated rollover trades increased 68% last year. If these trades were included in total customer volume figures, overall global FX trading volume would have actually been flat to even slightly higher from 2009 to 2010.

Likewise, the total amount of FX trading volume executed through electronic systems declined by approximately 10% from 2009 to 2010, excluding Tom/Next trades. Since Tom/Next and other short-dated rollover trades are generally executed electronically, any significant pick-up in Tom/Next volume will have a correspondingly large effect on e-trading volumes. As such, when Tom/Next trades are included in the count, global e-trading volumes were essentially flat from 2009 to 2010.

While that decline in e-trading volume was consistent between financials and corporates worldwide, the slowdown was not evenly spread among regional FX markets. To the contrary, any drop in global eFX trading volumes last year would have been driven almost entirely by declines in Continental Europe, where e-trading volume totals declined 20% from 2009 to 2010, and in the United States, where electronic trading volumes fell 18%.



Meanwhile, eFX trading volumes on that basis increased approximately 3% in the United Kingdom and 15% in Japan. Volume increases were also recorded in the much smaller markets of Latin America and Australia/New Zealand. The gains in e-trading volumes in Japan and the smaller regional markets mirror patterns in the foreign exchange market overall. From 2009 to 2010 overall foreign exchange trading volumes increased 12% in Japan, and 33% in Australia/New Zealand.

The growth in the United Kingdom is something else entirely. The fact that electronic trading systems were able to maintain and even increase their absolute levels of volume in a period in which overall U.K. trading volumes were down 8% represents a significant achievement.



Year-over-year percent change in Foreign Exchange Trading Volume vs. Foreign Exchange e-Trading Volume*

New users, bigger share

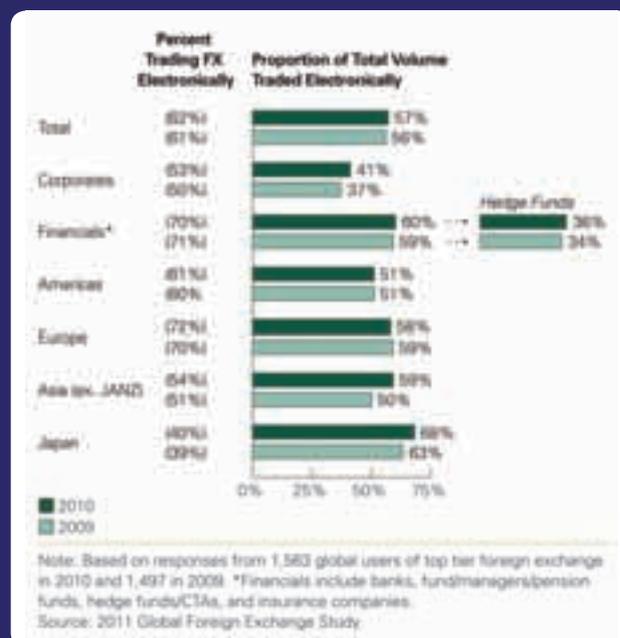
Trading platforms pulled off that feat in the U.K. by both attracting new customers last year and capturing a growing share of trading business from existing customers. In the United Kingdom, the share of FX market participants engaged in electronic trading grew to 77% in 2010 from 73% in 2009. Meanwhile, U.K. e-traders increased the share of their overall foreign exchange trading business executed through electronic systems to 64% from just 61%.

Such rates of growth easily top those of the global market overall. Worldwide, the share of FX market

participants trading on electronic systems increased to 62% in 2010 from 61% in 2009. That average pick-up rate included an increase to 40% from 39% among Japanese market participants and an increase to 69% from 68% among market participants in Continental Europe. Among the world's largest and most active FX traders — those generating more than \$50 billion in annual trading volume — 86% now say they trade electronically, up from 83% in 2009.

Globally, market participants that use eFX increased the share of their total foreign exchange trading volume executed through electronic channels to 68% in 2010 from 64% in 2009. As in the United Kingdom, eFX users in the United States made a big move in this direction, increasing the share of their total volume executed electronically up from 61%. In Japan that share increased to 88% from 85% and in the rest of Asia (ex-Japan, Australia/New Zealand) the proportion grew to 69% from 56%.

Electronic platforms' ability to attract new users and capture a bigger share of overall volume on a global



Electronic Trading Volume

basis expanded the profile of e-trading systems within the context of the broader foreign exchange market. Worldwide, eFX now represents 57% of global foreign exchange trading volume — up from 56% last year. In Continental Europe electronic trading platforms captured a steady 60% of total foreign exchange trading volume from year to year. In the United Kingdom, where electronic trading systems experienced increases in both number of users and share of these users' trading wallet, eFX decreased as a proportion of total foreign exchange trading volume to represent 56%, down from 57% in 2009.

Retail Aggregators

Perhaps the biggest driver of the declines in both overall foreign exchange trading volume and eFX volumes last year was the slowdown in activity on the part of retail aggregators. Overall foreign exchange trading volume among a matched sample of 25 of the world's largest retail FX trading aggregators fell 47% from Q4 2009 to Q4 2010.

Even in Japan — where total trading volumes increased last year and FX trading remains a near passion among retail investors — trading volumes generated by retail aggregators declined 12% on a matched sample basis. The falloff was essentially the same in electronic foreign exchange: while eFX trading volume was essentially unchanged from year to year among banks, fund managers and pension funds, electronic trading volumes generated by retail aggregators declined 49% from 2009 to 2010.

Hedge Funds

Electronic trading platforms captured 36% of hedge fund foreign exchange trading volume last year, up from just 34% in 2009. In a year in which the absolute amount of foreign exchange trading volume generated by hedge funds declined, hedge funds' total eFX trading volume actually increased 19%. That growth was the result of increases in both the share of hedge fund FX market participants using electronic systems and in the share of total FX trading volume routed to electronic platforms by these users.

In 2009, two-thirds of hedge funds active in foreign exchange markets traded FX electronically. In 2010 that share remained the same. Over the same period, the share of total FX trading volume executed electronically by hedge funds that trade online jumped to 57% from just 40%.

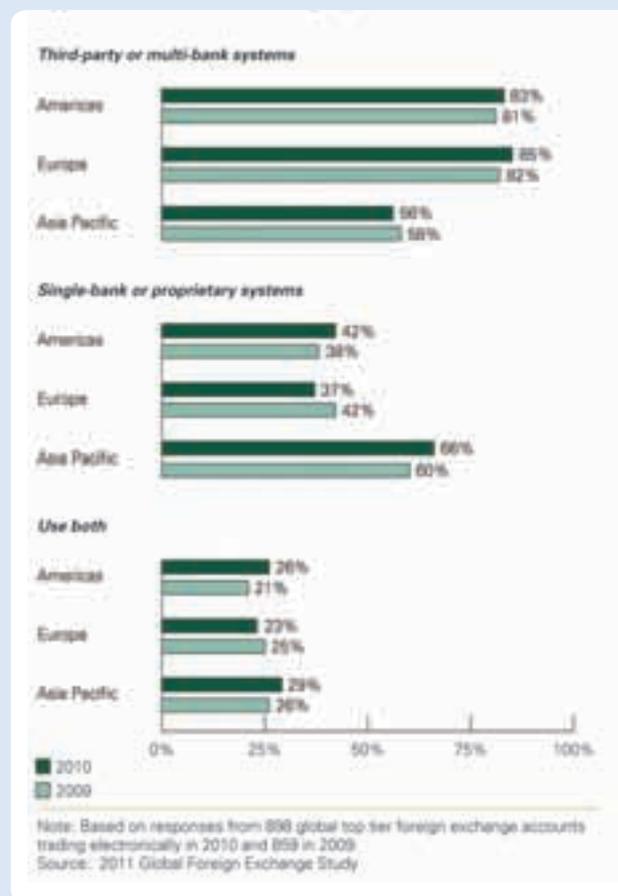
As a result of that growth, hedge funds now account for 11% of total electronic FX trading volume, up from 9% in 2009.

FX traders hanging up the phone

With electronic trading volumes fast approaching 60% of the global foreign exchange market, the share of volume executed through telephone transactions is shrinking. Among market participants that use electronic platforms, the share of total FX trading volume conducted by telephone declined to 28% in 2010 from 30% in 2009.

Meanwhile, the share of total global FX volume executed by this group through multi dealer platforms increased to 43% in 2010 from 40% in 2009. Much of that increase can in turn be attributed to shifts among the world's largest and most active FX traders.

Among market participants generating more than \$50 billion in annual FX trading volume, the proportion using multi-dealer platforms increased to 40% in 2010 from 34% in 2009, while the proportion using



Type of Electronic Trading System used

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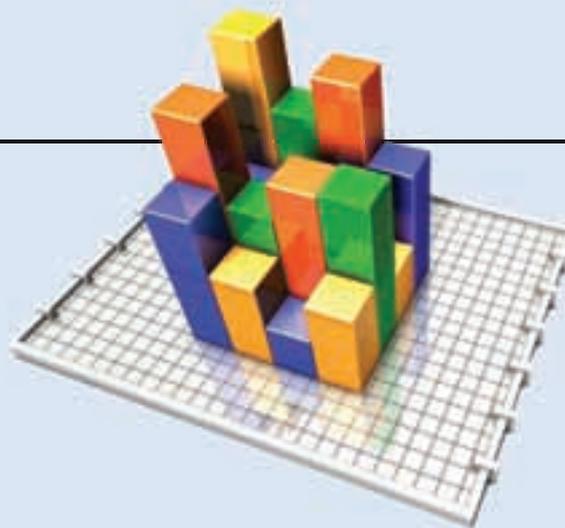
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APIs: Mainly a Tool For Retail Aggregators

About a quarter of banks around the world and about one-in-five hedge funds use APIs for foreign exchange trading. Despite that not insignificant level of uptake, the main source of demand for these sophisticated trading platforms are the world's large retail aggregators—about 60% of which use APIs to facilitate price discovery by integrating feeds from multiple banks.

Use of API



Note: Based on responses from 983 global top tier foreign exchange accounts trading electronically in 2010 and 908 in 2009. ¹Other financials include broker/dealers and credit companies. ²Includes treasury centers.
Source: 2011 Global Foreign Exchange Study

single-dealer platforms fell to 17% from 19%. Some of the business that was until recently conducted by phone is also moving to messaging systems like Bloomberg and Reuters.

Growing preference for third-party platforms

The study results suggest trading volumes shifting away from telephone-based transactions will increasingly move to third-party or multi-bank platforms. Globally, the share of eFX traders using third-party or multi-bank systems inched up to 78% in 2010 from 77% in 2009, while the proportion using single-bank or proprietary systems held steady at 45%. However, a closer look at the data reveals a bigger shift in Europe, where the share of eFX traders

using third-party or multi-bank platforms increased to 85% from 82% and the share using single-bank systems fell to 37% from 42%. Likewise, among the biggest and most active FX traders in the world — those generating more than \$50 billion in annual trading volume — use of third-party or multi-bank platforms jumped to 81% from 78% and the use of single-bank systems dropped to 52% from 56%.

These two groups, the market's most active traders and companies and financials in Europe, represent the most experienced and often most sophisticated foreign exchange traders in the world. Since trends that originate with this cohort generally carry over to the broader global market over time, we anticipate a continuing, gradual shift among users of electronic foreign exchange to third party and multi-dealer platforms.

Members of another group of sophisticated traders — hedge funds — increased their use of both types of systems last year. Hedge fund use of third-party or multi-dealer systems increased to 62% in 2010 from 53% in 2009. At the same time, use of single-bank systems ticked up to 66% from 64%.

While eFX users in the United States and Japan both shifted in step with their European counterparts toward greater use of third-party and multi-dealer systems last year, users in Asia (ex-Japan, Australia/New Zealand) moved in the opposite direction. In Asia, use of third-party or multi-bank platforms declined to 56% of eFX users in 2010 from 70% in 2009 and use of single-bank systems increased to 77% from 70%.

Methodology

Greenwich Associates conducted in-person interviews with 1,563 top-tier users of foreign exchange services at large corporations and financial institutions on market trends and their relationships with their dealers. Interviews were conducted in North America, Latin America, Europe, Asia, and Japan between September and November 2010. The findings reported in this document reflect solely the views reported to Greenwich Associates by the research participants. They do not represent opinions or endorsements by Greenwich Associates or its staff.



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From desktop to API - meeting new demand for FX Option platforms



By Frances Maguire

With all other instruments traded electronically and with new technology available for trading FX options, interest is now turning to the last bastion of telephone trading, writes Frances Maguire.

Getting the comfort levels to trade the more complex FX products electronically has taken longer than expected but coupled with the recent advancements in trading technology, the time is ripe for a final push towards the e-trading of FX options. Already first generation FX options are being traded on screen and with two new FX options platforms set to launch – one of them bringing an ECN-style platform to the FX options market for the first time – it looks as though a breakthrough has been made and one that will even bring new participants to the market.

Increasing demand

Ralf Behnstedt, managing partner of FX Architects International, a team of FX specialists advising on how to strengthen FX business and operations, believes that the increasing global demand for FX options is based on a variety of factors, not least because the financial turmoil and the resulting increase in regulatory requirements is forcing the sell-side to review the business models for providing OTC derivatives. He says: “The focus is shifting clearly towards cash and



plain vanilla products and this is forcing the sell-side to rethink distribution strategies. Ultimately we will see increased hurdles to market structured OTC derivatives and stronger demand to hedge client exposures using the FX cash and plain vanilla product spectrum.”

This is because Behnstedt believes the buy side is logically looking for the next asset class on the electronic channel now that simple cash products have been available for more than ten years. He believes that FX options are the next logical step for the buy side as plain vanilla FX options are increasingly becoming commoditised. Furthermore, the opportunities in the FX market are currently outstanding, with huge volatility in some currency pairs and the buy-side want a quick and easy way to take advantage of this.

However, Behnstedt says that a few challenges have still to be addressed on the FX trading platforms to meet buy side requirements and before a distinctive value proposition can be offered to the client base. He says: “First of all, similar to FX cash products, entering and capturing FX options must be simple and easy. Leveraging graphical features to facilitate FX options’ trade capture processing is inevitable.”

He says that apart from Oanda’s box option feature, which marked a new and innovative way to capture two options by drawing a window box on a FX chart, there have been very few solutions that are easy to understand and allow ease of use FX options’ trade capture.

Behnstedt says: “Demand is strong and vendors would be well advised to put effort into developing a solution that meets users’ expectations. Enabling trade capture FX options using an electronic trading solution is no longer considered ‘state of the art’ technology. Solution providers have to combine an electronic offering with using portals and mobile solutions. Innovative product and service offerings are required to market FX options via electronic distribution channels. New ways to present data and provide information are required. Solutions cannot just provide the information in tables as it has been done on paper before.”

He believes that as technology evolves the opportunities to create superior services to enable traders to view, execute and analyse FX options and their underlying data will grow. “Clients are expecting services like getting information based on pre-defined triggers, e.g. delta of an FX option reaches a pre-



Ralf Behnstedt

“Clients are expecting services like getting information based on pre-defined triggers, e.g. delta of an FX option reaches a pre-defined level or an ITM FX option has produced a pre-defined amount of return.”

defined level or an ITM FX option has produced a pre-defined amount of return. All these items are demanded and the demand will continue to grow,” he adds.

Capturing, processing and monitoring

Behnstedt also says that solution providers are also increasingly being asked to create packages which help clients in capturing, processing and monitoring FX options during the lifecycle of the trade, using graphical tools, to improve the decision making processes. “Just as in the era of establishing electronic FX cash trading solutions, once the client has made a decision for a specific electronic FX options platform the hurdles for competitors are higher to win that client back,” he says.

Unlike the sell-side, Behnstedt believes that the buy-side is looking at their traded products from a portfolio perspective and not from product silos, but

the digitisation of FX options, will force the sell-side to rethink and reorganise existing product silos and to interconnect silos within client portfolios. He says: “Clearly, if the client wants to hedge an underlying FX exposure, there are many ways to do so, for example it could be done using cash products or using options. Clients want to see alternative scenarios and compare them in order to make the right decision. Providing these decision-making features electronically, interlinking the silos and making historical trade data as well being part of that process will require serious innovation to create these value propositions.”

Finally, Behnstedt says that less is more when it comes to new technology and solutions providers are better off developing fewer products than risking not getting it right. “Establishing the whole business proposition -- from electronic trading, mobile application and portal integration - with just a couple of products is the better strategy than developing the whole FX options spectrum into an electronic trading solution but missing out the mobile application and portal integration. Strong project leadership, management focus, creative business analysts and experienced state of the art development teams are required to get that done.”

Impact of Clearing

For David Collins, head of strategic solutions at SuperDerivatives, the various factors affecting FX options trading arena are colliding. Firstly, he says, the need to clear FX options is forcing a pure OTC market to reconsider the way it operates and realise that benefits have been reaped in other markets through clearing platforms and electronic workflow. “This will help level the playing field for many smaller regional banks as credit will play less of a role in price than before,” says Collins.

Secondly, legislation may not yet be finalised but potential Swap Execution Facility (SEF) requirements and the need to show best execution, is making end-users reconsider the benefits of some of the banks’ direct execution platforms. Thirdly, FX is emerging as an investment asset class and can be traded by people who are used to electronic markets.

Says Collins: “This is all leading to increased interest in electronic execution which many see as a disruption event to the dominance of a few large banks. We are seeing specialist players emerging and wanting to play



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a major role in specific currency pairs e.g. Nordics or Emerging Market Currencies, as they see electronic execution platforms as a large channel to market. In addition, as vanilla flows are being commoditised, banks are driven towards electronic execution in order to retain market share and reduce cost per trade.”

He believes that it is too early to tell whether, and how, users will be able to further leverage the trading metrics generated by their e-platforms for use in other applications. He says: “It will take time for the platforms to gain the traction they need; we see this as the start of a journey of transition and do not expect it to be a big bang.”

He does believe, however, that FX will continue to grow in use as an investment asset class and there is still much to learn from the equity markets. “We think there will be continued growth in high frequency and algorithmic trading in FX and that this may spread into the options market but we believe that the pattern will track the equity markets,” he adds.

Innovation not emulation

For Collins the most successful strategies for delivering next-generation e-services will be the ones that innovate. He says: “Technology that just emulates the existing OTC markets on a point to point basis will bring little to the market; the future lies in one or many platforms that bring a new dimension to the OTC markets.”

The possible introduction of SEFs and clearing for FX options will have a huge impact on the market and will change forever how FX options are traded. “Execution through anonymous platforms will change relationships with bankers and brokers. Some of these relationships could be replaced by social media and specialist service providers will have a chance to enter a broader market, offering advice and research that is independent of brokerage and trading positions,” says Collins.

Stephen Best, CEO of FX Bridge Technologies, believes demand for FX options is coming from the maturation of individual spot FX traders, who are looking at new products as well as by new entrants who have experience trading options in other asset classes.

Best says: “One of the most important things when introducing options to new retail clients is for broker-dealers to give them the comfort level with the different instruments and strategies they need. To this end, FX Bridge has developed a robust education package which includes a Strategy Optimizer tool that allows the end-users to evaluate the different strategies and determine the best one for them.”

He says: “Historically, many of our clients have used our analytics to construct their own volatility surfaces and to make their own markets, but there is now a growing number of brokers that want to offer FX options to their end-trader clients but are not comfortable with managing an options risk book themselves.”



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David Collins

“Technology that just emulates the existing OTC markets on a point to point basis will bring little to the market; the future lies in one or many platforms that bring a new dimension to the OTC markets.”

At the beginning of this year, FX Bridge therefore went live with functionality that allows brokers to pass the risk on, and source liquidity from market-making banks, so they do not have to manage this risk.

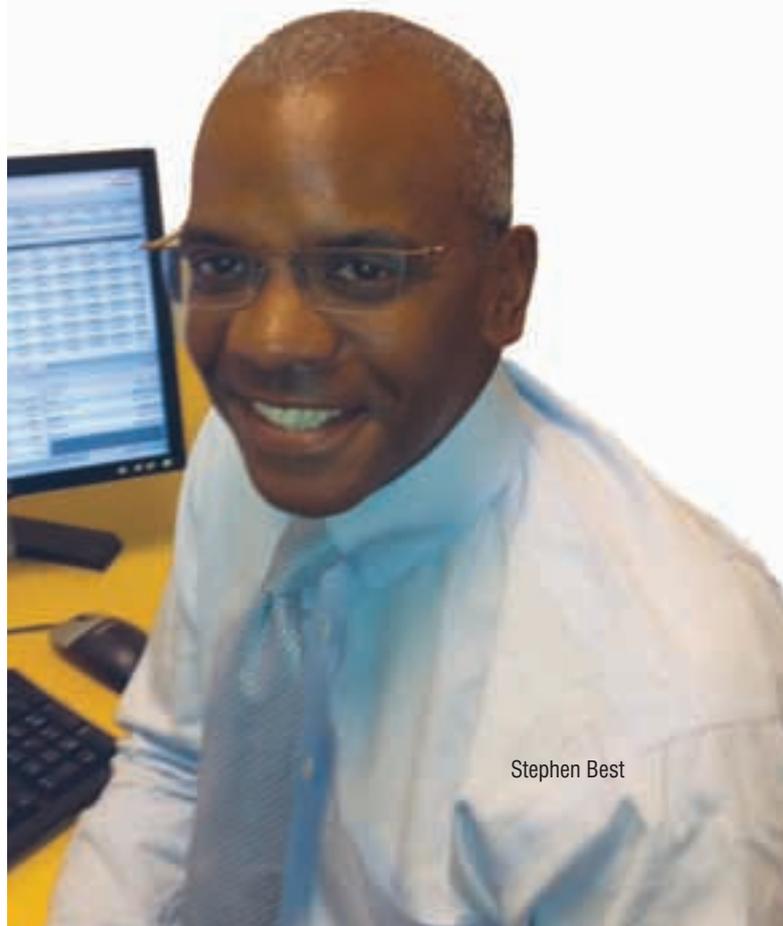
For the broker-dealers, FX Bridge has filled out its risk management offering to enable them to see their client risk, across spot, options and CFDs, on a single screen and run ‘what-if’ scenarios. The end-to-end solution, from decision support, execution and liquidity provision to risk management, provides all the reporting and compliance tools needed, across all jurisdictions. The platform can also be specifically customised for each broker-dealers’ reporting requirements, and, in fact, Best says, no two client systems look the same. FX Bridge can offer a broker-dealer linked multiple platforms for different client groups, or by product, and still risk managed in a single application, regardless of whether they decide to manage the price risk in-house or pass some or all of it on to a liquidity provider.

Next round of growth

Best believes that the growth of equity options over the past ten years is a good indicator of what is in store for FX options. He says: “One of the drivers behind this growth is that options were being offered in equities. FX options have not really been offered electronically as extensively, but we are seeing increased automation and there is already some algorithmic and high frequency strategies being used for FX options.” The FX Bridge platform has a published API to enable electronic trading and Best believes that this will increase rapidly for FX options.

“Every bank and broker offers a platform for spot FX, but just a handful offer FX options trading, and that is where the next round of growth will come. What is important now is having a strategy around taking advantage of the growth there will be in FX options.” He believes the provision of training is crucial to support this growth and FX Bridge has a comprehensive educational package that brokers can white-label and brand for both staff and customers.

“Electronic trading ends arguments, by providing an audit trail and a log. Phone trading has a history of miscommunication. As legislation pushes us towards automated ways of settling, the entire end-to-end process will follow.”



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Working with the biggest FX banks, FX Bridge has contributed to the standardisation of fixed APIs and electronic processes and Best believes that the implementation of clearing for FX options will only push users more towards electronic trading and straight through processing. This can only be a good thing, says Best, not only for the automatic audit trail provided by electronic trading. He says: “Electronic trading ends arguments, by providing an audit trail and a log. Phone trading has a history of miscommunication. As legislation pushes us towards automated ways of settling, the entire end-to-end process will follow.”

Regulatory pressures

Alfred Schorno, Managing Partner and head of sales at 360 Trading Networks, says, “What is holding back the growth, as well as further investment in technology by market-makers, are the regulatory discussions around the Dodd-Frank act.”

However, he says that demand from the buy side for FX options is still very strong and 360T is also getting more demand from the large banks. In fact, the number of FX options executed electronically on 360T has grown by more than 400% over the last year, boosted by the growing number of market makers quoting prices for FX options.

Schorno believes the implications from the regulators are that all derivatives, including FX options, will have to be traded on multi-bank venues, such as Swap Execution Facilities (SEFs) or the European equivalent, Multi-lateral Trading Facility (MTFs). These venues are not to be fully owned by bank market participants.

He says: “This clearly rules out single dealer portals that are 100 per cent owned by one market participant and telephone dealing. When this ruling comes, all FX derivatives will have to be traded electronically and single dealer portals will no longer be allowed to support trading in NDFs and FX options. We expect therefore a strong boost to this business and we are structuring our business to support this expected shift.”

The functionality built by 360T to trade FX options includes structures such as a risk reversals and multi leg option requests. Currently requests are priced manually but going forward Schorno believes that market maker banks will start supporting multi-bank portals with auto pricing instead of investing in their own single bank portals.

Furthermore, he strongly believes that FX options, first generation at least, are sufficiently standardised that they are tradeable electronically, and on a multibank portal.

He says: “When users first start to use a portal, they only use the functionality on the main, standard product. Then the more exotic instruments, such as FX options and NDFs, are gradually accepted over time when they become more comfortable with the electronic functionality. It is an evolution process. But already there is a clear tendency towards trading FX options electronically, just as there was seven to ten years ago for spot and forwards.”

360T has offered a request-for-quote functionality for FX options on the portal for the past three years and in the last year further enhanced the functionality to enable trading, not just on the life-basis, but also with a separate delta hedge, to enable trading on a volatility basis. There is also functionality for standard options – call, puts, European and American style – as well as smaller structured products such as risk reversals, bull or bear spreads. STP has been achieved for those customers that have high options volume, using a

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XML deal export interface to treasury management systems, which was not very a common three or four year ago, according to Schorno.

He says: “We focus on first generation only, and 360T concentrates only on communication and execution. There are no analytics as we focus on a best-of-breed approach and believe there are already systems out there for pre- and post-trade analytics, instead we are looking at linking into such analytics tools. For post-trade, STP is available when transactions are executed into position-keeping systems.”

Schorno says there is demand, on the institutional side, for hedging and leveraging, as well as generating alpha and the demand from the corporates is for physical and non-specific hedging. However, he adds, over the past few years there has been a backward towards plain vanilla, and less exotic, products. Schorno also believes that another area of growth will come from greater integration between execution venues and the providers of analytics, by embedding



Alfred Schorno

“What is holding back the growth, as well as further investment in technology by market-makers, are the regulatory discussions around the Dodd-Frank act.”

execution tools into portfolio analysis tools and treasury management system products.

ECN model

Two new platforms offering electronically traded FX options, which are based around different business models are about to launch. Evgeni Mitkov, CEO of SURFACEExchange, says that their new platform is still on-boarding clients and has been testing for eight months. The platform, which will be the first open ECN for FX derivatives, will trade spot, forwards and options in the G10 currency pairs.

There have been other attempts to trade FX options electronically, such as GFI, Icor (Reuters) and Volbroker and Mitkov believes not only that the lessons have been learned, but that this time around, the dynamics and timing have changed.

He says: “The buy-side has grown; the timing is better and most importantly we are not beholden to any particular player. We have taken the best from both worlds: the OTC contract specs and the electronic exchanges’ central limit order book. This resulted in a neutral marketplace that works for every institutional player. The electronic derivatives exchange market format has grown exchange traded derivatives volumes at 30-40% annually, and we are looking to do the same in FX.”

If we assume that every aspect of options’ trading will ultimately be made electronic, then there will be no manual processes at all. This is something that Mitkov believes will empower smaller players and will enable them to participate on an equal footing with the big players. “Initiatives in the past only offered electronic execution, while still requiring heavy manual intervention post trade.”

Automating the entire lifecycle on the SURFACEExchange platform makes it very easy for any sized bank or hedge fund, with a limited number of traders, to participate actively and not be afraid of the post-trade operational issues.

Mitkov adds: “Our independence is viewed as a great asset as people are comfortable trading with us and pleased that nobody is seeing their trades or acting upon the information that they leave behind in the platform.”

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Evgeni Mitkov

“On the options side there is very big gap between major banks and the rest of the participants in terms of technology, in terms of understanding the markets, and in terms of how they trade.”

Furthermore, the platform works differently for the different players. He says: “On the options side there is very big gap between major banks and the rest of the participants in terms of technology, in terms of understanding the markets, and in terms of how they trade. A small player might think in terms of premium whereas all the big banks think in terms of volatility and in delta hedge trades. We enable those two different marketplaces to meet in a single liquidity pool by just using technology. We can match the two counterparties and the SURFACEExchange becomes the translator between those two counterparties. Using technology we make the meeting of the most sophisticated traders and market makers with hedgers a lot easier.”

High frequency and systematic trading

High frequency and algorithmic trading has long been tipped as a growth factor and Mitkov believes the technology which underpins SURFACEExchange is geared to high volume in the expectation of the market to move in this direction. He says: “Clearly most players do not have high frequency technology in FX derivatives, but we have accounted for the market evolving in this direction and we are ready to support

this kind of trading. By building with 2010/2011 technology, we also safeguarded against our platform creating latency arbitrage opportunities.”

While high frequency trading is not expected to happen immediately, Mitkov does expect a greater roll-out of systematic trading models, another area that has been underdeveloped in the FX options world. “Systematic traders face serious challenges where they have to pick up the phone and call five banks and ask for prices. They also have a number of good models sitting on the shelves. However in an ECN, with all types of prices available, we permit existing models to be tuned to generate signals more often and shelved models to be deployed, becoming another source of liquidity to the marketplace,” he adds.

New players

While FX options are poised for growth, Mitkov says that the players that will bring this new growth are not in the marketplace yet. One of the biggest sectors is the second tier and regional banks, which cannot afford to participate in the interbank market but see increased demand from their customers as a result of greater volatility. The ones that are in the market are simply trading back-to-back with one or two banks, globally and, he says, the demand from these institutions is to see a multi-contributor, independent, unbiased price that is available to them in real-time.

There is also a renewed interest in FX as an asset class from pension funds and as a result a lot more money has been allocated to hedge funds. A lot of bank traders have now moved on to set up proprietary trading shops or hedge funds and need a platform where they market-make/take, similar to the tools they had when they were at a bank.

There are still more potential new players, says Mitkov, that are still not in the market and avoid OTC FX options because they are not electronic, require a lot of manual processing, and there is no unbiased trading venue available. The only way to trade OTC FX options is to pick up a phone to a bank and these professional traders do not pick up phones – they have servers and they cross connect.

One particular example is the equity options prop shops and market-makers. They have seen serious correlations between equities and FX, while equity volatility is three to four times higher than FX

volatility. They want to vega-hedge their equity exposure with FX, but currently CME is the only venue offering electronic trading in FX options.

He says: “With six interbank players disappearing in the crisis the liquidity has suffered massively. There is a serious dislocation between the liquidity provided by the banks and by the assets under management at the buy-side firms, which has increased significantly over the last few years. Banks don’t market-make as much as they used to and buy-side firms have much more assets to deploy in this market so it is a lopsided market at present, while there are plenty of new players willing to fill the void.”

Multi-bank model

Mark Suter, CEO of Digital Vega, says that its new electronic FX options trading platform, Medusa, which is in pilot phase, will shortly be rolled out to a diverse group of more than 30 buy-side firms covering corporations, asset managers, regional banks and broker-dealers. Liquidity will be provided by an initial group of 7 major banks, with this number expected to increase to 12 by year-end.



Mark Suter

“Until recently, I did not believe the technology existed to trade FX options electronically very well, but now there is much greater flexibility and participants are investing in new technology.”

The first release of Medusa will offer single vanilla options, straddles, strangles and risk reversals, with or without hedges, and will start with six currency pairs, which Suter says will be rapidly expanded once the platform is in operation.

Electronic trading platforms for FX options have been attempted before but Suter says that the ease of use of the platform will be a key to its success. He says: “It is a very easy to deploy a browser-based solution – it runs on any browser or platform, This is combined with the fact the platform will bring much needed transparency to FX options. Meeting regulatory requirements means greater transparency is needed, and proof of best execution so we have already built a lot of analytics and reporting into the platform.”

“Until recently, I did not believe the technology existed to trade FX options electronically very well, but now there is much greater flexibility and participants are investing in new technology. It is all being driven increasingly by the regulators, especially in the US, with the Dodd-Frank act. The drive towards electronic trading has been given a boost by the fact that foreign exchange options will now have to trade on a Swap Execution Facility (SEF) in the US, once the Dodd-Frank is in place.”

Conclusion

Suter believes the move online had already begun following demand from the buy-side community, as part of the evolution of what has happened in the FX cash market. In preparation for this, Digital Vega has built the tools to provide straight through processing functionality and is working with partners to deliver more complex STP solutions, building on what market participants have already delivered for FX spot and forwards over the past ten years.

However, despite this, Suter believes that some of the more exotic options will never successfully be electronically traded. He says: “Exotic currencies, yes, but exotic options are not an area we will venture into – they are too customised and specialist, and do not lend themselves easily to platform trading. We are looking at the more commoditised, more liquid products.” He believes there is now sufficient flow that can be traded electronically; as additional products and services are added to the platform and, against a backdrop of increasing regulatory pressure, he feels that the opportunity can only continue to grow.

Developing new Back Office and clearing connectivity services for FX

Connection to CCPs, Swap Execution Facilities (SEFs) and Trade Repositories will add another layer to an already complex and sophisticated automated system, writes Frances Maguire.

All aspects of the FX trade life cycle, pre-trade, trade and post-trade will be greatly impacted by the incoming regulations for OTC instruments and the systems in place to support this workflow, including telephone based trades, will need to be reviewed. Most importantly, credit risk systems will need to reflect changes in credit risk due to CCPs, while trade processing systems will need to be enhanced and configured to include OTC instruments for the newly established Trade Repositories.

Aggregation

Further to this, Gil Mandelzis, CEO of Traiana, says that the introduction of aggregation, such as that offered through the CLS Aggregation Service (CLSAS), a joint initiative between Traiana and CLS, and through Harmony NetLink, a retail aggregation solution offered by Traiana, provides an intermediate step that will also significantly change the way front to back office processing operates in FX. Last year, Traiana and CLS joined forces to enable aggregation of trades from post-trade through to settlement. Harmony NetLink provides a similar offering for firms aggregating trades from retail customers.

Mandelzis says: “Both CLSAS and Harmony NetLink aggregate trades before they get to the back office and are settled. By providing these solutions, we have changed the way the trade flows work to increase capacity and reduce risk in the industry.”

Mandelzis says that getting an affirmation of the trade before it is aggregated makes a huge difference to the efficiency of the back office, and in achieving real-time risk management of trades. Using these solutions, not only is operational risk reduced but trading capacity is also better managed. Using CLSAS, banks can dramatically reduce their volumes quite often arising from their prime broker businesses. Reducing these volumes equates to a significant improvement in operating efficiency and capacity.

Likewise, using Harmony NetLink retail FX market participants can reduce costs and decrease risk by



compressing tickets in a controlled and automated environment. Liquidity providers and retail platforms benefit from lower cost processing while still having visibility into the original tickets (called component trades) so they can manage their exposure.

With clearing for FX on the horizon, Mandelzis adds that significant complexity is added compared to the current situation. In a cleared environment, there will be changes in execution, because some of the FX products will have to be executed on SEFs. "We're currently working with major prime brokers to enable post-trade connectivity associated with SEFs and CCPs," says Mandelzis.

In a significant step towards developing a clearing solution for the OTC FX market, Traiana in March announced that it will provide straight-through-processing (STP) connectivity through the Harmony network to parties wishing to link to central counterparties (CCPs). The solution, called Harmony CCP Connect, will allow for connectivity and matching between executing banks, prime brokers, execution platforms and CCPs for OTC foreign exchange (FX) trades. In March 2011, Chicago Mercantile Exchange (CME) became the first CCP to connect to the Harmony network.

However, Mandelzis says that as the new regulation continues to be defined, it is still too early to say whether this will be a catalyst for the improvement of FX technology, post-trade.

Improving processing operations

But for Richard Kiel, global head of post trade services, sales and trading, at Thomson Reuters, the recent emphasis has been on the implementation of electronic solutions to increase processing timeliness and efficiency whilst reducing risk and enabling a more effective management of headcount versus technology.

"In some markets it is true to say that post-trade efficiencies have significantly improved the front office ability to increase trade volume. Electronic affirmation and confirmation processes have virtually eliminated the rising outstanding confirmation levels in the OTC markets, which regulators were demanding be addressed, and have provided a level of trade certainty not seen before. With the financial world focusing on regulation, risk mitigation is critical," says Kiel.

He adds that these processes are now given far more importance, moving closer to the point of trade execution so that details can be quickly, efficiently and



Gil Mandelzis

"Both CLSAS and Harmony NetLink aggregate trades before they get to the back office and are settled. By providing these solutions, we have changed the way the trade flows work to increase capacity and reduce risk in the industry."

accurately executed to provide trade certainty within seconds. He says: "Post-Trade automation is now seen as a requirement and a key differentiating factor rather than a 'nice to have' by all market participants, from the regulators through to buy-side customers."

Whilst we await the results of the consultation period for the FX exemption proposed by the US Treasury as part of the Dodd-Frank Act, and the pending EMIR legislation, Kiel says the financial markets are looking at how the new rules will be implemented.

Kiel says the fact that FX derivatives will need to be cleared will have a huge impact on cost and resources. He says that firms will need to re-prioritise their development roadmaps and redesign process and procedures to deal with such challenges as the bifurcated workflow between cleared and non-cleared trades; a margining process that is significantly more dynamic than that under bilateral CSAs; the reconciliation of portfolios and payments; new settlement processes and collateral implications; not to mention the individual CCP's Default Management Process which will need to be regularly tested with



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the ability to bid for and accept mandatory allocated trades from the portfolio of a defaulting member.

He says: “These issues will have a huge impact on firms’ back office processes and should not be underestimated in complexity or associated costs. Sell-side firms are also analysing their clients’ clearing requirements as part of the regulation and looking to provide bespoke services to meet their needs – this in itself is a huge project and a relatively new concept for clearing.”

Connectivity challenges

Furthermore the new regulatory requirements will force OTC trading onto electronic platforms and the concepts of a SEF, Multilateral Trading Facility (MTF) and Organised Trading Facility (OTF) are now widely accepted as being the solution. Trades executed on these venues will need to be submitted to clearing and as such a direct link between the two makes sense and provides customers with a compliant end-to-end solution. Kiel says this will prove a challenge for both the venues themselves - who will need to establish relationships, physical connections and provide the infrastructure - and to the trading entities, which will use the services provided. “As a result, customers will need to transfer their execution activity onto an approved venue and make arrangements either directly or through brokers or clearing members to access potentially several CCPs. This will be a costly process. Whilst the cost of execution has always been relevant, this may increase in a regulated environment and clearing costs as a direct or indirect member may prove significant.”

According to Kiel, there are also the technical challenges involved with physical connectivity and the new process and procedural requirements which should not be underestimated in cost or complexity. Thomson Reuters has publicly committed to being SEF compliant in time for regulation deadlines. He says: “We have been at the forefront of change in the FX markets for over 25 years and we have a major SEF-compliance programme in place right now to ensure that our platforms and processes meet regulatory requirements. It is our mission to ensure our clients understand the challenges that lie ahead and to deliver solutions that will simplify the compliance process for them.”

Kiel says that even before the formal regulation, regulators and key market participants were working together to address outstanding confirmation levels and operational efficiency. The Fed 14 banks have been working together now for some time and have made formal commitments to improve efficiencies with the target of T+ 0 trade certainty and confirmation. Whilst previously this process had focused on derivative asset classes such as CDS and IRS, the FX market has now stepped up to the plate. Electronic processing has been adopted widely in this high-volume market, increasing efficiency and reducing risk.

He says: “Upfront trade affirmation, performed immediately after execution and resulting in certainty of settlement and accurate confirmation matching downstream, has enabled traders to increase volume and business. Early risk management processes allow



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Richard Kiel

“Post-Trade automation is now seen as a requirement and a key differentiating factor rather than a ‘nice to have’ by all market participants, from the regulators through to buy-side customers.”

fast and effective trade booking to feed from the execution venue. And sell-side firms acknowledge that operational efficiency is a differentiating factor in attracting business, as well as a way to develop cost-effective and controlled processes. Many now offer electronic STP as standard, providing a ‘one stop shop’ for their customers’ needs.”

Benefits

The reduction of errors, obtaining certainty of settlement and lowering outstanding confirmation statistics benefit all participants to the trade, as well as the financial markets as a whole, by reducing operational overhead and risk.

Kiel is in no doubt that the benefits of new post-trade and back office services are the increased revenue, reduce cost, as well as facilitating regulatory compliance. “Regulation is about risk reduction and electronic process facilitates that concept in a way no other solution can. At Thomson Reuters, we regularly hear from our customers that the adoption of our electronic STP services increases the amount of business they see from their clients immediately,” he says.

He believes that firms benefit from access to a wider customer base and automated STP provides a huge value-add to the service they offer, providing increased ‘stickiness’. He says: “Regulation, whilst dictating many complications to the workflow, will allow those who embrace it to offer their clients compliant end-to-end trading services, from pre-trade and execution through to affirmation, legal confirmation and clearing within seconds of agreeing the trade details. This is a powerful offer in an increasingly demanding regulatory environment that clients must adhere to.”

Added to this, Kiel believes that significant cost savings are possible when electronic trade capture, affirmation, allocation and confirmation activities are deployed, especially when offered with the additional ability to access multiple trading venues via single connections for STP.

Workflow strategies

Peter Kriskinans, managing director of DealHub, says that due to the potential regulatory changes that are under review globally, it is essential that banks have a flexible strategy in place to handle changes to workflows for various FX instruments. DealHub helps banks and financial intermediaries execute on their strategies by providing a highly extensible framework that enables them to rapidly attain their target architecture and workflow.

“The requirement for some FX instruments to be traded on SEFs also impacts the post trade landscape. Banks will need to review their connectivity to SEFs and workflow related to orders, executions, price distribution and credit management. The DealHub Connectivity Manager is well suited for this. Already deployed at 5 leading FX banks for Request for low latency Quote (RFQ) Request for Stream (RFS) and Price Streaming the system has also been integrated to margin, credit, order management, risk management and activity monitoring systems,” he says.

Kriskinans believes the post-trade workflow for FX could change very significantly with regulation potentially requiring clearing of not only NDFs but also FX options, and some swaps and forwards deals. This will require new workflows to deal with multiple CCP interfaces as well as handling how counterparty risk is reflected for deals requiring clearing – before and after novation by a CCP.

He says: “Client clearing workflows are also likely to be impacted as banks clear client trades via various CCPs globally. Until the latest discussion around

an exemption for FX swaps and forwards is resolved this area remains unclear but all FX deal types other than spot deals will need to be sent to Swap Data Repositories (SDRs).”

He adds that this not only includes sending new deals but also sending deal confirmation data and valuation data to the Repository. Furthermore, there may also be a requirement for matching if the Repository opts for a dual submit model. “With a solution embedded above risk systems, DealHub customers are well placed to accommodate changes to these workflows simply by adding new adapters and altering routing and processing rules as required,” he says.

Flexible approach

As much of the requirements around clearing, trading on SEFs and reporting remains undefined, Kriskinans believes it is vital that banks have a system that affords them a flexible approach to their post trade management. He says: “As well as building flexibility with respect to trade routing and workflow, all of the above new workflows must be monitored and exception management systems must be in place to handle issues. DealHub can expose queues of exception events either to the DHView GUI or to other proprietary or third party systems.”

He adds that if the requested exemption for FX swaps and forwards is not granted then the impact to post-trade operations will be very significant and the global nature of FX will add even more complexity to implementation of some of the clearing requirements. New interfaces and monitoring systems need to be put in place to manage submission of trades to CCPs for matching and clearing. Risk systems to be updated as trades become novated. Exception management needs to be in place to deal with any issue arising after the execution has been submitted to the CCP.

“CCPs will perform margin calculations that may require pricing feeds from the bank and a host of reports will need to be processed regarding positions, collateral etc. Banks will also need to consider how this clearing process applies in the case of trades that they are clearing on behalf of clients,” Kriskinans says.



The introduction of SEFs will add further complexity to the post trade operations process for banks as they need to manage the process of interfacing their front office systems, pricing systems and credit systems to the multiple SEFs and managing the price negotiation and credit exception issues as well as the post trade workflow for these new venues.

Kriskinans believes the burden of reporting to SDRs will also fall on both the post trade front/middle office operations as well as on the back office. New trade details must be submitted as soon as technologically practical post-execution and confirmation data must be sent as soon as practical after legal confirmation of the trade. Valuation data or any data related to a change in the status of a live deal must be sent on a daily basis to the SDR.

“The post trade operations for OTC FX will need to evolve significantly or need to harness some of the existing clearing infrastructure at banks,” he adds.

Eligibility criteria

For Kriskinans the main issue with regard to connecting to SEFs and CCPs is the lack of clarity around what will actually be required since it remains an evolving landscape and having a flexible solution that can adapt to the landscape as it changes will give banks a big edge over competitors in terms of time to market with solutions.

He says: “There are likely to be a number of different SEFs and global CCPs and they will each have different message format and protocol requirements so banks will need to manage the process of handling multiple connectivity options, unifying different data formats and integrating new flows to their in-house systems. Banks will need to define the eligibility criteria for trades flowing to different CCPs.”

Some SEFs will offer the ability to manage credit limits within platforms so banks will need to integrate their internal credit systems with the new platforms and consider how they manage the global credit line for a customer trading over multiple new venues. Pricing feeds as well as feeds to submit orders and receive executions will need to be built for SEFs also. Alternatively this could be done within a third party platform such as DealHub which pools credit across all integrated venues and can supply adapters to SEFs, CCPs and SDRs.

However, Kriskinans adds: “Where a bank is clearing trades on behalf of a client then there are issues around registration or matching of trades and of ensuring the various status of trades are transparent to the client as the trade moves through the clearing process. The



Peter Kriskinans

“The post trade operations for OTC FX will need to evolve significantly or need to harness some of the existing clearing infrastructure at banks.”

bank not only needs to manage the interface between its in-house systems and the CCPs but also needs to ensure that margin management and reporting from the CCP back to the client is handled.”

For this reason, Kriskinans believes with the advent of new SEFs, CCPs and Trade Repositories, it is imperative that a flexible interface connectivity platform is implemented to unify various data formats that must be understood and transformed so that a bank can see a single homogeneous view of its interactions with multiple execution, clearing and reporting venues.

“As existing multi-bank trading platforms become registered SEFs, new SEFs are formed and various exchanges offer CCP services for FX products traditionally trade OTC, FX trading firms will need to cope with a host of interface changes, a variety of formats and protocols and a number of integration projects,” he says.

Post-trade technology can make this transition to the new post trade landscape less painful to the existing operations of banks by providing an interface and smart routing layer that makes the physical interface transparent to the banks internal systems, provides data in a single unified format and makes the data available in real-time to monitoring and intervention systems so that the flow can be managed efficiently in real-time.

Regulatory certainty

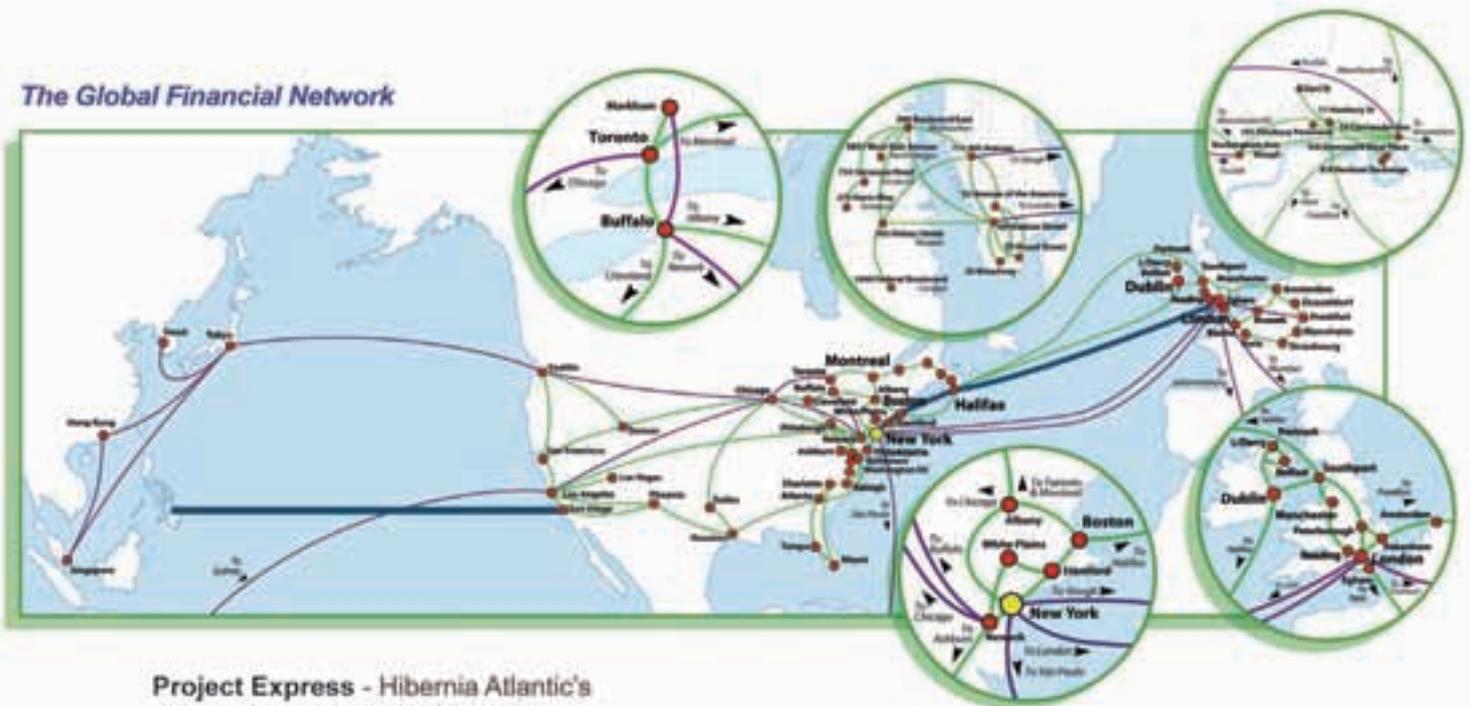
Jim Denny, senior vice president of SunGard’s end-to-end FX trading solution, Sierra, believes that the increased automation that is coming as a result of the regulatory requirements will transform the FX back office. However, he says the current challenge is trying to work out exactly what changes are taking place but regulatory certainty is now starting to come.

In the US, the National Futures Association has implemented some rules and regulation and what Denny says is that the need for more data is underpinning much of the new regulation. He says: “It is similar to the Fixed Income world where TRAX reporting has been built in recognition of the need for more detailed, and timelier, data on transactions with a break down of the executed orders, appropriateness of the counterparty, and the spreads. There is a big push towards finding out more about the client and their transactions, while still looking at the credit exposure and risk.”

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While this will not affect FX spot deals, it will have an impact on FX options and organising the reporting of this data is no small task. Dennelly says: “It will be interesting to see what the regulators require and how to get that data.” The FX cash market has become very electronic and much of the data is already reported, although liquidity providers are now being asked to provide additional information with their post-trade tickets to comply with regulations, but a large proportion of FX options are done over the telephone. “What kind of data collection will be required for telephone deals and how the back offices handle this reporting will be an interesting challenge.”

While SunGard is well placed in enabling banks to process exchange-traded derivatives, Dennelly says these are defined contracts; in the FX world, the purpose of the transaction from the corporate client’s perspective is to hedge and the transactions tend to be very specific and highly customised.

He adds: “Many are staying in the FX cash market because they have distinct hedging requirements and can use instruments such as window options where they can have a period to exercise forwards, and while the industry is headed towards a clearing solution for FX, there will also be a move towards client collateralised margining for FX.” Instead of going down the exchange/CCP route and similar to the OTC world for interest rate swaps, clients will be required to post collateral on positions, similar to the retail and corporate business. “Traditionally this was tied to retail FX trading but more and more firms are asking about it, because since the credit crisis they are looking at risk differently. They are starting to look at transactions with volatility-type methodologies and using VAR (Value at Risk) calculations for the first time in FX.”

Boosting STP rates

Dennelly says the regulatory focus on FX and the re-engineering of processes will significantly boost STP rates and help develop more effective e-confirmation services in FX because firms are going to have to collect data and publish data in very effective timeframes, which will result in building automated processes which will make the clearing of FX faster and more efficient. While there will be initial costs involved, it will reduce the average cost per transaction and create a more efficient back office process. “Clearing houses will no longer be a ‘nice to have’; they will be a ‘need to have’,” he adds.

A few years ago, banks’ FX back offices came under fire from the regulators due to the backlog of the



Jim Dennelly

“What kind of data collection will be required for telephone deals and how the back offices handle this reporting will be an interesting challenge.”

processing deals caused by the spiralling volumes of smaller ticket sizes. According to Dennelly this is not something that has completely gone away and for some of SunGard’s larger clients is still a concern. However, the bottlenecks caused by the huge amount of tickets generated by some of the prop desks can be resolved through greater automation.

A year ago, unrelated to the incoming regulation, SunGard began a rewrite of its back office FX functionality, which will be released in the first quarter of 2012. Dennelly says the decision was driven by the need for greater efficiency and the growing requirement to handle larger volumes by processing, but now ties in well with the need for connectivity to CCPs and SEFs, as well as trade reporting repositories.

He says: “The biggest benefit coming out of these changes is more efficient processing, allowing firms to deal with more high volume clients. Some of these firms are actually stepping away from the prop traders because they don’t feel they can effectively handle the risk. Until now, the front office technology in FX has been moving at a much faster pace than the back office. This has been driven by a lot of the liquidity

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platforms and the growth of algorithmic trading, leaving the back office in FX a few steps behind.”

Sierra already has a very strong margining algorithm but Denny says that SunGard has incorporated a lot more into the back office functionality. Apart from the clearing requirement for FX options and NDFs and the greater focus on data and reporting, Denny believes there is going to be a new emphasis on collateralised trading in FX and need to manage this risk.

“There is going to be a group of clients and business, which does not go to CLS or through central clearing agencies and this needs to be handled differently, as well as linking the reporting and collateral for those that do. We can get an idea from what the futures exchanges are doing, but much has still got to be hammered out,” he says.

If there is a greater convergence in how the different asset classes operate, Denny says that firms are

increasingly likely to take a fresh look at cross-asset trading and processing solutions. SunGard is looking at this, especially from a data Repository perspective and also for margining, by integrating Sierra with SunGard’s StreamCore and Stream Credit Monitor products to offer a best of breed product for centralised collateral and risk management.

Conclusion

The FX back office was already going through a transformation brought on by higher levels of electronic trading, the introduction of aggregation and the need for greater automation just to keep up with growing volumes of business. The addition of clearing and trade reporting for FX trades could well prompt the need for a complete re-engineering of some back offices based upon legacy systems that need upgrading anyway. The problem is the timeframe. The G20 have stipulated that this needs to be in place by the end of 2012 and yet still the FX industry is waiting for further clarification on regulations before it can really get started.

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Generation Y - spawning the new generation of Social Forex sales?

Without doubt the markets never stand still and as FX market participants, we are no different in having to keep pace with ideas, technology and the like. What is striking is that the question being asked is what might the next generation of FX salesperson begin to look like and what skills do they need to succeed? The biggest single driver affecting this is Social Media-come-Social-Forex.

The '20 somethings' have now been living in the Social Media and gaming world for their whole lives and see nothing strange in opening up conversations and relationships via online channels. They may never meet in the majority of cases, but that has never stopped them thinking people they meet

online could become their closest friends, in fact a very recent study from an unlikely source, the Cystic Fibrosis Trust, found users of Social Media sites have 121 online friends compared with 55 physical friends. Now one might say that this is a distinct group that finds a person with the same challenges in life, in this case an illness, but then in business life do we act much differently? For example in FX, we are wanting and needing to do business and keep our professional options open, so nothing much different here.

Multitude of online channels

Stefan Basiuk Co-Founder at LetstalkFX says that with the multitude of channels available from networks like LetstalkFX, LinkedIn etc, as well as various Instant Messaging (IM) execution platforms and Twitter etc, it's becoming harder to keep up with the pace



Stefan Basuik

Dealing with a multitude of online channels

of change never mind climb to the top. So if dealing with this complex environment as an experienced salesperson means you are having to learn as you go, whilst the young buck coming up – let's call him a Generation Y individual - alongside you on the desk has been working with it since he could spell, and sees it as the norm, it's a frightening position to find yourself in.

Picture the scene, he's watching the phones, talking to his favoured clients via IM, dispensing his views via his LetstalkFX groups, updating his professional status on LinkedIn, posting his Tweets on what he is seeing in the market, and he or she does this effortlessly! I used to watch my son gaming while he was on all manner of venues talking and watching TV at the same time, so believe me, this person exists and is going to become very much in demand from the institutions.

However, as Generation Y business people continue to enter the workforce some time will pass before you see this scenario in every dealing room. Elena Theodorou at Social-markets.net believes the reason for this is because Social Media is still a relatively new space. Senior management and traditional salespeople are still

a little unclear around the benefits of Social Media, how they can effectively leverage these channels and what their strategy should be. There will be increasing demand for the next generation of FX sales person once banks realise that by utilising these new social channels sales people will be able to get a much closer relationship with clients, that's more authentic and on a more personal level. They will then be able to tailor their sales offering to really meet the needs of their clients and be able to generate more business. Audiences now demand dialogue and if a bank's strategy is to overlook Social Media then they run the risk of missing the boat.

Tapping into expectations

Maria Aldous, Head of Electronic Markets at Elements Executive Search says that with areas of deregulation expanding choice and instant gratification becoming the norm, not only do businesses need to tap into clients expectations, they need to employ and nurture talent that is able to evolve with market and client demands. Electronic pricing has changed the

Social Media is still a relatively new space



Elena Theodorou



face of the FX sales person over the past 10 years, with many sales desks creating 'hybrids of traditional and 'e'sales people. However the talent pool has not grown as quickly as demand. The sales person of the future needs to evolve along with the methods used to reach their audience. Marketing and sales may then form a closer bond to promote that information and brand to a wider audience using the social media methods such as Twitter, Facebook, LinkedIn, Instant Messaging and more. Some banks already employ social media consultants to assist with this branding effort.

Relationships will continue to dominate, however, information is power and the choices we have for how, what and where we access this intelligence, data, pricing or products may help differentiate at the end of the day.



Maria Aldous

Sales person of the future needs to evolve

As Social Forex continues to gain momentum over the coming months and years so will the need for this new style of salesperson maintains Elena Theodorou. "In the short and medium term, we will see the next generation FX salesperson embrace these channels and even help the older more traditional salespeople get to grips with this new style of doing business with clients. We may initially see a 'culture clash' just as we did when electronic trading first entered the dealing room but instead of it being about the benefits of trading online it will be around how effective Social Forex is and resistance to its value proposition. The young bucks will be clear on the benefits as using these channels to engage their clients is second nature to them," she says.

As the years pass and these new 20-something graduates climb through the ranks, become trusted advisers to their managers and go on to become managers, they will be finally be in the position to potentially reinvent their companies' processes completely. It is at this point that we will likely see that Social Forex has been completely ingrained into the business and they will be faced with new dilemmas around how to drive the business forward, engage their clients and increase sales, believes Theodorou. It has been predicted that by 2020 the mobile device will be the Internet user's primary way of accessing the Internet (Economist Report, 2009) and if all of our corporate information is there, it stands to reason that becoming more social-network savvy is the way forward. Yet while we will all have to adapt to a world where multitasking, filtering, and doing business from a smart phone or tablet is the norm, the fundamental sales skill set of the FX professional will stay the same.

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Nedbank Capital is the investment banking arm of Nedbank Group, one of the four largest banking groups in South Africa. The full spectrum investment banking offering provided by the firm stretches from debt advisory and long-term project financing to equity trading and research to South African and international clients. The business, which celebrated its centenary, in London in 2006, provides extensive knowledge of and experience in, doing business in South Africa and the rest of Africa. The Nedbank London office ensures that this local knowledge is supplemented with up-to-date international and capital market expertise.

As a leader in the investment banking arena, Nedbank Capital consists of a number of divisions that together manage the structuring, lending, underwriting and trading businesses. The business seeks to provide seamless business sectors.

With this client service and growth strategy in mind Nedbank recently expanded their growing e-commerce presence utilizing 360T's multibank

TEX platform. Combined with 360T's multibank platform for sourcing liquidity, the bank can now offer its clients a fully functional cross-product cross-region platform.

"Originally the decision to start e-trading on 360T was driven by a desire to constantly look to improve our service offering to clients, as well as sourcing better pricing, liquidity and transparency. The functionality incorporating multi-product and multi-bank environments was also unique to 360T and as such gave our business room to expand into other areas of e-trading," said Colin Clarkson, head of Corporate Treasury Sales at Nedbank Capital.

After a rigorous selection process, Nedbank Capital selected 360T as their service provider due to the following reasons:

- Good pricing and liquidity
- Client demand
- Multi product/Multi bank
- Stability of platform
- Independent ownership
- STP expertise
- Simplicity of set up and cost structure
- Global operation and 24 hour support
- High level of customer support and service

Stable and liquid platform

"When we selected 360T we were looking for a stable and highly liquid platform across multiple products (Forex Spot, Forward, Swap, orders and money market deposits) which would be easy to deploy and efficient in terms of Straight Through Processing (STP) and reducing traders time spent processing tickets. This project went extremely well. We have a good basket of liquidity providers and seamless straight through processing for all our traded tickets. 360T offers a streaming service and Request for Stream (RFS) which means we have the choice of environments for trading and placing orders as well as the benefit of passing this liquidity and method of trading on to our clients", says Clarkson.

"With our market making we are constantly looking to improve our electronic service offering to clients and to deliver a client-centric approach. We knew 360T had good client penetration in the markets we were active in and was a platform we could use to utilize our reach to existing and new clients. This meant we could offer our clients multiple products across timezones and in many cases automatically priced. The flexibility was key to us, as was the effortless ability, technology-wise, to roll this out to clients and offices globally. 360T is an active part of our e-trading capabilities at Nedbank Capital's offices and as such allows us to enhance our strategic presence as well as offer our clients the efficiencies that come from e-trading. STP is key for us and means increased efficiency and reduced operational risk for our clients and the bank".

The Future

The future will see Nedbank Capital continue to take clients' feedback on products offered and their resulting efficiencies. "At Nedbank Capital, we are committed to ensuring our customers feel the difference when they interact with us. This relentless focus on our customer is underpinned by our commitment to deliver a differentiated experience through the development of a series of service and channel enhancements".



Financial Network Communities - offering FX Trading firms access to execution venues and service providers



Roger Aitken

Roger Aitken explores the continued drive by FX trading houses to secure low latency trading solutions and discovers how financial network community ecosystems, built around co-location, proximity hosting and managed service offerings, play a pivotal role in allowing trading participants to remain efficient, secure and generate profitable returns, amid rapidly burgeoning daily FX trading volumes.

At a time when global equities trading volumes in North America have dipped, it is not surprising that interest in the trading opportunities of the FX market have become an enticing proposition as firms seek diversification in their strategies and alternative ways to generate profits and potential alpha. Evidencing this trend, a recent report from Boston-based Aite Group indicated that high frequency traders (HFT) accounted for some 28% of the total volume in the futures market, which includes currencies and commodities. This was up from 22% in 2009.



New generation of communities

Against this backdrop, a new generation of financial network communities are being developed that provide FX trading firms with hubs for improved access to various execution venues, FX liquidity sources and FX market data and service providers. Furthermore these financial ecosystems are continually expanding in response to seemingly unabated customer demand.

This demand is coming from a range of firms all looking to establish and interconnect themselves within these Financial Services ecosystems, notes Robin Manicom, Director, Financial Services, Europe at Equinix, leading operator of International Business Exchange™ (IBX®) data centers in 37 markets across 12 countries in the Americas, EMEA, and Asia-Pacific. “As the growth of automated Foreign Exchange (FX) trading continues to advance globally, we are seeing increased demand for data centre solutions from trading participants. When segmenting our 650+ strong Financial Services customers, across the top 16 global financial markets in which Equinix currently operate we can see that the world’s most important FX trading venues, financial institutions, service providers and major networks are coming into our data centres to interconnect with FX retail and institutional traders and the multiple FX trading venues and ECNs located across the globe,” he says.



Robin Manicom

Equinix lists a whole number of FX venues within its global data centres, including ICAP EBS (i-Cross), Currenex, Hotspot, FXall, GAIN Capital and others. According to Manicom, a large proportion of participants in Equinix's financial services ecosystems are from the buy-side. "Additionally we have a mix of customers including buy side and sell side firms as well as financial technology service providers such as market data and financial networks. These customers typically have located servers and infrastructure within data centres to support mission-critical, financial services applications with low-latency connectivity," he says.

Connectivity

One way to achieve low latency connectivity is through co-location or proximity hosting at specific data centres. Such a move reduces the physical

"It's just the beginning. People recognise that placing and centralising your IT systems into a data centre provides business opportunities to sell more, cut costs and increase security and availability."

distance to a particular FX exchange or market venue to virtually zero by placing trading engines/algorithmic servers (hardware) at or near the matching engines of a particular execution venue.

In essence there are three types of scenarios on offer from financial data centres to market participants depending on their strategies and latency tolerance. The first situation is where the infrastructure of an FX venue (i.e. primary matching engine) fully resides within a data centre.



Varghese Thomas

“You can reduce latency by consolidating servers, refining the high-tech hardware and improving the application.”

The second is where an execution venue maintains its own data center or uses a third-party provider, and a specialist provider has a centre physically close to it in the same building or perhaps around the block. The third situation is a twist on the second, but where another vendor also has some space in the same physical building.

According to Varghese Thomas, Global Head of Financial Services at Savvis, an outsourcing provider of managed computing and network infrastructure for IT applications, a new generation of financial ecosystems are being developed that provide trading firms with hubs for improved access to trading venues and facilities across multiple asset classes, including FX. “Certain ecosystem providers offer access to multi-asset class strategies. It’s important to provide services to a wide group of clients such that they can then access these by either being co-located next to them [i.e. the matching engines], potentially via a Software-as-a-Service (SaaS) offering, a managed service within the facility, or through direct network connectivity.”

Offering low latency connectivity on a global basis, Savvis currently has 32 data centres globally and are in

all the main financial cities across the globe. “We take a look at the best fibre routes in each region and put in the low latency connectivity,” says Thomas. “We do it on behalf of customers or customers can choose to do it on their own. So, it’s a very flexible approach.” Savvis presently has c.48% of global spot FX matched in its datacenters (including Currenex matching engine and trading platform in a Savvis datacentre in New Jersey), plus CME Group, FXall in its NJ2 facility in New Jersey as well as low latency access points to ICAP and Hotspot (source: Exchanges). Reuters Dealing access point was scheduled for the first half 2011.

Meeting the latency challenge

Clearly the challenge when chasing the latency game is that it can prove very expensive simply because having various locations from an infrastructure perspective means one needs to be in all the relevant locations and be in a central location, says Thomas. “You can reduce latency by consolidating servers, refining the high-tech hardware and improving the application. Clearly you need to look at it right across the board and really fine tune each of those components that make the end-to-end flow of the trade cycle.”

One of these critical components is the network connection. As John Owens, Vice-President, Exchanges & ECN’s, at Transaction Network Services (TNS), a financial extranet provider, says: “Once market participants have decided they’re going to trade FX and avail themselves of an FX ECN, the last thing





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they really want to do is destroy all of their investment and efforts by using an internet connection, which is going to give you slow access to a particular high-speed trading platform.”

Market participants therefore need to ensure they have an extremely reliable and fast network connection, says Owens. “And, then they want to make sure they have speedy access to venues when they decide that they want to go there.” TNS manages the whole service on behalf of trading firms who opt for their offering. By doing so firms do not have to invest in staff and IT resources to facilitate matters. “This is because it’s not the process that will be making them money”, says Owens. “Rather, it’s their trading strategies and available capital that will potentially yield returns and where they need to focus. That said, clients want to have the IT services to enable them to fulfil their ambitions with regards to their investments.”



John Owens

“Once market participants have decided they’re going to trade FX and avail themselves of an FX ECN, the last thing they really want to do is destroy all of their investment and efforts by using an internet connection.”

Accessing a community

TNS offers its TNS Classic, a standard extranet service where users are connected to the nearest POP and then routes across the firm’s extranet. Owens points out that this probably “satisfies 97%” of the community. TNS Extreme, their lowest latency service, is offered to those firms looking for a proximity service. It provides a direct fibre connection between where a particular firm is located and the venue(s) they want to access. “TNS Extreme could also be applicable to High Frequency Trading (HFT) and algo trading firms, if they wanted to locate their black boxes at a remote site or at their own data centre, and they don’t want to co-locate with the execution venue,” says Owens.

According to Owens, it is all about providing FX market participants with access to a community as it is rare that these players are trading with just a single counterparty. “In some cases these participants may be aggregating those and routing them on to a platform for execution. In other cases they’ll be trading directly with counterparts themselves. So, granting access to a community is an extremely important part of the whole scenario.”

“A financial community network such as TNS is a very large established community and provides participants rapid, secure and robust access to more than 1,700 end points today. And, there’s a fairly good chance that anyone who wants to trade with someone who is involved in the FX trading space will already be on our network,” he says.

It’s also important to recognise that not everyone in the FX trading game needs ultra-low latency solutions, although a significant number of key players desire this. With that in mind there are premiums attached in opting for proximity hosting and co-location services, which are sought out by the small fraction of high frequency and algorithmic traders. “Not everybody wants to absorb those premiums because certain strategies pursued by some firms may not be predicated on the lowest level of latency,” Owens points out.

A provider like TNS is in a strong position through its financial extranet to provide more than satisfactory access to multiple execution venues, multiple trading counterparties and multiple service providers as they already have those connections built. Clients benefit in terms of cost savings and efficiencies by leveraging the TNS infrastructure to get to the venues they wish

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The BT Radianz Shared Market Infrastructure brings together a community of 14,000+ customer locations globally. Through a single connection, the BT Radianz platform enables customers to access hundreds of applications and services covering all asset classes across the entire trade cycle.

to trade. Customers are then charged a share of TNS' overall costs to get access to their desired trading venues and counterparties.

As well as constantly working to ensure that the latency between TNS POPs on its network are minimised and brought down to the lowest levels, it also provides stable and reliable connectivity with SLAs, multi-pathed routes and full management and monitoring of the network with helpdesk support in Europe, North America and Asia. This is not just from the installation side, but also once the connection has been established. "It's no good having the fastest route in the world if it turns out to be the most unreliable route," Owens contends.

Adding value to ecosystems

According to Yousaf Hafeez, Capital Markets Development Director, Global Banking & Financial Markets, BT, one of the important aspects to bear in mind about the FX market is that it is expanding globally. Therefore it's important to provide customers with access to applications in as many markets as possible. "We are giving customers the ability to access these applications and currently we're in 64 countries. The second thing we are undertaking is offering market participants the ability to co-locate their FX algorithms and programs geographically around the world in order that they can access a multitude of FX venues with the lowest possible latency," he says.

Looking at ways low latency communication and specialist network providers are bringing value to Financial Network Communities to enable these communities to extend globally the 'zero-hop' connections amongst their members, Hafeez argues it is about scrutinising the entire chain. "Where our strength really lies is in looking at and evaluating the whole community and the entire FX chain. We don't look at just one part of the chain. So, it's not just about putting a big piece of fibre in the ground that provides super low latency."

BT's stance is to look at the front office as well as the back office. "In terms of the front office I'm talking about the ability to access venues with low latency, having low latency messaging platforms within your cloud and the ability to have complex event processing (CEP) software," says Hafeez. BT also looks at the back office, which involves for example, on-line notification and confirmation services, trade aggregation and real-time margining, all of which is designed to provide a holistic FX trading solution for customers.



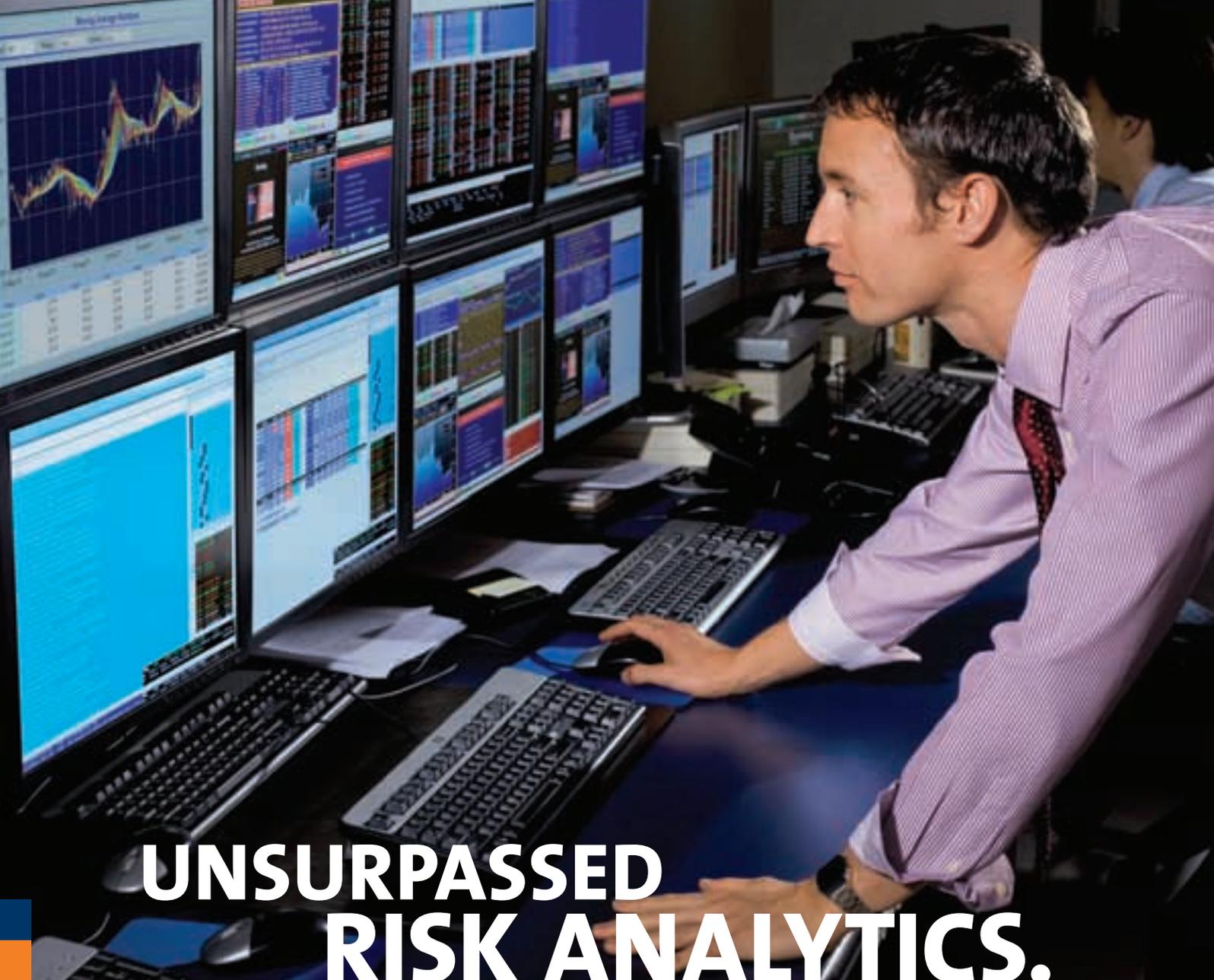
Yousaf Hafeez

"It's important to offer market participants the ability to co-locate their FX algorithms and programs geographically around the world so that they can access a multitude of FX venues with the lowest possible latency."

"We can work with customers to give them very low latency connectivity," Hafeez adds. "But what we do on top of that is provide very deterministic low latency, by which one can be pretty sure that the low latency you get today will be the same as tomorrow. Whereas with some other services that latency can fluctuate."

Manicom and his team at Equinix look to add value by spending significant time meeting and talking to other participants within their ecosystem. "That might be in the shape of the low latency network providers, trading matching engine technology providers, high-speed market data/low latency providers and managed service providers who come in and take large areas of space and offer it to their customers and bring more customers into trading," he says.

"Essentially it boils down to the ability to utilise the same infrastructure therefore from multiple services. And, one of the things market participants can do, if they have a single infrastructure and that infrastructure allows you to access a wide range of FX services, is cut back on their costs immediately, rather than having dedicated infrastructure for every single FX service



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they require,” Hafeez points out. The consolidation of infrastructure is therefore important in order yield large cost savings.

Ultra low latency

With respect to addressing the issue of ultra low latency for critical FX trading and brokerage activities, BT’s Hafeez says: “From our perspective we are engaged in two things. The first one is the ultra low latency network that we have, which is available in a number of key financial centres around the world, which provides customers with the ability to access FX venues in key cities with sub 1 millisecond roundtrip delay (RTD).”

He adds: “The second thing is to provide customers with the ability to proximity host their algorithms in their cities so that they can access those venues with low latency. For example, if you wish to trade on FXall and you’re sitting in London, you’re probably looking at 70 odd milliseconds roundtrip there and back. Whereas, by placing your algorithmic set-up in our data center in New York then we’re probably looking at sub 1 millisecond latency.” BT is also continually assessing their customers’ “roadmaps” in the FX sphere. (FXall’s matching engine is located in a Savvis data center in New Jersey).

In terms of low latency offerings, BT Radianz Fusion allows the provider to put an infrastructure on a customer site and through that infrastructure they can access these particular services through BT Ultra and other services via a standard BT Radianz connection. “This allows customers to segregate the applications they want to access. Or, in the case of a sell-side firm, they can say ‘OK, we can segment our customers dependent on their strategies and how important they are to us,’” says Hafeez.

Differing trading requirements

On examining how algo and high frequency FX trading firms can leverage the services and facilities provided by Financial Network Communities to improve the performance of their trading applications and develop innovative new strategies through improved access to trading venues, it all rather depends on the individual firm in question and how fast they wish to be. For some players it’s critical to get their orders to the top of the queue.

However, this is not the case for all trading firms. “It’s important to remember that not everyone is a high frequency or algorithmic trader,” says BT’s Hafeez. “And, while we do certainly cater for that constituency, we also have another set of customers who have totally different strategies. So, it’s really about the ability to cater for all strategies and giving customers the option where we say ‘Right, we’ll give you the infrastructure and services to allow you to execute that strategy,’” says BT’s Hafeez. It may be the case that a firm will have a high-frequency strategy today yet in six months time that may change and go in a different way. And, the reason why this may change is that the returns the strategy is achieving from high-frequency trading may not be as great as it is by having for example a long-only strategy.”

It’s all about flexibility, says Savvis’ Thomas. “Centres are looking at two factors, depending on the trading strategy. Obviously it’s about the ability to reduce costs because it can be very cost prohibitive. And, really only perhaps 5% or less of the high frequency



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traders are looking at shaving nanoseconds or sub-microseconds off their trading life cycle. The rest are within the microsecond or millisecond range, depending on where they are located and where they are accessing the service from. However, it's really become microseconds where some players need to be."

Thomas adds: "What I think is fundamentally important for financial communities is being able to offer them the full range of services from middleware, feed handlers, databases and other providers that are within these ecosystems, as a cost-effective model. Taking managed hosting services enables significant reduction in end user costs, without the need to invest capital for IT infrastructure and facilities."

"This becomes more accepted in the high frequency trading (HFT) market and where CEOs and CTOs are looking to reduce cost," notes Thomas. "No one is building data centres - except for some of the larger firms, but even then they are potentially not even undertaking that themselves. What they're looking for is finding the right provider that can offer them the right mix of latency infrastructure as well as applications within the community itself whilst cutting costs associated with the business."

Security is also a key consideration for FX traders looking to use a data centre, says Thomas. "Risk management aspects are clearly huge. We provide risk management applications through partners. But also we have the ability to undertake power processing for managing real-time risk where access is required to perform numerous calculations. Savvis' platforms enable users to have 'grid-type' environments to undertake real-time risk management and positioning, achieving scale and enabling access to compute and storage," he points out.

Multiple asset strategies

The leading colocation solutions are delivering fast, reliable and secure applications for FX and helping firms to minimise risk, control costs and capture new investment opportunities, not least by enabling them to pursue multiple asset strategies within a single data centre. For example, the Equinix London 4 and London 5 (LD4 and LD5) IBX data centre campus environment (just west of London), offers trading firms access to

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services suitable for multiple asset classes. Being located in Slough, all under one roof, Equinix provides access to 110+ financial services customers and 8+ trading venues, either via co-location next to a matching engine or via proximity by an access node, comments Manicom.

For firms wanting to execute multi-asset class trading, Equinix's financial services ecosystems presents an enticing proposition for trading participants as well as vendors and other service providers who wish to interconnect. And, with major network links running from the city through Slough, before they make the transatlantic crossing to the US, LD4 and LD5 are becoming an attractive data centre campus environment for currency trading. Manicom contends that the place is quickly becoming one of the "centres for FX trading in Europe" as the requirement for ultra-low latency, a key driver in the equities market where high frequency traders use time advantages to drive higher trading profits, is now becoming a FX market prerequisite too.

"Not only have we got a significant amount of the key FX trading venues within our data centres, which is encouraging the development of a robust and mature FX community," says Manicom. "But due to the very nature of multi-asset trading requirements these days, you're increasingly witnessing from an FX perspective how currencies are key to arbitraging between different markets."

Equinix does not provide applications directly itself as such. Its primary focus is on building and running data centres and interconnecting today's modern financial services participants into ecosystems that act as virtual marketplaces. However, it is able to respond to customers' demands for other services (e.g. UTP satellite time stamping of orders, Business Continuity Trading Rooms and other Back up solutions). It facilitates this by reaching out to a clutch of specialist technology providers and maintaining a vertical business structure that provides access to a team of leading subject matter experts. Manicom refers to this as "triple win" for customers, vendors and Equinix.

Future growth and demand

As interest in FX as an asset class continues to grow



in markets around the world, increasing numbers of alpha seeking trading firms will be looking to leverage financial ecosystems to help them achieve competitive advantages. The impact of global regulatory change will also act as a driver here. A reduction in counterparty risk associated with centrally cleared, Exchange-based trading, makes investing in currency products on these venues an even more attractive proposition.

Increasing numbers of exchanges are therefore positioning themselves to provide products and services aimed at high performance currency trading firms who will as a result require improved access gateways. All these developments will stimulate increased demand for data centres and dedicated network connectivity solutions and many leading ecosystem providers have already begun expanding their global footprint to fill the gaps.

Equinix's Manicom says: "It's just the beginning. People recognise that placing and centralising your IT systems into a data centre provides business opportunities to sell more, cut costs and increase security and availability." Equinix has recently entered into the South American market with ALOG Data Centers of Brazil S.A., a Platform Equinix Company, opening its third IBX data center in Brazil and Manicom says there are plans to establish additional data centres in other new emerging global financial markets where customer demand is high.

Meanwhile BT has recently increased access to the Russian markets (RTS and MiCEX) for high speed access between London and Moscow. So, as this year goes by we should expect to read more and more news from other leading providers about their global expansion activities in this fast growing business.

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Fine tuning e-FX performance

e-Forex talks with Kevin Ashby,
CEO of Velsys, a leading e-FX
solution developer

Kevin, how did Velsys get into the FX business?

Velocity Systems was formed in 1999 in Australia. The company has always been focused on the FX business and at the outset the company developed complex pricing and risk management solutions for major banks. As e-commerce started to take off, Velocity was asked to develop solutions to connect banks to liquidity providers, internal systems and more recently the ECN and API community. In 2008 the company embarked on the development of end-to-end trading systems. In 2010 the company's trading systems development caught the interest of the investment community and two major funds invested in the company and as part of this process the company moved its headquarters to the UK and was renamed Velsys.

What core financial software and connectivity solutions does the company offer to FX trading firms?

Velsys offers both a range of components and complete trading systems. These are grouped into connectivity solutions – ViSTRA, and trading systems – V-FX.

Why did Velsys decide to invest significant resources in developing your cloud-based FX workstation, V-FX and what range of trading models does this solution support?

Velsys recognises the power of service-based models and has for some time offered its solutions on this basis. So the company was extremely well positioned to embrace



Kevin Ashby

cloud computing when this model became the preferred method for rapid deployment and support of trading solutions. Velsys understood the operational model before “cloud” became fashionable.

The commercial model embedded in service-based propositions works very well in the FX market. It allows systems to be deployed rapidly with a manageable level of integration to existing systems, and with a low initial investment. The providers income is primarily tied to use and is therefore fully aligned to the growth of a client’s business.

However, the primary reason for making the investment was a recognition that most of the solutions in the market have been around for some time and were not designed either for rapid deployment or to cater with the demands of today’s market. For example many were designed before ECN’s, API and retail margin trading became important distribution channels.

In terms of trading models, Velsys provides the complete supply chain from aggregation of pricing and liquidity through to distribution of liquidity to multiple destinations, via trading screens (GUI’s) for internal users and external clients, API’s and broad ECN connectivity. Our solutions support multiple business models. For example, in the area of pricing and liquidity management, we can support agency trading (back-to-back) market-making and position management models, plus combinations thereof including flexible trading rules to allow our clients to tightly manage their client and trading profitability, positions and exposure.

In this edition of e-Forex we have reported on the advantages of the FX White Label business model in delivering e-FX products and services. What are the main benefits that institutions get from taking a White Label version of V-FX?

The priority with White Label is to offer a great service to all of your customers, irrespective of the mechanism the end client uses to trade (screen, portal, API or ECN) who they prefer to trade with, or the style of trading they prefer (Cash, Margin or High Frequency) And all provided 24x6 with automated hedging, client position management plus where appropriate warehousing of positions to maximise value.

There are a wide range of options available to a bank seeking to deliver an e-commerce solution to their clients via a white label model. What we see as a common theme, with V-FX clients, is speed to market, but the real driver is control over their supply



chain. From how they source and derive pricing and liquidity, to instant views on profitability and positions, automated risk management but most important distribution to end clients, via multiple channels and for many the ability of one system to offer both cash trading and an integrated Margin FX offering.

What key features and functionality are provided with your ViSTRA connectivity solution for FX and what types of trading venue can also be connected with it?

ViSTRA comes in three flavours, up-stream, downstream and STP; ViSTRA is also an integral part of V-FX. As the names imply, up-stream is the provision of adapters to allow organisations to seamlessly connect to external sources of liquidity/marketplaces and pricing whereas downstream is connectivity to ECN’s, GUI’s, Portals and API’s in general. STP covers a range of adapters that provide connectivity to a wide range of recognised third party middle, back office and messaging solutions, plus a framework for connecting to proprietary systems.

While it is easy to see “connectivity” as a commodity service, within the FX market, products like ViSTRA have to be “intelligently aware”. For example, connecting to an ECN can be straight forward,

however, understanding and managing the various workflows, account mapping rules and message handling mechanisms deployed by each of the ECN's requires significant industry knowledge if the adapter is going to perform effectively. We are also planning to add further intelligence at the adapter layer. Velsys believe by putting intelligence e.g. smart order routing, closer to the connectivity layer we can reduce the complexity of pricing engines and simplify the trading environment. It is also possible, at the adapter level, to aggregate flow and undertake intelligent analysis and better manage and predict patterns, more effectively and with greater flexibility if this task can only be accomplished large and complex pricing engines.

What solutions has Velsys recently developed to cater for the fast growing high performance, high speed end of the FX market?

In order to answer this question, let's first define how Velsys sees this market. We divide the market for high speed trading into two segments.

The first being the ultra high frequency market where participants want the fastest access they can achieve, and directly to primary liquidity partners. In this segment, any technology that sits between the pricing engine and the client's execution algorithm adds latency. In other markets co-location of algorithmic systems and the source of liquidity (i.e. exchanges) has become a market norm and this is also happening in the FX market. However, the application of

algorithmic trading is different due to FX offering multiple trading venues for a product that is extremely fungible – v's the non-fungible nature of, for example, the futures markets or the more rigid and regulated structures of the equities markets, including alternative venues such as the dark pools. Velsys primary involvement in this sector is low latency connectivity solutions.

The second market is lower intensity API market, which is more relationship based, and the ECN marketplace. While a user of an ECN may well be using either a screen or an API, from the bank's perspective they are connected via an API.

A common factor in API markets where banks are competing with multiple other providers, is that price distribution must be as fast or faster than your competitors. If a bank's prices are arriving too slowly, and the bank is getting the order, it's because the market has moved against their price. So, to avoid getting

“caught” banks widen their prices and inevitably see less business.

We were recently working with a bank that, in a few years, slipped from the top 10 list of providers to a particular ECN to somewhere south of the 70th provider, purely due to having to widen prices to

overcome high latency from an earlier generation vendors solution.

This market is a significant opportunity for Velsys. Any bank relying on systems from the previous generation of solutions will need to upgrade to compete in the ECN marketplace, or any other marketplace, which provides price discovery from multiple entities. This market is growing, helped by legislation and the penetration of the ECN's into the traditional client bases of the regional banks. With newer technology and a range of high speed connectivity solutions, Velsys is particularly active in this sector.

Why are increasing numbers of institutions choosing Velsys to supply and support their e-FX operations and what do they like about the value proposition that the company offers?

Simply the need for more control over the whole of the FX supply chain coupled with necessity. We have all seen the BIS numbers which show the market doubling in size since 2007. What the reader may have missed is that the BIS also reports the in the same period the average transaction size has halved – i.e a 400% increase in trading volumes. Furthermore, that the market share of the “other” financial institutions is growing at a much higher rate than the market as a whole –i.e. more entrants and therefore more parties for banks to interact with and manage – electronically.

There are two main reasons why more banks are looking to Velsys for solutions. The first being to the desire to implement an e-commerce trading system they can control. Such organisations are likely to be moving from

either using multiple LP systems, a white label solution from a single LP or perhaps from using an ECN as their e-commerce solution. As mentioned above, these organisations are looking for control and flexibility. However, many do not know how large their business will grow and are therefore attracted by the “cloud” model, which involves limited initial investment plus volume related charges – i.e. a low risk approach.

The second group, often driven by poor transaction experience in API venues, are banks seeking to upgrade from an older system and benefit from the flexibility that can be achieved from modern systems and the rapid deployment that is possible. Many of the adopters of earlier solutions took over a year to implement and commission their current system. Many find these older technologies very inflexible and not built to effectively support multiple sources of liquidity and pricing and very limited with respect to ECN and API connectivity and the ability to provide browser based trading solutions and portals.

A recent report by a leading research firm indicates that technology spend in FX is set to substantially increase over the next 2 years. In what ways do you think the expertise Velsys has in understanding the structure of the FX market will enable you to take advantage of this future investment in technology?

I believe that our timing could not have been better. At Velsys we have in excess of 10 years experience in the FX market and this is reflected in an up-to-date solution that is effective and easy to deploy and we have the financial backing required to be successful in the market.



Regulatory effects of clearing FX Derivatives upon Post-Trade & Back Office processes

Nichada Katchamart, Back Office Product Manager and Mark Biezup, FX Product Manager, at SunGard Sierra discuss the need for flexibility in preparing for Dodd-Frank.

The regulatory changes for clearing FX derivatives that are proposed to be implemented by the Dodd-Frank Act will have multiple repercussions upon post-trade and back office operations. The proposed central clearing party processes for FX derivatives will require new technology and personnel investments to comply with these regulations. Even with the proposed exclusion of FX Forwards and FX Swaps from this process, at the very least there will be reporting demands for the trade repositories.

As the requirements for the implementation of Dodd-Frank are still being finalized, the need for flexibility



in connectivity, reporting and compliancy will be important factors in how entities meet these regulatory requirements.

Connectivity with new platforms

The move to an exchange-style trading and clearing model will necessitate changes in connectivity to Swap Execution Facilities (SEF), Central Counterparties (CCP), and Swap Data Repositories (SDR). SEFs will provide trade execution venues, the CCP will provide the clearing services, and the SDRs will provide data warehouses for trade details from initial events through other life cycle events to maturity.

While connectivity to all will not be applicable to all dealers and traders, the downstream effects will likely affect every participant. Although the details of these three types of platforms are still to be determined, it is clear that processing systems with robust and flexible connectivity options will be needed to allow for connection to these platforms.



Nichada Katchamart

Establishing standards

These new platforms will also require standardization of many static data items, some of which may not be present in existing systems. For instance, the proposal for Unique Counterparty Identifiers (UCI) will require co-ordination among entities to achieve standardization, and thus the need for flexible but eventual firmness in the definition of this data. Additionally, the ability to add new data types required by the trade repository (SDR) that dealers' current systems do not contain will be crucial, as the trade repository requirements are expected to be very detailed, including ongoing reporting of each trade and its events.

The foreshadowing of the data required by the SDRs can be seen in the recent NFA Nightly Reporting regulations that went into effect in February 2011. Besides many trade-level and customer details, and relationships between entities, details such as snapshot rates at trade time and (potentially) tick-by-tick rate changes have to be captured to ensure compliance with the new reporting requirements. At this stage of the Dodd-Frank implementation, a comprehensive but easily extensible data model is required to handle the finalized requirements.

Impact on the trade lifecycle

In April 2011, the U.S. Department of the Treasury proposed to exclude FX Swaps and FX Forwards from the "swap" designation and associated requirements detailed in the Commodity Exchange Act. However, FX Options and FX Non Deliverable Forwards (NDFs) will still be subject to the "swap" requirements of the Dodd-Frank Act legislation, from trade execution through clearing and finally to reporting, while FX Swaps and Forwards will be subject to at least the reporting requirements.

The trade processing life cycle for the above products will be impacted by the new regulations. This includes the introduction of new workflows and processes for clearing as well as trade life-cycle reporting. Banks will need to focus increasingly on the detailed workflow changes that will result from the regulatory changes. For example, counterparties on transactions in some installations will now become the CCP instead of individual counterparties, which will drive major players to increase their focus on clearing.



The impact to OFAC checking by these changes is another consideration that will need to be re-evaluated as requirements are finalized. To support these new workflows, a review of existing systems will be needed to determine if they need to be enhanced or replaced, potentially creating new costs for institutions to modify existing processes and infrastructure. In addition, back office staff will have to learn additional operational procedures based on the new requirements and obtain additional training to understand the regulatory changes.

Getting ready

Because the full effects of the Dodd-Frank legislation are yet to be determined, there is time for financial institutions to anticipate the implementation and be proactive in following the emerging, more-detailed requirements. Thus far, the stepped nature of the implementation, involving many government-issued proposals with requests for comments, ensures that the industry will have time to absorb the new demands.

Similarly, institutions and individuals can prepare for the new regulated environment as new competencies or re-training will be needed for both the SEFs and CCPs, as well as the institutions affected by these changes. Due to the currently uncertain nature of the implementation of Dodd-Frank, organizations can best prepare for upcoming changes by having a system with flexible integration points, data structure, and reporting capabilities.

Minimising costs and market impact with a new breed of FX algorithms



Nicholas Pratt

Nicholas Pratt explores what developments within the FX market are influencing the use of algorithms and whether proposed changes to the way the FX market operates will create new opportunities for these to add value.

such as 1940's philosopher and novelist Ayn Rand, the 1980's computer entrepreneurs of Silicon Valley and former Federal Reserve chairman Alan Greenspan and plotted a course that went from the rise of moral objectivism of the 1950s to the deregulation of the derivatives market in the 1990s to the financial crisis of 2008. Central to the plot was man's misguided belief that it was possible to use computer networks to create stable societies and markets that could operate free from the vagarious interference of political control.

The programme certainly evoked many interesting debating points and highlighted some provocative associations between key figures in the development of both banking and technology. Russian-born but US-based Ayn Rand was the founder of the objectivism movement, expressed most notably in two novels by *Rand*, *Fountainhead* and *Atlas Shrugged*. Rand believed that man's highest moral purpose was the achievement of his own happiness.

Her theories were largely ignored by academics and her books were poorly received by critics but she attracted a loyal group of followers in the 1950s including future Federal Reserve chairman Alan Greenspan who arguably did more

The BBC recently broadcast a series of documentaries by film-maker Adam Curtis entitled *Watched Over By Machines of Love and Grace*. The first of these programmes, *Love and Power*, looked at the rise of information technology and its use in transforming the financial markets. The programme's narrative weaved together the rise of influential individuals





than any other individual to deregulate the capital markets, accelerate the advancement of derivative instruments and pave the way for a decade long, global economic boom.

Rand was also highly regarded by many of the entrepreneurs of Silicon Valley that believed her ideas were central to the creation of a computer-based utopia where the power of networks would create a self-stabilising society that would free man to fulfil his goals uninhibited by political, social or moral restraint. This idea was encapsulated in an experiment devised by computer graphics engineer Loren Carpenter who set up a mass-sized game of Pong (a basic computer-based tennis game) controlled by the collective behaviour of the 500 audience members. Carpenter's argument was that a similar level of control could be exerted over computer networks if left to naturally propagate rather than artificially imposed by rules or regulations.

Computers become too powerful

The counterpoint to such arguments, and the central premise of countless science fiction works, is that the computers become too powerful to control and allow instability to run rampant through society, creating chaos. In the financial markets, this same premise is made. The internet has not become a self-policing network and mathematical models have not been able to predict market events and eradicate market risk.

Furthermore it suggests the argument that deregulation of the markets and the development of technology have jointly led to the growth of algorithmic trading, which embodies the havoc that can be caused when the pursuit of profit is unhindered by market regulation and turbo-charged by high speed technology. The integrity of markets was undone as short-term gain rode roughshod over long-term stability and traders were powerless to stop their powerful algorithms running away from them once market conditions deviated from the programme.

Of course the truth of the matter is more prosaic. As influential as algorithms have been, they are still only enacting the strategies of the human traders that devised them and are more akin to labour-saving appliances than mystical alchemy tools. However it is garbage in, garbage out and no algorithm will turn a bad strategy into a good one.

Of more pressing concern to the exponents and proponents of algorithms, especially in the FX market,



"..the concept of price and available volume is often based on the credit profile that you have. This means that two counterparties may have different credit profiles and a different perception of market volume."

is how the latest generation of FX algorithms will be developed. How can the latest FX strategies and trade scheduling models assist firms to meet their implementation goals and investment objectives via appropriate order slicing schemes? What impact will the growing need for market surveillance and real-time trade analysis have on the future development of FX algorithms? What factors contribute to overall trading costs and need to be addressed by FX algorithms? What types of proven strategies can be adapted from other asset classes for the FX market? In what ways can quantitative frameworks be combined with algorithmic FX trading methodology to help firms better manage transaction costs? Can we expect to see the development of anti-gaming algorithms similar to those being used in other markets? Will proposed changes to the way the FX market operates create new opportunities for FX algorithms to add value?

Factors influencing use of FX algorithms

According to Gary Stone, chief strategy officer at Bloomberg Tradebook, there have been two major developments in the FX market that have influenced

the use of FX algorithms. The first of these stems from the fact that more and more institutional investors, for whom FX may be a by-product of their central investment strategy, actively questioning the quality of their FX trades if passively completed by their back-office and custodians.

In some cases this questioning has reached litigation levels, as in the case of California pension fund CalPERS, which sued State Street in 2009 for alleged over-charging on their FX transactions since 2001. It is not just litigation that has illustrated the importance of FX executions to institutional investors. Several studies have shown slippage in current FX management processes.

As a consequence, institutional investors are now looking to have more control over the FX execution process. This focus has existed on the equities markets for some time thanks to the development of best execution policies and transaction cost analysis (TCA). But efforts to establish similar resources in the FX market are still evolving, have had to overcome some market structure issues that make this job more difficult – not least the lack of central counterparties providing comprehensive and up-to-date trading data.

On the buy side, FX is still typically done outside the order management system infrastructure and most buy side traders do not have execution time stamps on their currency trades. There are also some market structure issues with FX being an over-the-counter (OTC) market. For example, liquidity fragmentation, and the lack of trading and volume information make the creation of execution quality benchmarks difficult but not impossible.

"Firms in the FX market are using proxies to create a mid-point between the high and low points of the market," says Stone. "They can look to see how they have executed against this mid-point and in some cases firms that have many clients' data can create an execution universe and determine how they executed in relationship to their peers. Firms can use this benchmark and determine if their passive approach to FX trading produces execution results that are clustered at the extremes of the market rather than across the spectrum."

The second development has been regulatory. In the US the supervision of the FX market is spread across four different regulators – the Federal Reserve, the Securities and Exchanges Commission

ability to hide your tracks is a vital property of any execution algorithm

(SEC), the Treasury and Office of Controller of Currency (OCC) and the Commodity Futures Trading Commission (CFTC). They are predominantly focused on regulating the banks and ensuring they manage their risk rather than end-client interests. So while they have all uniformly adopted rules concerning capital adequacy, little has been adopted in terms of best execution. Furthermore, the FX market has fallen through the cracks in other wide-ranging regulatory initiatives, such as Dodd Frank, meaning that there are no real obligations to define or seek best execution in the FX market.

There are similar developments in Europe where the Markets in Financial Instruments Directive (MiFID) did address the FX market but focused on equities first. MiFID II may yet address this in the future, although there is still an element of uncertainty what will result from the current discussions. FX is after all, a 24 hour global marketplace. “The concern for regulators in both the US and Europe is that any radical steps may see FX trading migrate to environments with a lighter regulatory touch,” says Stone. This puts the onus on regulators to work together and seek to adopt a less prescriptive, principles-based approach in order to keep its large share of the FX market’s volume and activity.

In addition to the regulatory environment in the FX market, there are also some differences that result from the trading motivations of certain participants and this has implications for the technology used for trading. “For some buy side participants, FX is not central to the primary strategy of the firm thus it is considered an operational

aspect and left to the back office to clean up,” says Stone.

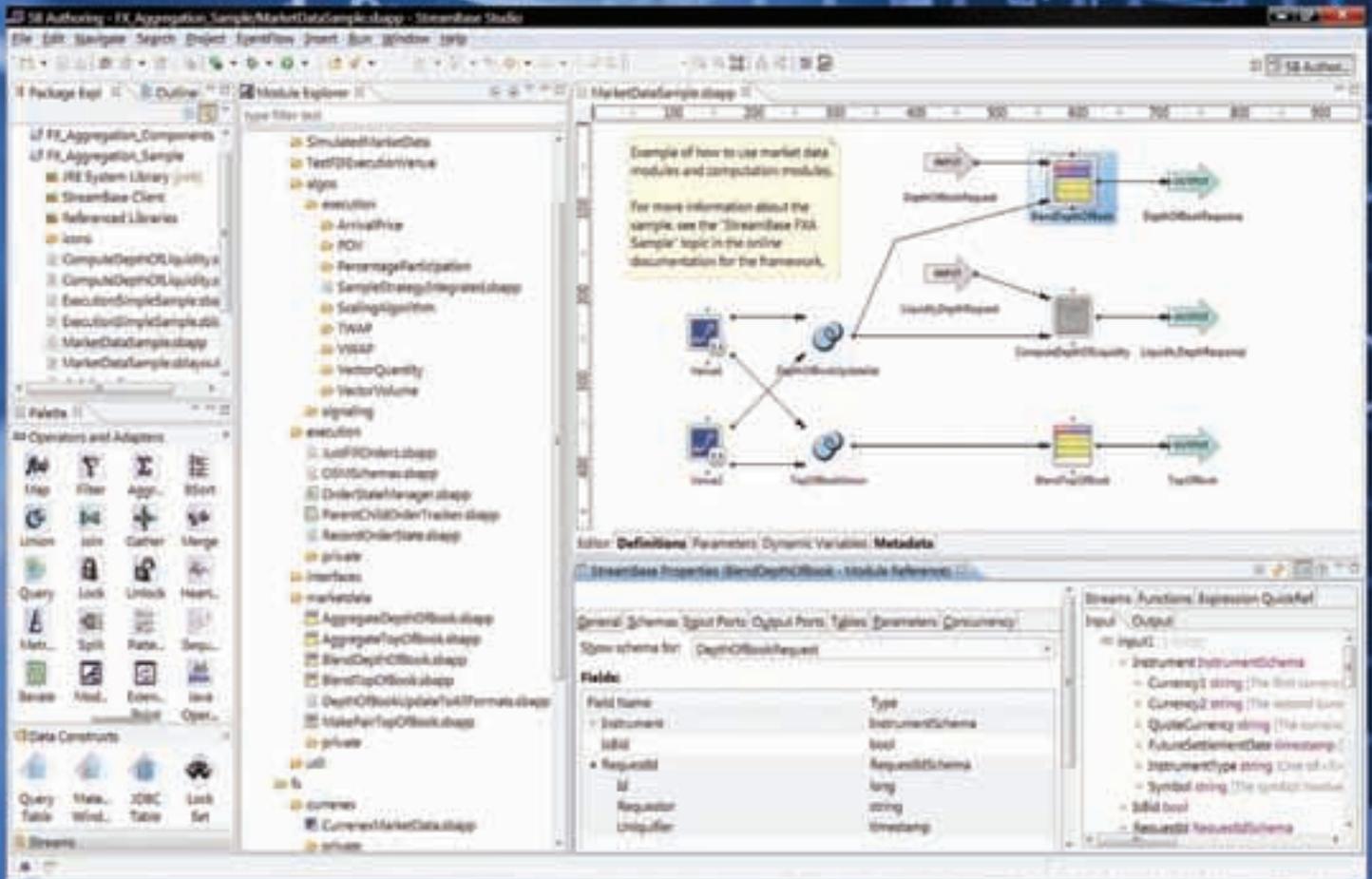
“Order management systems often do not capture FX trades and timestamps are seldom captured so the exact time of the trade is not always recorded. The lack of technology creates difficulties when it comes to assessing the quality of execution and the costs of transactions. Furthermore there is no consolidated tape for the FX market. And the concept of price and available volume is often based on the credit profile that you have. This means that two

counterparties may have different credit profiles and a different perception of market volume.”

Anti-gaming

Anti-gaming has also become an important consideration in the use of FX algorithms particularly for the less aggressive traders in the market who are keen not become the unwitting victims of other participants’ arbitrage strategies. In order to avoid being gamed, FX traders have to look at the environment in which they are operating and seek to gain as much information as possible about its machinations.

“The quality of your ecosystem is really important,” says Stone. “In the aggregated sense, the FX market is so fragmented and it can become difficult to tell what is ‘phantom’ liquidity and what is true liquidity. At Bloomberg Tradebook we are trying to create an FX marketplace where both buyer and seller can benefit from engaging each other. We also externalise orders so that it’s possible to get liquidity from other markets. We can examine the fill rates, price slippage and have started to look at ripple factors from events in the FX market to determine the quality of the liquidity.”



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Execution algorithms

Right now there is a big push towards execution algorithms in FX, says Irene Aldridge, managing partner at Able Alpha Trading, a multi-asset high frequency and quantitative trading and investment consulting firm. In the equities world these algorithms, the likes of TWAP and VWAP, have been used for a number of years but they are now making their way over to the FX market where they are being employed by traditional FX traders.

They are not being used as the basis of an opportunistic, arbitrage-based trading strategy but as a way to disguise their orders and to minimise market impact. The problem is that these algos – the TWAPs and VWAPs – have not always performed well in their primary function which is to disguise a trader's orders, says Aldridge. "They are very easy to spot because TWAPs and VWAPs tend to break orders down into equal-sized chunks so anyone that spots regular intervals in a trading pattern can then frontline that particular person's trades."

The latest execution algorithms in FX are being developed to minimise this predictability, says Aldridge, by acting in a non-linear fashion. "These algorithms have been developed not to follow TWAP and VWAP but to use them as abstracted benchmarks. They operate via quadratic functions and Sharpe ratio specifications that will slice and dice an order just as effectively as the classic TWAP and VWAP algorithms but execute them in a more random and unpredictable fashion."

ITCH and OUCH

Another development that could be seen in the world of execution algorithms is a push to adopt new faster data protocols. For years the industry has held the consensus that the FIX protocol should form the basis of an industry-wide messaging standard for sending and receiving trading-related data. However, in the equities market, traders are developing a preference for the proprietary protocols developed by Nasdaq named ITCH and OUCH (the names apparently are not acronyms lest one should try to work out what each letter stands for). ITCH is used for information exchange and is equivalent to other direct data feed protocols such as transmission Control Protocol (TCP) or User Datagram Protocol (UDP) and makes it possible for subscribers to track the status of their trades while OUCH is used for active trading.



Irene Aldridge

"The buy-side gets very concerned about being front-lined so the ability to hide your tracks is a vital property of any execution algorithm."

Whereas FIX is XML-based and is designed to be readable to everyone, ITCH and OUCH are both binary-based which makes them much faster. "FIX is getting slower and slower and more cumbersome with more and more add-ons which also makes it increasingly expensive for users," says Aldridge. "A move to ITCH and OUCH would involve sacrificing readability for speed but many traders see that as a good thing. For example, FX quotes are often sent via UDP or TCP and these messages are completely transparent to anyone listening in."

For now these demands for new data protocols are predominantly coming from the equities markets yet where the equities market treads, the FX market is likely enough to follow, eventually. "FX has been lagging behind the equities world for 10 years now so it is difficult to tell if the demand for ITCH and OUCH will reach the same level of intensity as in the equities world but it is increasingly apparent that equities traders are moving into the FX world," says Aldridge.



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Natural arbitrage

This migration is especially evident because the equities market is very saturated right now, however this is not to say that arbitrage strategies, high frequency trading and opportunistic market makers are wholly new developments in FX. “There have always been market traders in the FX world exploiting the inefficiencies of the FX market and now we are seeing more equities traders looking to exploit inefficiencies between different international markets in the FX world,” says Aldridge.

Nevertheless, the fact that there are also different types of participants in the FX world such as corporates who are trading because they have to rather than in the pursuit of profit does create natural arbitrage opportunities that do not exist to the same extent in other markets and will help fuel the growth of algorithmic FX trading. However does this growth need to be carefully managed? Does any care need to be taken that the relationship between these arbitrage seeking opportunists and the non-profit driven users



“For example when a key economic indicator is released an algo can quickly calculate the difference in the actual and estimate values and trade the appropriate product.”

in the FX market remain mutually beneficial and that the pursuit of short-term gain does not threaten the long-term integrity of the market – a gripe that has been levelled at the equities market and also the commodities market?

“I think the relationship between the two types of participants is mutually beneficial,” says Aldridge. “The corporates have a large range of options when executing. If they are particularly risk-averse they can use either the futures market or the swaps market to hedge their FX transactions. Dodd Frank and equivalent regulation in the EU is looking to tighten up those markets and employ a greater use of central counterparties but the FX market is much harder to regulate and it is less necessary. It is structured so that inherently it protects national markets from suffering any systemic shocks as a result of volatility in one currency.”

Market making strategies

In addition to the use of algorithms for minimising market impact, Aldridge also sees growth in the use of algorithms for executing market making strategies in FX, particularly given that manual trading is still so prevalent in FX. “Despite the increasing popularity of algorithmic trading, there are still a lot of FX trades that are handled manually either by voice traders or floor traders. I realise that in many cases these are relationship-builders that are trading on behalf of their clients but they are very expensive entities that require large bonuses. You can make markets just as successfully with computers. It can take time and money to successfully mimic the behaviour of a floor trader but once this is achieved, they are much cheaper to run.

The average computer-based trader will consume no more than \$500 of electricity a year – the equivalent sum can spent quite comfortably inside a hour for any respectable City trader on a night out. And there is also the added comfort that a computer is unlikely to take a day off to recover from the night before or suffer any emotional breakdown after excesses at work or anywhere else. As Aldridge says: “Computers are much more stable.”

Obviously this concept of stability should not be stretched to systemic proportions as was arguably the case in a more utopian era but clearly the boundless possibilities for greater efficiency through the use of

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algorithms is still to become apparent to everyone in the FX market.

Event processing

Another factor that is more influential in the FX market than any other asset class is that of events. Whereas all asset classes are price-driven to an extent, the FX market is very event-driven. Consequently the next step in the evolution of FX algorithms is to focus on events as opposed or in addition to volume and time and price.

According to Rob Passarella, vice president of institutional markets at Dow Jones,

most firms are looking to integrate systemic trading of currencies based on economic events. "For example when a key economic indicator is released an algo can quickly calculate the difference in the actual and estimate values and trade the appropriate product." As with many other algorithms, the speed of execution is critical to its effectiveness. "So the delivery of low-latency data is becoming a factor in the fast moving 24 hour FX market. These programs may not only be for client order execution but may also have offensive capabilities as well – as firms understand the micro-market structure of the participants.

As many others have stated, the unique structure of the FX market does create issues when it comes to disguising your trading objectives and minimising market impact, says Passarella. "Just as in the equity world, the idea is to minimize the impact of large orders on electronic trading systems. What is tricky in the FX world is the lack of a centralised exchange for particular currencies. The key for participants is to

evaluate levels amongst many connectivity networks to see the aggregate availability and volume. Time slicing of an order may not be a priority instead it may be price over multiple dealer parties. The market will decide the right strategies but clearly we are starting to see algorithms enter the FX marketplace."

The larger impact is in event processing and alerting, says Passarella. This impact is evident in the development of machine readable news, a service that elementises and disseminates news articles, press releases, newswires and official announcements (such as a central bank's decision to change interest rates) in order for it to be fed into

an algorithmic trading engine. "Elementised news or news as data is becoming a factor. It starts with numeric data content in releases but it will quickly expand to other types of semantic data," says Passarella.

Conclusion

It is still early days for FX algorithms in general and particularly for the use of event-driven algorithms and elementised news feeds but once it develops and matures it may not just be the traders that face being replaced or augmented by computers. Some time far into the future there is the remote possibility that news could end up being reported and read by machines. Of course journalists and reporters do not command the same six or seven figure bonuses as successful traders do thus reducing the amount of money saved in the substitution of humans for machines but, in the case of journalists, the increase in mental and emotional stability could be enormous.



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FX on

Exchanges align for new FX business

While volumes continue to grow, the world's derivatives exchanges are busy tweaking their FX contracts and launching new instruments in the light of the current regulatory debate over mandatory requirements for clearing bilaterally traded OTC contracts, as well as the general push to get as many of the standard OTC contracts traded on exchanges as possible.

New contracts from ICE

The IntercontinentalExchange (ICE) has launched ten currency pairs to add to the larger sized contracts in its existing portfolio. The larger contracts are more akin to exchange-traded contracts and will sit alongside the smaller contracts (€100,000).

ICE purchased the New York Board of Trade, and a thriving FX business, almost five years ago and the selling point at the time was that the FX products were all priced exactly to the way they are priced in the cash and EFP business. However, competing exchange Chicago Mercantile Exchange (CME) has built substantial volumes in screen traded activity by offering larger sized contracts (€125,000) as well as the €100,000/£62,500 contracts.

Ray McKenzie, vice president of ICE Futures U.S., says: "The dollar index has been very successful for us and we have seen such substantial growth – nearly 40,000 contracts a day last month, compared to 6,000 a day in May 2010 – that many of our customers trading the index have said if we matched CME's sized contracts in the euro and sterling, we would get a lot more business from them on the ICE platform

Exchanges



Ray McKenzie

“The main message is that we are very dedicated to the FX market, and are building our FX products on the back of the success of the dollar index contract.”

because they like the speed of the platform and the lower fees. They also like the fact they would be able to cross margin currencies against the dollar index.”

Regulatory uncertainty

McKenzie believes that the continued uncertainty over OTC regulation, and what products will and will not be cleared, is driving more market participants to exchanges. He adds that ICE intends to offer the best of both worlds and notes that ICE already clears many OTC products, in other commodities.

He says: “We intend to offer a choice to our customers, whether they want to trade and clear OTC products through us, this is what we have been doing for years, or if they want to trade a futures contract on a listed exchange. The main

message is that we are very dedicated to the FX market, and are building our FX products on the back of the success of the dollar index contract.”

He adds that the OTC market has evolved with more than 100 platforms to trade spot, but ICE believes that FX futures have always been a proxy for spot, and with low interest rates and good liquidity, McKenzie says many are moving towards the more transparent futures market. “The futures exchanges have extremely good technology which is a very compelling selling point and the buy-side customers are starting to look at cleared exchanges as part of their business. I think the market will continue to evolve and you will see more and more FX business traded on exchanges. This does not mean that OTC trading will go away, it is just that FX will grow to a much more significant percentage of overall exchange volume.”

New options from ISE

In January this year, the first wholly electronic options exchange, the International Securities Exchange (ISE), increased its options portfolio with the launch of currency options on the Brazilian real. ISE currently lists FX options on ten currency pairs. The USD-based, or “per US\$,” currency convention is available for all ten pairs and allows investors to express their views on the strength or weakness of the US dollar relative to global currencies while adopting the trading strategies they currently use for equity and index options. In a further boost for the options’ business, ISE then received regulatory approval for early opening (7.30am ET) and extended the FX options trading hours.

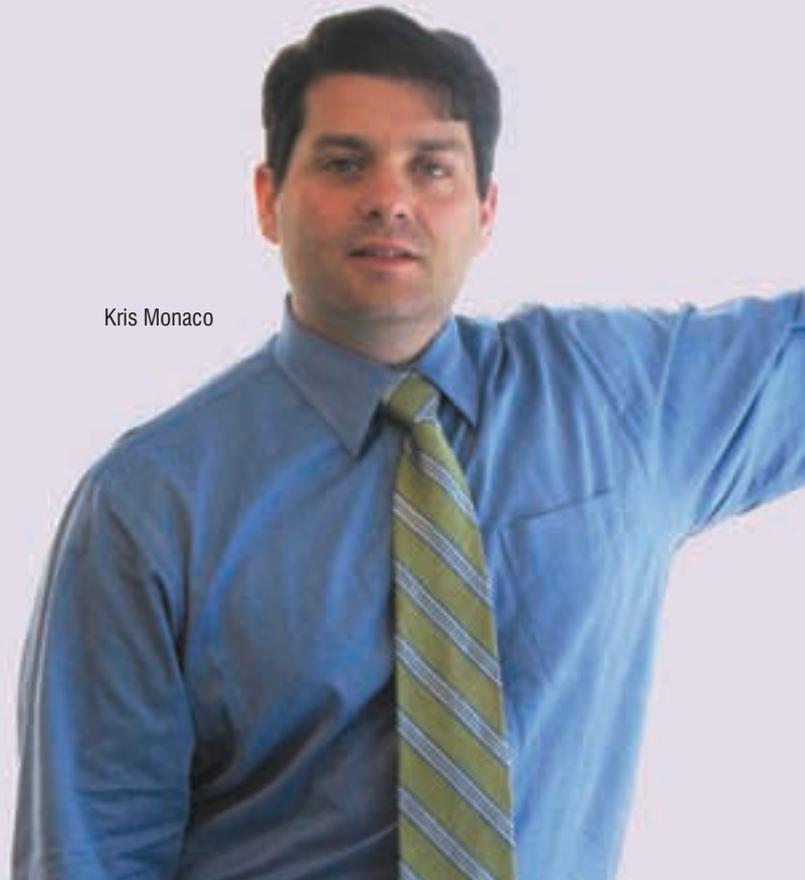
Kris Monaco, head of new product development, at ISE says: “By opening the market two hours earlier, we are meeting demand of a broader range of foreign exchange traders, especially from the UK and other countries in Western Europe. We have seen ISE’s FX options products benefit from additional liquidity during peak FX trading hours, although volume in the products has been flat over the last several months.”

Optimise

In April, the ISE began rolling out its new options trading system on Deutsche Börse Group's Optimise™ trading architecture. With Optimise, ISE will significantly improve the latency profile of its trading system and offer enhanced functionality to member firms. The Optimise launch began with ten symbols that trade in ISE's Second Market. The migration of symbols in ISE's primary market began in May, with the full roll out expected to conclude by the end of July. Initially, Optimise is being rolled out to replace ISE's options trading system in the US only. The cutting edge technology has the capability to ultimately connect the global network of exchanges, operated by ISE's parent company.

"By opening the market two hours earlier, we are meeting demand of a broader range of foreign exchange traders, especially from the UK and other countries in Western Europe."

Kris Monaco



More competitive FX market on JSE

The Johannesburg Stock Exchange (JSE) is making its currency derivatives market more attractive and competitive by providing incentives for larger currency deals and greater trading flexibility for investors. The measures include changes to the fee structure and the launch of new trading strategies.

The local currency market was first established in 2007, but institutional investors and corporates only entered the market in 2008 after a special dispensation in that year's budget address. Since then 20 million contracts worth R175 billion have been traded. Dollar/Rand contracts make up more than 80 per cent of the trading activity on the exchange.

Warren Geers, general manager for Derivatives Trading at the JSE, says: "We believe that there is still huge potential for growth in our market, especially now given the considerable discussion regarding derivatives reform and proposals to move more

trade on exchange. Investors want flexibility and risk management; we believe that we can offer them both.”

New fee structures

Because competitive pricing plays a key role in attracting participants, the JSE is set to introduce new sliding scale fee structures as an incentive to trade greater volume at the exchange and to encourage same day trading activity, the JSE has committed to a zero fee for the second leg of all intraday trades. “We would like to see more day traders participating in our market. At present this type of investor is not very active in our market,” says Geers.

To promote cross currency trading, the JSE will now only charge on one side of the transaction. This allows participants to synthetically trade any two foreign currencies against each other and the fee will be as if the participant was trading the direct cross-currency.

An advantage of trading JSE-listed derivatives, as compared with over-the-counter (OTC) alternatives, is that on-market instruments require no foreign exchange clearance and are settled in rand. JSE’s derivatives also offer the reassurance of Reserve Bank and Financial Services Board regulation along with South Africa’s five major banks as counterparties.

Flexible contracts

The JSE has launched a new initiative on the foreign currency contracts. Any Day Expiry contracts allow investors the flexibility to pick the expiry date of the contract. The introduction of this new currency product is in response to the wholesale market looking to hedge their currency risk with increased precision. “This new contract meets the needs of a certain clients, for example, hedge fund managers working on a short term currency strategy or those in the import and export arena who would like to match exact expiry dates with those of the delivery of goods,” says Geers.

Apart from the added flexibility of picking the expiry date, all other contract specifications and fees remain the same as the existing currency derivative products, which expire on set quarterly close-out dates.

“Many investors prefer using OTC derivatives because traditionally they are more flexible than their listed counterparts, but the reality is that they have a number of disadvantages, including counterparty risk and opaque pricing. Products like the Any Day Expiry currency derivative demonstrate that the JSE is cognisant of the investor’s needs for both flexibility and sound risk management,” adds Geers

Demand for customised products

In line with international trends, the JSE is seeing a greater demand for customised derivatives products that are traded on-exchange and with the introduction of more flexible contracts being listed and the exchange is experiencing even more demand from the asset managers and hedge funds as this suits them more than standardised contracts.

Says Geers: “We have seen the demand increase from users of OTC products trading more regulated exchange styled products. This has been driven due to mandates from funds and of course better price discovery.”

He adds that the launch was prompted by the need for more flexibility from exchanges, as opposed to only allowing for the normal standardised products. “Clients were also required to trade/hedge to specific dates and unless we were able to accommodate them, they would have continued to merely trade OTC styled products,” he adds.

As a result the exchange experienced its biggest month of trading in March 2011 since inception, and Geers says it was purely attributable to the new styled contracts being launched.



Warren Geers

“Products like the Any Day Expiry currency derivative demonstrate that the JSE is cognisant of the investor’s needs for both flexibility and sound risk management,”

OSE gets set for FX growth

Matthias Rietig talks to Frances Maguire about how the exchange's FX market is poised for growth when Japan's new leveraging limits take full effect.

Osaka Securities Exchange's (OSE) OSE-FX market offers eight yen currency pairs and three non-yen products. At present, the OSE has four designated Market Makers: Money Partners, JP Morgan, Citi and Ueda Harlow. In addition, 14 online brokers connect to the OSE-FX market.

Matthias Rietig, advisor to the board of OSE, says that depending on demand the exchange may consider adding more exotic currencies in the future but at the moment the bulk of the trading activity is concentrated in Euro/yen, US dollar/yen and euro/US dollar contracts. Currently the user base of OSE-FX is completely made up of retail flow, most of them short to mid-term speculators, but Rietig says: "The market structure of OSE-FX also appeals to the very active crowd of Nikkei mini futures traders and we also start to see this layer engaging in our FX market."

Order book market

The exchange provides an order book market, which Rietig says attracts the non-traditional FX players. He believes the market is set for growth due to the changes in regulation regarding the levels of leverage allowed in



Matthias Rietig

"The market structure of OSE-FX also appeals to the very active crowd of Nikkei mini futures traders and we also start to see this layer engaging in our FX market."

OTC products. Japan has seen explosive growth in the numbers of retail customers trading foreign exchange on margin through OTC online-brokers however the Japan Financial Services Agency (JFSA) reduced leverage limits for OTC-FX contracts to 50 times in August 2010. This will be further reduced to 25 times from August 2011. In addition there is a difference in taxation between listed and non listed FX products.

Rietig expects the exchange to win business because of the greater transparency offered by exchange-traded contracts. He says: "In order to promote transparency and offer a fair market the regulators are saying they want this business to move on to the exchange, and a regulated, market, OSE is the first of its kind that actually offers market depth."

He adds that there is also a difference in the taxation because OSE contracts are technically derivatives – futures contracts with a CCP – and are more tax efficient at 20 per cent taxation as opposed to up to 50 per cent for OTC-FX contracts in Japan. He says: "We will most likely trade a lot more from August because then we will see the effects of the harmonisation e.g. the equalisation in leverage between OTC FX and exchange-traded FX. In addition the tax advantage and transparent order book should push more volume on exchange."

"The platform we have is relatively strong, fast and stable, with latency at around one millisecond, this is also of interest to the agency brokers. FX is gaining more popularity among HFT firms globally, due to our very active Nikkei Futures and Options market a lot of these players are inquiring about the possibility to participate in our FX market as well. We haven't rolled out next step yet, since we first want to grow the market a bit further but it will certainly come soon and then the whole FX market in Japan will change dramatically because we will have the tools to provide even more competitive tighter spreads to be a viable alternative to the OTC brokers and our competitor Tokyo Financial Exchange (TFX)."

Once OSE makes the step to connect agency brokers, if there is demand the exchange will also offer co-location, proximity and direct connection services – already offered with the OSE matching engine and used by retail brokers trading OSE on the new J-Gate platform that went live February 14th this year. The OSE-FX market provides FIX connectivity and is hence easy to access offering a global standard connectivity protocol.



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Gerry O'Kane

Gerry O'Kane looks at growth in e-FX throughout the Middle Eastern markets and how resistance to electronic systems is changing rapidly in the fast shifting economic and socio political geography of the region.

Regional e-FX perspective

Only five years ago there was an acceptance in most of the international banking community with operations in the Middle East, that resistance to electronic systems was fairly strong. Traditional ways of doing business in the region, based on relationships, had a strong pull.

Today the consensus is that currency products are becoming increasingly interesting as a means to hedge risk and speculate, if only in a relatively limited way. Increased competition and demand from the buy-side has seen a previously reticent banking and broking sector gradually climb aboard the electronic bandwagon.

“If customers are happy doing trades over the phone then the local banks aren't bothered with electronic systems, however this is changing and many are now seeing use of the e-channel provide benefits like



on the Middle East

transparency and liquidity,” says Mark Warmis, head of sales, for EMEA at FXall.

“There is no doubt that in the Middle East FX Trading has been growing, maybe not at the same level of somewhere like Japan, but there is certainly an opportunity” confides Karim Farra, Chairman of Amana Capital in Lebanon.

The trouble with the Middle East is that nothing is clear – the trading landscape is as clear as a desert sand storm and differs from country to country. Even the most recent tri-annual report from the Bank of International Settlements has few concrete figures, with Middle East trading mixed in with African numbers.

Growing GCC awareness

While the GCC (The Cooperation Council for the

Arab States of the Gulf),* States may have taken their eye off the bigger institutional FX picture, other FX markets in the region have quietly been doing well. “In the past, we would typically see the majority of our FX volumes coming from money managers in the Gulf states and self directed ‘professional’ traders from countries such as Turkey, Egypt and Lebanon. We have over the last few years seen a vast increase of business coming from ‘retail’ orientated brokers and high frequency traders based in Israel and more recently Cyprus,” says Farooq Muzammal, Head of foreign exchange at Marex Financial.

“Naturally countries vary and there’s simply no data on types of product in demand, in either trading systems or FX instruments,” warns Mark Kiley, Global Head of Sales, Treasury Transactions Services, for Thomson Reuters. “The fact is there’s always been a certain amount of international exchange, but it’s now

* Six Gulf Arab countries, i.e., the United Arab Emirates, the Sultanate of Oman, the State of Bahrain, the State of Qatar, the State of Kuwait and the Kingdom of Saudi Arabia



Karim Farra

“It remains a challenge to open accounts online directly without face-to-face interaction; but doing it directly online is becoming a growing trend for the retail market”

on a bigger scale and with more sophistication. And sharia law hasn't got in the way of that growth.”

Institutional, corporate and retail sectors in the region have all increased their exposure to FX hedging or speculating. This has meant more interest in online FX, but a widespread hug to the latest e-platforms and trading systems is yet to happen. The benefits, so often touted about electronic systems, from reduced execution risk, reduced staffing, reduced errors from automated STP and efficient operations, are not necessarily arguments that certain markets in the Middle East will accept yet.

FX opens doors

“In terms of investment within the GCC those interested in FX were often those who were heavily involved in equity markets from early 2000,” explains Iskandar Najjar, CEO at Alpari Dubai. “They were achieving outstanding results of 200-300% per year on certain stocks. That opened doors and made noise around speculative investments and, let's say, how you could make money with a click of a button.” But the local equity market bubble burst around 2005, as anyone might expect with such high levels of return. “The players became better aware of risks and more sophisticated and diversified in their investment portfolios and sought alternative investments with a

similar nature. The best of these was FX. That's opened the doors for the GCC,” adds Najjar.

But the levels remain well below other big international markets. In part because much inter-regional currency trade is between currencies already pegged within narrow limits to the US dollar. As a result, products of greatest interest are US dollar forwards and spot trades against the major currencies like Euro, Yen, Swiss Franc, Sterling and increasingly, Yuan and Indian rupee products. This is primarily to facilitate trade, rather than pure speculation.

Naturally crude oil prices create a strong link to the state of the Middle Eastern economies, with oil receipts accounting for up to 90% of government revenues in several Gulf countries. But many governments have pursued expansionary economic policies, with free-trade zones, in particular building financial centres and gradually extending investment rights to foreign nationals. These huge investments have brought infrastructure project trade and finance, expat banking services and boosted traditional business like gold and commodities.

“Remember everything is being imported, from watches to cars, and there are huge ongoing infrastructure projects that have to be paid for” points out Kiley.



Mark Warms

“..the first clients we went after in the region have been more those who were clients of western banks, which includes local banks and sovereign wealth funds or branches of western corporates,”



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Corporate FX market

In essence this leaves companies and people managing risk whether importing, exporting or investing in the region or outside.

“I’d say we’ve managed to embed ourselves into the corporate market and we’re balancing our huge corporate capabilities with the requirements for an expansion into the financial institutions space,” says Declan Clements, Head of eCommerce Middle East and Africa at Standard Chartered Bank, which now has the largest FX dealing room in the region. From an eCommerce perspective we have developed a comprehensive coverage of GCC currencies and those of the broader region. Our single bank platform allows us a great deal of customisation capability which differentiates us from vanilla offerings in the market.

“There is definitely a much larger proportion of smaller corporates and SMEs transacting when compared to European markets, while at the other end of the spectrum local financial institutions are generally putting funds outside of the region for investment. The local equity markets don’t have a tremendous amount of depth apart from Saudi Arabia,” Clements adds. “A lot of the region’s banks are fairly risk-averse and it’s similar with the corporates which are mandated to only trade FX which is directly related to their business.”

Certainly for FX all the corporate FX market has been important. “Traditionally we’ve had a large base of corporates because they deal with western banks. So the first clients we went after in the region have been more those who were clients of western banks, which includes local banks and sovereign wealth funds or branches of western corporates,” reveals Mark Warms.

But it is vital to understand that how e-FX will develop in the future, is based on how the region itself has been developing. There is the Arab Spring to consider which brings a question mark to stability for market growth, (privately observers believe that Bahrain may have jeopardised any hope it had of gaining more influence in financial markets following the ignominious shifting of the central bank’s operations after protestors turned up on its steps), issues of sharia compliance, traditional ways of doing business, pegged currencies and so on.

Growth of e-FX

Prior to 2005 electronic systems were being pushed with limited success across the region. There were



Mark Kiley

“The fact is there’s always been a certain amount of international exchange, but it’s now on a bigger scale and with more sophistication. And sharia law hasn’t got in the way of that growth.”

several reasons. Local banks and brokers working on behalf of companies, funds or whoever had control of pricing and were making healthy margins. Electronic systems could put a stop to this.

“It remains a challenge to open accounts online directly without face-to-face interaction; but doing it directly online is becoming a growing trend for the retail market” observes Farra. “However, the actual FX Trading is predominately done electronically with only about 20% of the trades done through phone calls. Traditionally, brokers have been reticent to take on e-commerce. Often, the houses don’t know about it because they still offer traditional products like stocks and bonds. I’d say the majority of those offering e-FX are new Middle Eastern companies or older European or US companies” he adds.

For banks and brokers going down the advanced electronic route, white labelling has become the norm making more sense than developing their own turn-key solution.

But things are changing. “The National Bank of Abu Dhabi’s trading room has gone from 5 to 50 people in last six years to supporting expats, corporates and the



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oil and gas industry. How do you scale a business like that? You simply can't go down the road for a coffee each time, you need to encompass new ways of doing it," proves Kiley.

And these electronic systems usually bring price transparency.

"Of course you've had some electronic trading for years but in the past you also had institutions which were taking FX positions against the clients. At ADS our only interest is the client and we don't have a book, and this is why firms like ours are growing and why electronic and online systems are becoming more popular," argues Philippe Ghanem, Managing Director, ADS Securities.

"Now we're seeing probably the majority of local banks offering electronic trading, especially those who were pioneers in more adventurous FX, but not all. White label e-FX solutions have been selling to banks over the past five years but over the last year or two that demand has expanded," agrees Najjar of Alpari. "Now brokers and banks realise there are profit opportunities elsewhere and this goes hand-in-hand with the regulation," he adds.



Iskandar Najjar

"Now we're seeing probably the majority of local banks offering electronic trading, especially those who were pioneers in more adventurous FX."

It should be noted that many of the regions markets have put in place regulations that can handle the demands of FX electronic trading and their broad range of financial instruments, many of which could be considered non-sharia compliant.

Sharia compliance

The cheap headline would be that Jordan's top religious official issued a fatwa banning electronic trading of currencies owing to the 'financial risks' involved in such a type of business in 2008. In reality the Jordanian government had enacted a new law regulating the trading of currencies on the internet after high numbers of people went bankrupt, suffering big losses in currency trading with foreign markets.

"The fact is that brokers and systems weren't regulated and the official figure is that there was \$350 million in retail FX investment and as a proportion of Jordan's \$4-5 billion GDP it's large - some believe it was far greater than that," recounts Najjar.

"What happened in Jordan was a failure to oversee the activities of FX businesses but it had little to do with sharia issues and other regulators have learned from this," agrees Farra.

But the sharia question remains and one would have thought it would have had a material impact on the regional growth of e-FX. In the simplest of terms margin trading, or contracts that do not settle can be considered gambling, while forwards and swaps include interest calculations, is something again frowned upon.

"It's true that you have to adapt to the local rules as you do everywhere, however in the UAE, there's no law demanding you to be Shariah compliant. Where a client chooses to be Shariah compliant, it's up to them to police themselves through their Shariah supervisory boards," says Ghanem.

"There are major challenges but the largest investors, the sovereign wealth funds for example, invest most of their portfolio in conventional products so being sharia-compliant is not a must in the region," accepts Farra.

"Certainly regulators in the region better understand the FX trading tools and it's tacitly understood that it's up to the investor to make up their own mind if this is sharia compliant or not and use what they're comfortable with and that is in line with their beliefs," agrees Najjar.



Differences in sharia compliant currency trading and non-sharia trading

According to Farooq Muzammal of Marex Financial the main difference is in the interest or fees paid on the account or the position held. A traditional FX account would be set up to pay or receive a swap fee (interest) when rolling the position for a future date (speculation).

A sharia compliant trading account must be set up as interest (Riba) and swap free account and there should be no additional charge or penalty for rolled open positions.

Taking Murabaha (contracts of sale) as an example, the intermediary (service facilitator) purchases the goods from the supplier and sells it to a buyer (end user) after marking up the price. Under the Murabaha structure, the full ownership of the underlying position (or goods) should be transferred to the new owner in order to fulfil the sharia requirement for this product.

As the FX position would have two legs (Buy and Sell), a similar activity will take place to reflect the completion of the trade. The difference between the cost and revenue for the two trades would constitute the spread. Some brokers link the forex trade into a commodity (i.e. metals) where a metal position is rotating between the three parties (client, intermediary and broker or bank).

The client will end up with a cash position only that would reflect the profit and loss of the forex trade executed.

But there are a growing number of sharia compliant products out there. "Most existing platform vendors offering sharia products in reality are merely offering Riba (interest free) trading. This effectively means that instead of adding or subtracting interest swap fees a charge is levied instead," explains Farooq Muzammal. "Because of our interests in the commodities markets we can use the warrants of these products in order to provide true hedging for client FX hedging purposes."

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Some of the products are designed to be international, at least accepted by the most active sectors of the Islamic financial marketplace, others with a stricter and more local interpretation of sharia.

“There are swap products that exist which are sharia compliant even here in Saudi, often within the banks because they’ve innovated a suitable structure. But they can each be very heterogeneous and their own sharia boards will come to their decisions on what is acceptable. In reality these products are primarily about economic flow rather than speculative trading” says Tristan Attenborough, Managing Director and head of J.P. Morgan Treasury and Securities Services in Saudi Arabia.

But these specialised and more complex structured products create problems of their own. “While various institutions mainly in the Gulf region are offering the standard Islamic Financial Products, not all of these products can be traded electronically due to the complexity of the rules that qualify them to be compliant,” says Muzammal. “Few institutions have managed to map FX Trading and Murabaha

“In the past a client would typically find a money manager to trade his money for him. Although a good percentage of volumes still come from money managers, we are seeing more and more professional traders trading for themselves.”



Farooq Muzammal

into their electronic offering and other products as Musharaka (Joint Venture), Ijara, Wa’ad, Hibah (Gift or Donation), Mudaraba and Wakala (Agency) are also offered to clients but not in a fully automated service.”

Agreeing on standards

But the hiccups don’t stop there. “Products are global and sharia banking has become quite fashionable,” Kiley remarks. “The challenge is that Emirates doesn’t agree with Malaysians on what constitutes sharia and the Saudis don’t agree with the Kuwaitis, so coming to a widely agreed standard is difficult. But in all fairness it doesn’t influence trading,” he adds.

But it certainly isn’t the other way around. “For clients dealing directly on our system there has to be some sort of level playing field. Because we’re a platform that puts counter-parties together, you have to apply a standard which is more of a western standard – spots, swaps, forwards, and so if we do provide a system to a client and they are distributing onwards, it’s up to them to see how it fulfils their needs,” says Mark Warms. “Any bank in the Middle East, for the most part, that runs their own books and that trade with western banks will often have to play with the international rules for the most part. However for their own customers they may take other actions or modify the product structure for them, its their prerogative.”

Popular products

“Margins, spreads and liquidity mean that clients typically stick to the liquid G7 currency pairs and precious metals,” reveals Muzammal. “Most professional customers tend to have a short term outlook to their trading with most customers not maintaining a position longer than a few days.”

Often holding conventional swaps on an intraday basis is not unusual as it allows settlement in a way that it is not regarded as compromising sharia.

The reality is that trading in the GCC currencies is limited. “The currencies are pegged to the dollar and each central bank ensures the market trades in and around that peg,” says Attenborough. “Those who are doing genuine business are looking to hedge the currency risk component, even if it is relatively stable between the GCC currencies, or you have people who want to speculate or take a position. The latter of those two is not so common other than when there is speculation over revaluation against the peg,” he adds.



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There has been a lot of talk since 2007 of de-pegging from the dollar because of its fall in value compared to the economic growth of the GCC states. “That talk caused some wider ranges than usual to be traded but nothing in comparison to Euro or dollar on a normal day,” recalls Najjar. “If they do unify to one currency it could be something interesting but we’re talking a long way off and it’s been in talked about for long time.”

“My personal view is that it’s unlikely that this currency revaluation will happen soon because the GCC is focussed on stability and calm given events of this year,” observes Attenborough.

While the pegged rates of the GCC currencies offer limited opportunities, Mark Kiley says that the release of Thomson Reuters’ Spot Matching Service for four of the six currencies has seen growing interest. “It was slow at the start but FX volumes are increasing and we’re seeing trading coming from top banks and financial institutions from London, New York, Singapore and Zurich,” he says.

“In truth it’s the international currencies that interest investors, the motivation behind the GCC products is more of a marketing tool rather than an investment tool - you see very little volume and the ranges in which they trade,” argues Najjar.

“Risk mitigation is certainly the main part of the FX business in the region,” says Clements.

“Investment Companies acting for large government funds and sovereign wealth funds overlay their speculation with FX primarily to mitigate and hedge asset risk. The key missing component in the Middle East electronic market space is the participation of local banks on the sell side.

From his viewpoint, the most common players in the electronic marketplace



Declan Clements

“Risk mitigation is certainly the main part of the FX business in the region.”

are the international banks with FX platforms, Bloomberg and EBS. “Reuters deal-matching is widely used but we still see a lot of transactions via Reuters conversational systems. In addition, there are the single bank portals of which many of the local banks were early adopters. However we’ve seen some real estate pressure from local banks using several single bank portals resulting in a marginal move towards multi-bank portals. Standard Chartered’s own single bank platform has seen significant take up from corporates in the region given the deep liquidity in GCC and regional currencies, and our broad coverage across the Asia and African footprint.

And through these go deals on hedging gold bullion, trading oil, using spots and forwards, swaps and even NDFs. “The amount of NDF traffic has been growing year-on-year. At Standard Chartered we are seeing much more hedging of Asian restricted currencies as trade corridors between Asia and the Middle East expand rapidly,” says Clements.

But the vast majority of trading stays within more obvious markets. “Investor’s are mainly looking at

liquid markets and they don't want to be stuck with assets that they couldn't sell like in 2007/8, on the other hand where you see currency volatility, you will see a regional interest," says Ghanem.

Retail investors

"It's up to investor sophistication, but retail players are far more comfortable trading the recognisable currencies. From an institutional point of view they know there are greater fluctuations with emerging currencies like the Rial or Peso, so there is interest but it's dedicated to the more sophisticated trader," agrees Najjar.

However, retail traders are increasingly having a part to play in the regions e-FX development. "There has been growth in the retail business throughout the region which does have a high number of high net worth individuals and I do think from our point of view there are more banks taking advantage of electronic systems as a way for them to reach their clients including retail," says Warms.



Philippe Ghanem

"It's true that you have to adapt to the local rules as you do everywhere, however in the UAE, there's no law demanding you to be Shariah compliant. Where a client chooses to be Shariah compliant, it's up to them to police themselves through their Shariah supervisory boards."

"Internet penetration, a greater awareness of new investment avenues and also being able to access more information all makes investment in FX more comfortable for many people and gives them more confidence to trade," repeats Najjar. It has required a greater personal interaction with potential clients than might be found elsewhere but gradually, he feels, the retail market is finding it easier to trade online than getting on the phone to a broker. And from the retail perspective it has pushed FX providers to use new technologies to keep customers and utilise new business models to attract more.

"We have our own estimates of the industry in the Middle East and we reckon there are over 100,000 retail accounts dealing \$ 200 million per month and that's doubled in the past four years," reveals Karim Farra of Amana Capital.

He also believes that the most popular platform remains MT4. "It's easy and players know how it works and while there are some customised Arabic interfaces, in general, English is preferred," he adds

"In the past a client would typically find a money manager to trade his money for him. Although a good percentage of volumes still come from money managers, we are seeing more and more professional traders trading for themselves. Low returns on local stock markets, improved internet speeds and 'retail' orientated all-in-one trading platforms have made life a lot simpler and cost effective for these customers," agrees Muzammal.

But the future growth of retail online markets in the region is open to question. The internet has become far more common in the region and this is also driving business, but there remain drawbacks. While the Egyptian market is not huge, the uprising against President Mubarak saw the internet cut off leaving companies and retail investors unable to close positions.

"You couldn't make an electronic trade or do a wire transfer for two weeks and so couldn't fund a position. For us these sorts of problems require a case-by-case approach rather than a policy but do show the sorts of issues that might arise," points out Farra.

One area where technology is still to make an impact throughout the area is high frequency or algorithmic trading, although like everything else regional confidence is 'high'.



Tristan Attenborough

“My personal view is that it’s unlikely that this currency revaluation will happen soon because the GCC is focussed on stability and calm given events of this year.”

“High frequency and algorithmic trading? No it doesn’t exist to any big level, if you’re including Israel in the Middle East then there are some operations,” points out Warms.

There are moves for this to change. “The market is opening, but more so to sophisticated traders, and there is more and more noise around, so I expect this year to be a big one for algorithmic trading. It’s something we’re thinking about in seeking partners,” says Farra.

Conclusion

According to Philippe Ghanem, pressure on local institutional players to be able to compete in the international marketplace has brought clients searching for black box solutions. So there is optimism that both the forex market and the use of electronic platforms in the Middle East will grow rapidly and certainly faster than in the past five years.

“I think the driving factors for electronic FX are fairly universal in that its speed, efficiency, reduced cost of processing and having the ability to distribute prices and reach to your clients easily. Add to this upcoming Regulatory changes, many financial institutions and banks are embracing the benefits of increased technology.” predicts Mark Kiley.

Taking steps to achieve success in the Retail FX industry

Lars Holst, CEO of CFH Markets, talks about the steps organizations should consider taking which can help them achieve success in the ultra competitive Retail FX sell-side space.

What factors are likely to influence whether an institution chooses to build or buy-in the expertise required to develop and deploy an online FX trading platform geared towards Retail FX operations?

It depends very much on the institution in question. The major banks for example, have often found that size and resources do not necessarily equate to expertise in a particular field. Several banks have ended up taking third party technology simply because they do not have the required resources to produce something within what is effectively a niche technology space. Time to market is another factor; to develop a full, front to back-end system can take several years, even if you have the relevant know-how. Finally, I would say a lot depends on intellectual ownership of the technology, along with independence; so many platforms are extremely similar and easily recognizable, the only way to really stand out is to create your own GUI skin from scratch as we do each time at CFH.

What steps can new Retail FX sell side firms take, to gain access to interbank liquidity from the top FX banks?

Obviously the best way to access this level of liquidity is to go direct to the banks themselves. But we all know that is has become tougher to get and it requires a lot of resources and patience more than anything, along with a significant balance sheet if you want to deal with the tier 1 banks.

So the optimal and most efficient route is to choose a broker who will give them access to clean interbank liquidity, one that doesn't run any kind of internal risk; that will immediately put them at a disadvantage and affect their clients' trading experience, more often than not in a negative way. We have already seen a growing number of second tier providers offering STP solutions (some more STP than others, it has to be said), and we believe this trend will continue.

In what ways can CFH Markets help firms to build a presence and quickly establish a brand in markets they wish to target?

Being highly focused on technology, as well as being able to offer access to interbank liquidity, we can allow a firm to be up and running as a fully operational, independent entity within 4-6 weeks. Our technology is extremely flexible, allowing us to brand our platforms in any way the client wishes. We provide them with technology that allows for fully automated client on boarding; from the demo registration process, to CRM integration, to converting client accounts to live. But above all we have people with know-how and expertise that you don't find anywhere else in the industry and in the end it is a peoples industry more than anything.

How far throughout the Retail FX business value chain can CFH Markets assist firms to minimize risk, maximize profits and overcome operational hurdles?

We are one of extremely few firms globally, who can offer them the entire value chain, all in a one stop shop and all hosted by us, along with 24 hour



Lars Holst

support. The tools we provide firms with allow them to automate more or less every aspect of the business. In terms of maximising profit, we give them 100% control over the levels of commission and spreads they wish to apply and we give them access to unrivalled interbank liquidity. In terms of operational hurdles, they are provided with a sophisticated yet intuitive administration tool which lets them create and modify client accounts on the fly, and they can view their internal and external risk in real time.

What lessons can new entrants to Retail FX learn from successful sell-side players who have utilized the industry knowledge and insights provided by leading specialist consultants like CFH Markets?

The most important lesson is that no two companies are the same; there is no set formula that works for everybody across regions and regulatory frameworks. That is why it is more important than ever to work with the right people that care about the client without any conflicts of interest. With CFH they get access to unique global know-how and infrastructure that allows them to become leaders in their space with a setup that has been tailor-made to their specific needs and requirements.



High Frequency FX

where trading opportunities meet new technology

Opportunity is essential to any trading strategy but, as Nicholas Pratt explores in this article, what sets high frequency trading apart is the speed at which these opportunities are discovered and the speed at which the resulting trades are executed. All of this has been made possible by technology, both the provision of it and the lack of it, for it is the disparity in the extent and sophistication of technology that first presented the kind of opportunities that saw high frequency trading blossom in the FX world.

opportunities arise as new technology is developed. Furthermore, will the FX market, which was slower to adopt high frequency trading than the equities market, actually provide more long-term opportunities for arbitrage-based strategies due to its over-the-counter nature and various idiosyncrasies?

Market structure

Certainly some of the issues facing high frequency traders in the FX market are a result of the inherent differences in market structure in comparison to other asset classes, says Peter van Kleef, chief executive of high frequency trading firm, Lakeview Arbitrage International. The most obvious of these is the fact that there is no central marketplace akin to the exchanges of the equities market. This means there are multiple connections that are needed and much more fragmentation in the FX market than elsewhere

There is also a much smaller choice of products available in FX. There are only really a handful of major currency pairs that have a lot of liquidity rather than thousands of stocks on the equities markets. Given that most high frequency trading firms will operate in multiple asset classes and will also trade FX rather than operating solely in the FX market, this makes the idiosyncrasies of the FX market all the more conspicuous. Aside from the market structure, the other major difference is the fact that not all participants are profit-driven.

FOCUS **T**he fact that some liquidity providers are slower in their pricing than others creates anomalies that opportunistic traders can seize on. Inefficiency lies at the very root of any arbitrage strategies. But over time these inefficiencies have been ironed out as technology becomes more ubiquitous, regulation seeks to restore order and market structure looks for stability.

So how has the high frequency trading world adapted? Are the opportunities of the last five to ten years rapidly fading, never to be seen again or will new



“Central banks that set interest rates can intervene in the FX market in a way that does not happen in other asset classes and is not based on profit. You also have participants, particularly corporates, that are trading in the FX market because they have to for operational reasons, not because they are seeking to make money,” says van Kleef. “For high frequency trading firms this does create more arbitrage opportunities than would be the case in other asset classes.”

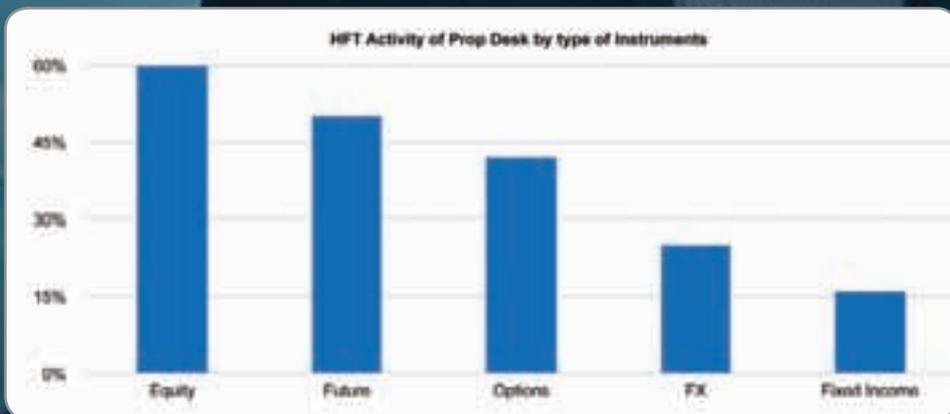
Technology issues

There are two predominant, long-term technology issues in the high frequency trading world. One is the classic dilemma of buy or build, the other is need for low latency. High frequency traders are increasingly

using some element of off-the shelf technology these days, says van Kleef. “The technology has become more accessible and because more people are using it, the price has reduced markedly. It is not like it was 20 years ago when firms had to develop their own technology.”

The pursuit of low latency has become less pronounced in other asset classes – particularly equities – where many firms feel they are reaching the point of diminishing returns and where they could end up spending hundreds of thousands in order to be first to a trade that will only make them thousands. In the FX market, however, latency will likely remain an issue for some time because of the different latency levels of various price providers, says van Kleef.

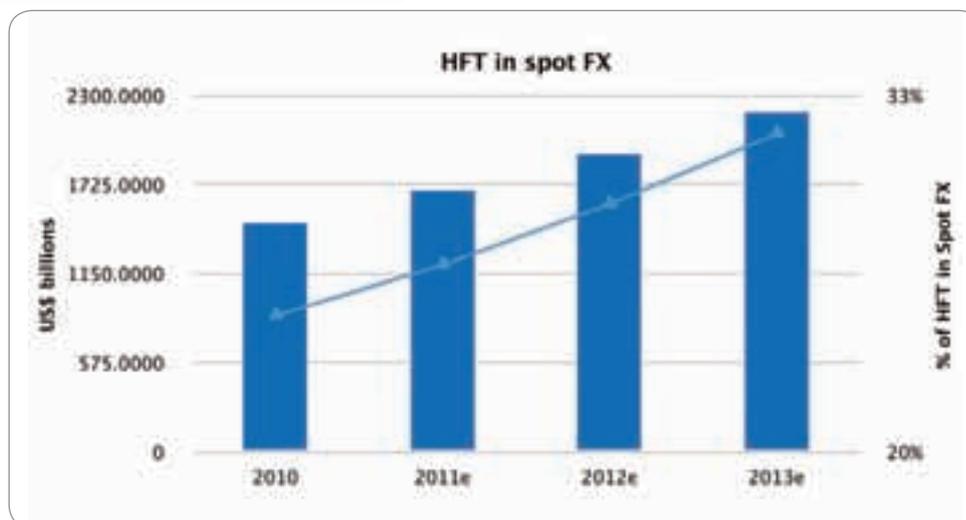
“There is a differential there that does not exist on other asset classes so speed is very important. The price providers can be taken advantage of by price takers with the right technology and this is a big arbitrage opportunity for HFTs. Price providers have to constantly look at their technology and their latency levels, otherwise they will not be around for long.”



HFT by asset classes

Source: WFE, HFR, Exchanges, Celent estimates

■ Spot FX ▲ % of HFT in Spot FX



HFT growth in Spot FX – Celent estimates
Source: WFE, HFR, Exchanges, Celent estimates

The determined pursuit of low latency also tallies with the competitive element behind many HFTs strategies and in the past many of them may have considered that the use of off-the-shelf technology would dilute their proposition. This is also changing, says van Kleef. “Some of the strategies are latency-driven but many others are more down to tactics and strategy in which case it makes sense to outsource. If the strategy is all down to speed, that is not very sustainable because it takes a lot of money to keep on being the fastest.”

“It is possible for HFTs to rent everything now in terms of their set-up and to be in a position where they only have to concentrate on their strategy,” says van Kleef. “So rather than trying to build everything from scratch, we are seeing more HFTs use somebody else for outsourcing.”

The embracing of the outsourcing model is not something that comes easily to many HFTs, given the highly secretive nature of their strategies but van Kleef says this reticence to employ third parties is fading. “When you use a bank to store your valuable jewellery, you don’t expect it to open the safety deposit box and it is the same with the trading strategies, even though the bank has all the information on who you are trading with and when. HFTs are becoming more comfortable with the idea of outsourcing. Some are still paranoid but there is a cost involved to doing things on your own and many are now considering just how much they are willing to pay for their paranoia.”

So where will the FX industry focus on next when it comes to technology? In terms of the technology that it has to focus on now, van Kleef says that an

increasing awareness of machine readable news is apparent in FX, more so perhaps than in other asset classes given the importance of ‘events’, such as central bank announcements, in terms of volatility in the FX market. There is also likely to be greater attention to hardware rather than software as FX traders look to sharpen their set-up.

There is also likely to be an increased focus from high frequency trading

boutiques on the treatment of the reams of data that form the basis of any statistical arbitrage strategy. There are so many different market places all with different data that the storage and processing of this data can become very expensive without widespread data standards, says van Kleef. “Protocols like FIX Fast are becoming more widely adopted and generally the industry is becoming more standardised. There is a realisation that anything proprietary is not really helpful.”

Cost and opportunity

According to Erik Lehtis, president of high frequency FX trading firm DFX Consulting, the dynamics in the high frequency trading market are primarily driven by cost and opportunity and a number of developments in the FX market are conspiring to both increase the cost of competing in the traditional cash-futures arbitrage market and to reduce the number of opportunities. For example, the fact that liquidity is migrating from the multi-participant wholesale ECNs such as EBS and Reuters toward the single-bank platforms, has reduced the effectiveness of their algos due to lower market penetration.

This was not always the case, says Lehtis. In fact the opposite was true in that it was the poor quality of banks’ single-platform, marketing making ventures that created so much opportunity for high frequency traders in FX. “Banks original efforts at market making ranged between pathetic and disastrous. High frequency traders would pick them off and continue to make money at their expense until they were eventually turned off by the banks because they considered them toxic.”

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After a period of being continually arbitrated and tiring of defending their platforms from 'toxic' predators, a number of banks left the single platform business and never went back, preferring to seek safety in the multi-participant platforms such as EBS and Reuters. Some banks, however, decided to address the issue and to build better platforms that could not be so easily gamed, says Lehtis.

"Banks also decided that they would prefer to internalise their flow rather than use a multi-bank platform or exchange such as EBS and Reuters because it is cheaper in terms of transaction fees and makes it easier to hide their hand. And banks still get the last look on every transaction so provided that they are fast enough, they should be able to prevent any toxic flow."

The increase in the market's efficiency necessarily reduces the arbitrage opportunities for the high frequency traders that seek out anomalies. These opportunities are becoming rarer, not least because the market is becoming more efficient, banks are becoming better at internalising their own flow and aggregated trades create fewer anomalies. The easy money-making opportunities that existed many years

ago by exploiting the opportunities by the limitations of EBS and Reuters are no longer there.

Cost is also increasing for high frequency traders in a number of ways such as the price of dark fibre. For example, dark fibre provider Spread Networks released a new, ultra low latency dark fibre route between New York and Chicago that raises the stakes once again for those traders that consider low latency and high speed execution a vital part of their strategy. For some HFTs the only way to compete is to continue to be faster, however this can become an expensive pursuit.

"As we all know, the low latency game is a perpetual arms race with no finish line, so the cost of playing the game is not even a constant but rather a steadily increasing function. Only firms that can leverage their infrastructure across asset classes and play the game at the highest level will have long-term success. I don't think it has reached the point where people are spending thousands to make hundreds. For those firms that have already been successful, the extra investment in staying fast is a way to maintain cash flow. But it is a significant barrier to entry for any newcomer. Unless you have a significant edge in terms of a trading idea or some kind of intellectual property, it is too much of a risk to try to simply be faster," says Lehtis.

Spend wisely work smart

There is an increasing realisation among high frequency traders that it takes more than spending truckloads to be successful, says Lehtis. "You also have to spend wisely and work smart. The firms that have real intellectual property and make that the foundation of their efforts will be rewarded. There are still lots of opportunity in the market for people that understand the evolving landscape and develop a plan to attack it."

However, Lehtis believes there are new types of opportunities for these participants. "For the high frequency traders there will be an opportunity to operate in the space between the single bank platforms and the multi-bank exchanges like EBS and Reuters and act as a market maker of sorts." This will involve some risk for the high frequency traders, as is the case for any market maker, not least that some of the flow they get will come from other high frequency traders that are rejected by the banks. Trades between two similar types of participants rarely work out well for both, particularly when they are both high frequency traders, so this is something that a potential market maker will have to bear in mind.

In some ways such a model would be a return to the roots of high frequency trading, says Lehtis. "High



Peter van Kleef

"If the strategy is all down to speed, that is not very sustainable because it takes a lot of money to keep on being the fastest."

frequency traders have a reputation for being toxic but essentially it is a style of trading that looks for liquidity and acts as the intermediary between two disparate markets. It is often a very small edge and there is a risk involved in showing your hand but if you can be quicker than your two counterparties, the only risk you are taking is in the quality of your hedge.”

Relationships

When high frequency trading first emerged in the FX market, it did create a new dynamic in terms of the relationship between participants. This change became more acute with the arrival into the market of high frequency traders from other asset classes, such as equities, that were not wholly aware of the traditional relationships that had stood for so long in FX.

“FX has always been a relationship business. There was a highly effective system of self-regulation where if you screwed someone once, you would not be able to do it again. But this changed a lot in the 1990s when the business became more electronic, EBS and Reuters dominated and the interbank market consolidated, leaving the smaller players unhappy with how they were treated by the bigger banks with too much volume,” says Lehtis.

There is an opportunity for this all to be addressed now, says Lehtis. “If banks can learn to treat high frequency traders as another type of client – with different needs and expectations to corporate customers but with an equal importance – and if high frequency traders can learn more about the FX market and how it works (and not treat it as another market in which they can aggressively target the participants, burn them and move on), then there can

be a bright future. But banks will have to learn what exactly it is that high frequency traders are looking for and be able to provide it.”

In order to meet this challenge, technology will be key. As time has gone by, technology has become more granular. Co-location now has a completely different meaning. People are working in micro-seconds but there is still value in chasing it all down. New technology is always being developed such as Field Programmable Gate Array (FPGA), which enables the development of specialist hardware and design of high performance logic that by passes the operating systems and protocols that inhibit computers and slows down the execution time of carefully designed algorithms. “No-one knew what FPGA was but now it is the new emerging technology of choice. And there will be similar technology discoveries that will drive the markets of tomorrow and create huge opportunities for the people that discover them,” says Lehtis.

Impact of regulation

Regulation can generally be relied on to cause some disquiet for market participants and particularly for high frequency traders who are more sensitive than most to any changes to market structure created by legislation. Furthermore, high frequency traders have emerged as a target for many rule makers, regardless of whether this targeting is warranted.

There are particular efforts to focus on counterparty risk as seen in the legislation of the futures market in





Erik Lehits

“High frequency traders have a reputation for being toxic but essentially it is a style of trading that looks for liquidity and acts as the intermediary between two disparate markets.”

the US and the effort to bring more central clearing into securities markets. One of the trading risks that emerged in the wake of the Lehman Brothers collapse in 2008 was the confusion over the ownership of underlying assets and it is hoped that central clearing will help to counteract this by instilling more transparency and control into trading.

The FX market though is an over-the-counter market on a global scale and is therefore unlikely to be subjected to the introduction of central counterparties. As a consequence, one of the indirect impacts of regulation will be that several more high frequency traders operating in equities or other similar asset classes, may look to work more in the FX market.

“An increasing number of large banks are opening up FX dealing desks and offering an FX broker/dealer service to sole traders, hedge funds and even retail traders,” says Victor Lebreton, who manages the strategies and the electronic trading platform for the prop-trading company Quant Hedge. “This is a big change for the FX market in that it is bringing in a number of new participants that previously only saw the FX market as a cash management function rather than as an asset

class in its own right. And of course some of these new entrants, particularly those on the hedge fund side, are looking to trade FX on a high frequency basis.”

Strategies

As other exponents of the art have noted, it is becoming tougher to successfully do high frequency trading in FX, says Lebreton. “One opportunity in the past has been to look for price arbitrage – euro-yen then yen-dollar and trade on any price discrepancies that emerge but this strategy appears to be working less and less as the market becomes more efficient and pricing anomalies become rarer. Prices are being transmitted at a faster rate and on a more correlated basis. Consequently more high frequency trading firms are pursuing longer-term liquidity-based strategies that employ slicing and dicing algorithms and rules-based execution based on time correlations and in-depth statistical analysis.”

The type of strategy a firm pursues is the biggest influence on the technology it employs, says Lebreton. For example, a firm focusing on statistical arbitrage will have to invest in effective data management systems able to store, cleanse and process large amounts of data. Whereas execution-matching strategies will need to establish a strong rules-based execution engine that matches its very specific trading limits and targets – something that often requires very specific software and infrastructure.

Furthermore, the growing tendency for FX high frequency traders to employ a number of strategies means that they are unlikely to find one system that meets all of their strategic needs. “These strategies are based on precision and cannot afford to be compromised so a firm may employ a number of different software systems. Many of these may be developed in-house although in-house development is still mostly a path open only to the larger firms able to afford the big team of IT developers needed to fix any problems that arise and to devise new codes.”

For those firms that are not blessed with those kind of resources, the world of off-the-shelf software is becoming more attractive and it is possible to configure off-the-shelf software to create a credible trading platform for relatively straight-forward high frequency strategies such as spread betting or trading between two baskets. There is also a scarcity of quality help on the development side given that there is an increased enforcement of non-compete agreements allied to a proliferation of high frequency trading firms entering the market. Consequently this means that the

demand for developers far outweighs the supply.

Pace of change

According to Sean O'Donnell, director of technology at trading technology provider First Derivatives, the biggest issue facing high frequency trading in general is the pace of change - from technology innovations (networks, hardware, software etc) though to evolutions in algorithmic models and changing strategies. However, in the FX arena it is the rapid explosion of firms now trading as high frequency traders that is the biggest issue. "They are employing highly active and aggressive trading strategies, says O'Donnell. "It is one firm trading against one another."

Unlike the equity space where HFT has been established for many years this is a new addition to FX that has accelerated in the post-financial crisis era due to the fact that there is more volatility to be found in the FX market than in the relatively flat equities world of recent years. "High frequency traders like volatility and arbitrage opportunities and they see those in FX," says O'Donnell. Part of the reason for the arbitrage opportunities is structural. Foreign exchange is an OTC market with a matrix of connections and relationships with a huge amount of price discrepancy. There is also still a discrepancy in the technology that some participants are using. Despite the overall improvements in the market's development of and use

"..more high frequency trading firms are pursuing longer-term liquidity-based strategies that employ slicing and dicing algorithms and rules-based execution based on time correlations and in-depth statistical analysis."



Victor Lebreton

of technology, some of the platforms used by liquidity providing banks are still too slow and they can 'gamed' by high frequency traders.

Buy or build

For high frequency trading firms, technology choices are critical to all aspects of its infrastructure – from trading platforms to execution algorithms to system architecture. One of the decisions a high frequency trading firm has to make in this regard is whether to buy or build. According to O'Donnell, there are five key considerations that will influence the decision to buy or build. The first of these is performance and reliability. "A well tested third party algo trading platform that is running large scale models 24/7 is of lower risk than an initial home grown solution."

The second consideration is flexibility and configurability. Typically this is where high frequency trading firms feel they can add value by changing strategies rapidly so the flexibility of a solution is critical to achieving this agility, says O'Donnell. "This is why, when it comes to the development of our own products, we have focused heavily with the Delta platform on API access, configuration driven changes etc to ensure that high frequency trading firms get the best of both worlds."

Depth of connectivity is a third consideration. "Providing bidirectional connectivity for quotes and orders is important to high frequency trading firms. But building adaptors to ensure this connectivity can be an arduous and error prone process so typically this is where most high frequency trading firms would look to buy rather than build."

Another consideration that is tipping the balance in favour of both versus build is the speed to market, says O'Donnell. "This is definitely a major factor where new or existing high frequency trading firms are looking to leverage the investment of an off-the-shelf platform rather than the slower build out approach." It is not always a simple binary choice between buy and build though. A newer development has been the emergence of a buy and build approach that focuses on buying a platform that can be extended out based on the specific requirements of a high frequency trading firm as relates to core components, exchange connectivity, a strategy engine and back testing.

The use of new technology solutions to speed their time to market is an important change for many high frequency traders and an interesting development for technology providers, says O'Donnell. "Up until a

few years ago the concentration of effort was getting the software correct and once deployed it typically stayed in production for a number of months if not years. Now with market forces demanding constant change, the software development lifecycle has become very agile and changes that were planned in months are now implemented in hours and days. To achieve this you need a platform that is built from the ground up with this in mind. Adding new venues, new data streams and changing strategies can be achieved through smart configuration and hot deployment rather than through code changes.”

Latency and speed of execution

Another influence in the technology approach of high frequency trading firms is the pursuit of low latency. This influence may be waning in some asset classes where there is only so much more than can be achieved in terms of reducing latency but it is a pursuit that still has some mileage left in the FX market, says O'Donnell. “In some other markets, low latency can be a futile pursuit – it is just one API against another but in FX there is still a long way to go



Sean O'Donnell

“High frequency traders have to analyse every level of their technology stack, from co-location of data centres to their market data providers, networking technology and routing algorithms, hardware and operating system profiling – all levels need to be considered.”

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- FX Derivatives Development
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- Difficult RMB Market Construction

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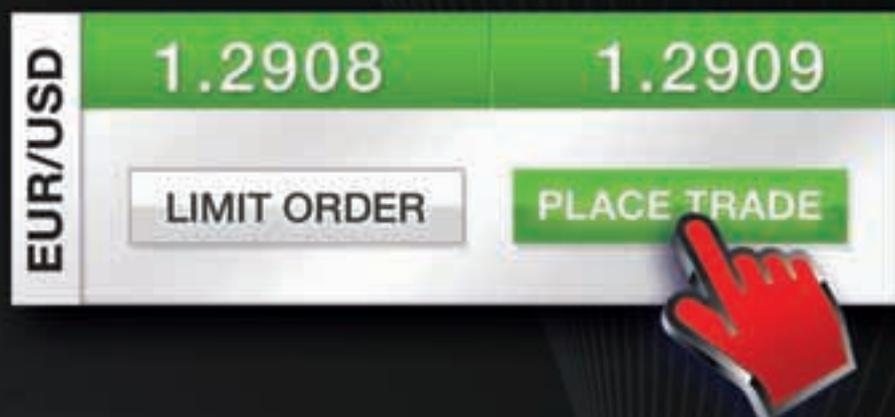
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before we reach that point.” Therefore it is important that high frequency trading firms consider the various ways that even lower latency can be achieved and the levels of market data connectivity can be increased.

“High frequency traders have to analyse every level of their technology stack, from co-location of data centres to their market data providers, networking technology and routing algorithms, hardware and operating system profiling – all levels need to be considered. Also, once market data is captured from the operating level, how it is handled and managed from their algo platform software is critical. This is where some of the biggest areas of reductions of latency can be achieved. Message marshalling, serialisation/de-serialisation of messages and the choice of internal message formats are all crucial decisions that need to be made because they all contribute to the ability to increase the number of market data feeds possible”

High frequency traders also have to consider options aside from removing latency that can increase the speed of their executions, such as where their strategy

engine is situated and the use of various co-location services. “There are firms such as ourselves who can host their liquidity/strategy engine and provide co-location services with the major liquidity providers,” says O’Donnell. “This type of service allows the high frequency trading firm to concentrate on their core business, such as defining ways to trade and managing their risk more efficiently, whilst the service firm manages the core infrastructure”

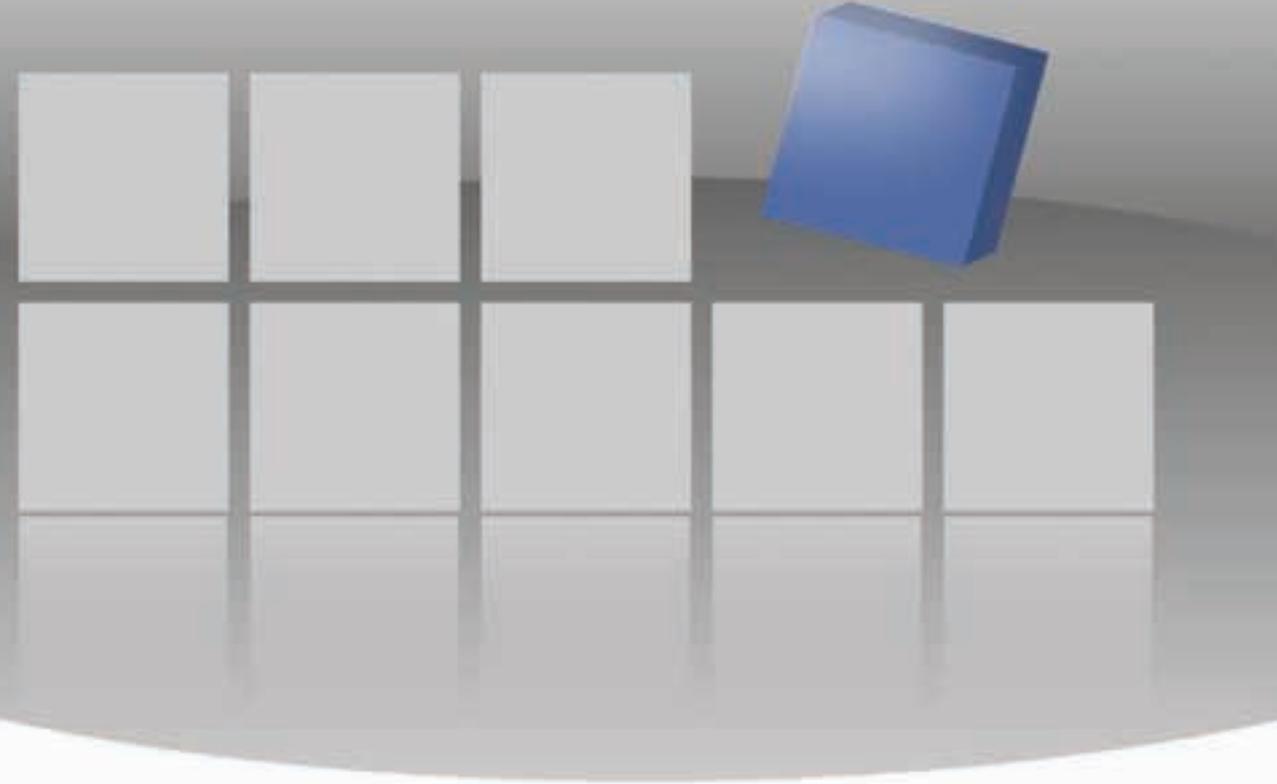
The treatment of data has become a more important consideration for high frequency trading firms of late and many are now looking at what underlying technologies can assist them in their efforts to process, clean and store data more effectively, says O’Donnell. “Having solid data that high frequency trading firms can build their algorithms on and back-test against is mandatory and without it they are lost. There are three things in particular that they should be looking at - high speed processing off the wire; rapid algorithms that cleanse the data on the fly based on dynamic rules; and high volume in memory storage.”



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White Label partnerships: Taking the quick route to establishing an online FX business



Heather McLean

Whether dealing with retail individuals or institutional firms, building an FX system in-house can involve prohibitive costs and long time delays. The alternative is a white labelled solution from a third party provider. Heather McLean, examines how white label solutions can expedite entry into the burgeoning and lucrative FX market.

The retail FX industry has grown nearly tenfold in the past decade, and in 2010 was estimated to be at \$315 billion in average daily turnover. In addition, annual revenue of the retail FX brokerage industry is estimated to be at nearly \$10 billion, according to Aite Group. These provide compelling reasons for financial services and brokerage firms to enter this fast growing and lucrative market.

Deciding factors

Tom Levine, senior vice president for institutional sales at GAIN Capital, says “When considering any kind of strategic partnership, and in particular an FX white label partner, a firm needs to consider the fundamentals associated with both client facing and back office features”. He notes: “Institutions should ask themselves questions like: Does this firm have a good reputation in the market? Is the firm going to provide a reliable and scalable service? How deep is this company’s expertise and how will they be able to help me post product launch?”

Luis Sanchez white label specialist at Dukascopy Bank, notes: “A white label solution can help

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a broker or bank to quickly offer comprehensive FX trading services to its clients, and thus generate additional growth and revenues for the broker. White labelling offers an opportunity to start a business from zero to up and running in one to two months, while designing a solution in-house could be expensive, and takes years to implement.”

While Hayel Abu Hamdan, Chief Operating Officer at Hantec Markets, says that for ways in which white label programmes can help trading firms to grow their market share and take advantage of new regional business growth opportunities, using an FX white label software as a service (SaaS) solution is the answer. “SaaS, whereby solutions and services are delivered on demand, provides partners with the opportunity to enter new markets quickly without having to own and operate any IT infrastructure. There is no system software to install, no migrations to plan, nothing. It’s very easy and effective,” he maintains.

Levine observes, “White labelling is advantageous for firms looking to grow market share and footprint. It can be an especially attractive opportunity for those firms that have a strong local or regional presence and want to take advantage of the growth in the retail forex industry. These firms should look at FX as an opportunity to cross-sell into their installed client base, as well as a way to gain market share by using their existing presence, marketing, regulatory licenses and reputation.”

“With respect to reputation and corporate stability, make sure the company being considered has solid financials, detailed risk management policies and procedures, strong corporate governance, a solid grasp on regulatory and compliance issues and the ability to provide partner references,” Levine warns.

He continues: “Service reliability will be instrumental in delivering an exceptional customer experience. Be sure the firms being evaluated can provide detailed statistics regarding system uptime, order execution rates and speed, and opportunities for price improvement. Also, an institution will want to be sure that the white label solution provider’s technology, service and business can scale as their business grows with them and that they have a proven track record building successful white label partnerships. Lastly, the provider should be able to provide detailed information about their disaster recovery and business continuity plans.”

In addition to reputation, reliability and scalability, Levine recommends looking for a company that has deep familiarity with the inner workings of online retail FX trading. He says “institutions will often rely on brokers to provide best practices pre- and post-launch. Their technology should be well tested, and the company should be at the forefront of product and service innovation, because once an offering goes live, it should continuously evolve and improve”, Levine states.

On the deciding factors for choosing a white label partner, Jørgen Hauglund, senior vice president and head of institutional business at Saxo Bank, agrees a lot of areas must be taken into consideration. “First of all, the basic requirement is of course that the provider is able to offer a trading solution with the functionalities and qualities that are needed to support the current business needs of the bank or broker. Secondly, the bank or broker must carefully evaluate whether the white label provider has the resources, skills, willingness and technologies to support the development of the business going forward.”

Hauglund continues: “To enter into a white label relationship is an important strategic decision. The provider must not only be able to support the current business of the bank and broker but should also be able to support, guide and then lead the development of the bank or broker’s online trading business in the future”.

“A good white label provider should be able to continuously present new business opportunities to the bank or broker, rather than locking the bank into an inflexible solution that may satisfy today’s needs, but not tomorrow’s. That is exactly what we



Luis Sanchez

“White labelling offers an opportunity to start a business from zero to up and running in one to two months.”

Artur Filipowicz

“Operational risk (IT risk) and Market risk are things to consider carefully.”

aim to achieve with our trading solutions for banks and brokers; to enable them to take advantage of new business opportunities and helping them remain competitive in times of fast changes in technology and markets,” he adds.

“Contrary to many other white label providers, we are able to provide a multi-asset platform,” remarks Hauglund. “This enables the same platform to support the trading needs of the bank’s or broker’s customers if and when the bank or broker decides to add more products to the offering. According to many of Saxo Bank’s white label clients, this multi-asset capability of the platform is one of the most important qualities of the offering.”

Tick list

Hamdan says choosing a white label partner should be a process of answering many questions, including: How solid and reputable is the white label provider?

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Where are they positioned in the market? Who is their offering targeted at (retail or institutional)? Is this in line with your target audience? (It would be disastrous to choose a white label solution that is not catered towards your target audience.) Who are their clients? Can you compete in that space? What will be your value proposition if several other major competitors are using the same white label solution? Is the white label solution scalable? What future upgrades or new features are in the pipeline, and what is the provider's roll out map? What are the costs involved? and What is the set up timeframe?

The choice of white label provider solution should be made based on a few important factors; the technology itself, its recognition, stability and the time frame of the implementation are of course all significant, says

“To enter into a white label relationship is an important strategic decision. The provider must not only be able to support the current business of the bank and broker but should also be able to support, guide and then lead the development of the bank or broker's online trading business in the future”.

Artur Filipowicz, relationship manager and white label specialist at Dukascopy Bank. He adds that the setup and maintenance costs also represent key factors.

Another important factor is the risk, notes Filipowicz. He explains: “Operational risk (IT risk) and Market risk are things to consider carefully. The Operational risk is difficult to quantify. Nevertheless, one should determine what the security and stability level behind the service is, such as what the backup servers or redundancy lines are like. In regard to Market risk it is essential to identify how the hedging works, at what price and liquidity the execution takes place and whether the hedging executes automatically. Last but not least is the flexibility of the technology. What revenue model can be implemented such as commission based or markup? What level of customisation does the partner get access to?”

Core services

On core services necessary for a successful white label relationship, Levine says working with a firm that has a deep level of FX expertise will ensure that the financial institution is well supported during all phases of the white label relationship. “In most cases,



Jørgen Hauglund



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FX is not the expertise of the institution and they will want to work with a company that can offer a turnkey white label solution that will include client services, marketing support, compliance, and dedicated development resources to build a customised trading platform and offering.”

“One of the options that GAIN provides its’ partners is the choice to outsource customer service in its entirety or in part”, says Levine. He adds that this allows partners to enter the market faster by saving many man-hours on training, testing and certification of support staff. “At a minimum, clients should be able to access live support 24 hours a day during FX market hours through phone, email and chat. If a firm is not prepared to do so, then their white label provider should be able to seamlessly step in and assist,” states Levine.

“Alternatively, should the firm choose to take on sales and support functions directly, the white label provider should have the facility to provide client service and industry training to get representatives up to speed as quickly as possible,” he adds.

“White label providers should supply a 24/7 support service”, says Hamdan. “Training programmes are also provided to partners to insure they are fully aware of the functionalities and features of the software. These, as well as a complete set of marketing literature, help with a smooth efficient client on-boarding process, as well as an enriching end user trading experience.”

On technical support, Hauglund says as part of the integrated front-to-back white label set up, Saxo Bank runs a number of operational services on behalf of its white label clients. The services are integrated into the trading applications and end-of-day files and can be extracted for further use into the white label client’s own back office system to support regulatory or management reporting.

All the back office processing at Saxo Bank is done using anonymous customer identities, ensuring the bank has no record of the white label client’s customer contact details. The back office system supports the following operations; end-of-day processing; account interest; FX rollovers; set up of asset classes; commission charges; corporate actions; market data services; transfer of securities free of payment; risk management; and margin handling.

Marketing support

Levine adds that pre and post launch marketing support is essential. The partner should have all the tools and resources to either create or help build a website that will attract, convert and capture customers on day one. This includes providing educational materials in the form of video tutorials, webinars, and reference guides. The white label partner should also provide marketing consultation services to provide insight on how to best spend marketing dollars.

Continuing, Levine notes: “As a core requirement, a dedicated development team will be critical to getting

a trading platform live as soon as possible and bug free. The technology itself should be able to support multiple languages and currencies with custom account settings including adjustable leverage, spreads, maintenance margin, and liquidation levels.”

Part of the criteria for a successful white label solution is that the customisation is done as quick and smoothly as possible, says Hauglund. He says Saxo Bank’s trading platforms and the majority of its supporting tools are developed in-house, based on internal expertise and because of this they are easy to customise, he states. “The individual needs of the white label client can therefore effortlessly be incorporated, resulting in improved responsiveness and easier integration into the white label’s current system.”



Tom Levine

“White labelling can be an especially attractive opportunity for those firms that have a strong local or regional presence and want to take advantage of the growth in the retail forex industry”.

Timelines

With respect to timeframes that are typically involved in getting a white label partnership programme set up and the FX trading business running, Hamdan believes the typical set up time is about four weeks, although he adds this obviously depends on the complexity of the selected solution and how efficient the provider’s after sales support is.

Hamdan continues: “This would be followed by three to four weeks of stress testing to insure all the data feeds, liquidity bridges, back office integration, and latency issues, if any, are resolved. There is absolutely no advantage in cutting corners to go live as technical issues will come back to haunt you,” he warns. “And if you are trying to break into the market with an offering that does not offer the client an uninterrupted trading experience, you will not last very long in this competitive market space.”

While Hauglund remarks: “We have implemented more than 100 white label solutions with banks and brokers of all sizes in many countries. Because of that we have gained a lot of expertise in white label implementation. This means that the banks and brokers can expect a fast and efficient on-boarding process, handled by specialist staff with extensive experience. As a result, Saxo Bank can often implement a fully branded and customised white label trading solution with a bank or broker in only one month, although typically it will take longer due to decision making processes and commercial preparations prior to launch, and other factors.”

Under the hood

On what key features and functionality partners should look for in scalable integrated trading platforms from white label firms, for both retail and institutional FX markets, Sanchez notes: “The most important feature of any platform is its individuality and flexibility. Any bank or brokerage house client has different needs and the platform should be able to offer or propose a concrete solution for any client base. Platforms should provide manual and automatic trading, chart trading, and offer historical back testing using real data, with an intuitive interface.”

On revenue share models, Hauglund says: “For us, the most important aspect of the commercial model is to ensure that the model makes economic sense for both parties. It has also to create a strong incentive for the



Hayel Abu Hamdan

“If you are trying to break into the market with an offering that does not offer the client an uninterrupted trading experience, you will not last very long in this competitive market space.”

bank or broker to expand the business, by providing a quality service to their underlying customers. This is achieved in many ways and we are always interested in discussing revenue sharing models that suits the strategy of our white label clients.”

“Today, Saxo Bank’s white label business is a major part of our overall business,” continues Hauglund. “We launched our first white label solution in 2001 with a visionary Portuguese securities dealer with 150 years of market experience. I think the reason our white label business became so successful is that many financial institutions, not least since the financial crisis, have realised that it doesn’t make sense to use a lot of money and try to build your own trading

platform when you can get a top notch white label solution.”

Revenue sharing and channel partnerships

Filipowicz says popular revenue sharing models in white label partnerships include volume commission revenue models, since they are transparent towards clients. “With Dukascopy Bank’s white label solution, the partner has the freedom to set up any commission level he wants, while Dukascopy Bank charges only \$3 per million USD traded. Some other white label solution providers may charge for the white label set up cost, plus a monthly or yearly maintenance fee, which nowadays is less popular.”

The most commonly used revenue sharing programme is a rebate programme where white label partners are rebated a certain percentage of a pip, states Hamdan. Other models rebate a percentage of the commission charged. “There are however certain brokers who do not adopt a straight through processing model and instead generate their income from managing their exposure and risk and who would consider sharing their revenue with their white label partner,” he says.

At GAIN Capital, channel partnerships represent a significant part of the business and are an important component of its long term growth strategy. In 2010, over 40% of GAIN’s retail trading volume came from its indirect channel partners, including white labels, said Levine. “We work with a wide variety of partners, most of whom are using a strong regional presence and a loyal client base, including Zecco Forex in the US, Standard Bank of South Africa and Questrade in Canada. With such a diverse sampling of partners, we recognise the fact that not all partnerships are built the same way, and will tailor a partnership to meet the needs of our partners’ specific business and technical requirements.”

Conclusion

Hauglund sums up: “The single most important criterion for selecting a white label provider is whether there is a good match between the two organisations in terms of culture, values and strategy. We are proud of the fact that some of the largest banks in the world have chosen to work with us in developing their online trading businesses. Given the extensive due diligence and quality requirements demanded by such banks, we feel that these relationships serve as documentation of the quality of white label solutions offered by firms like ours.”

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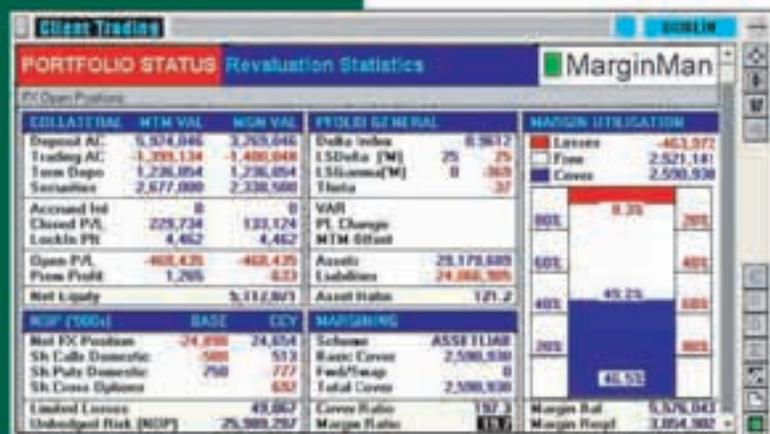
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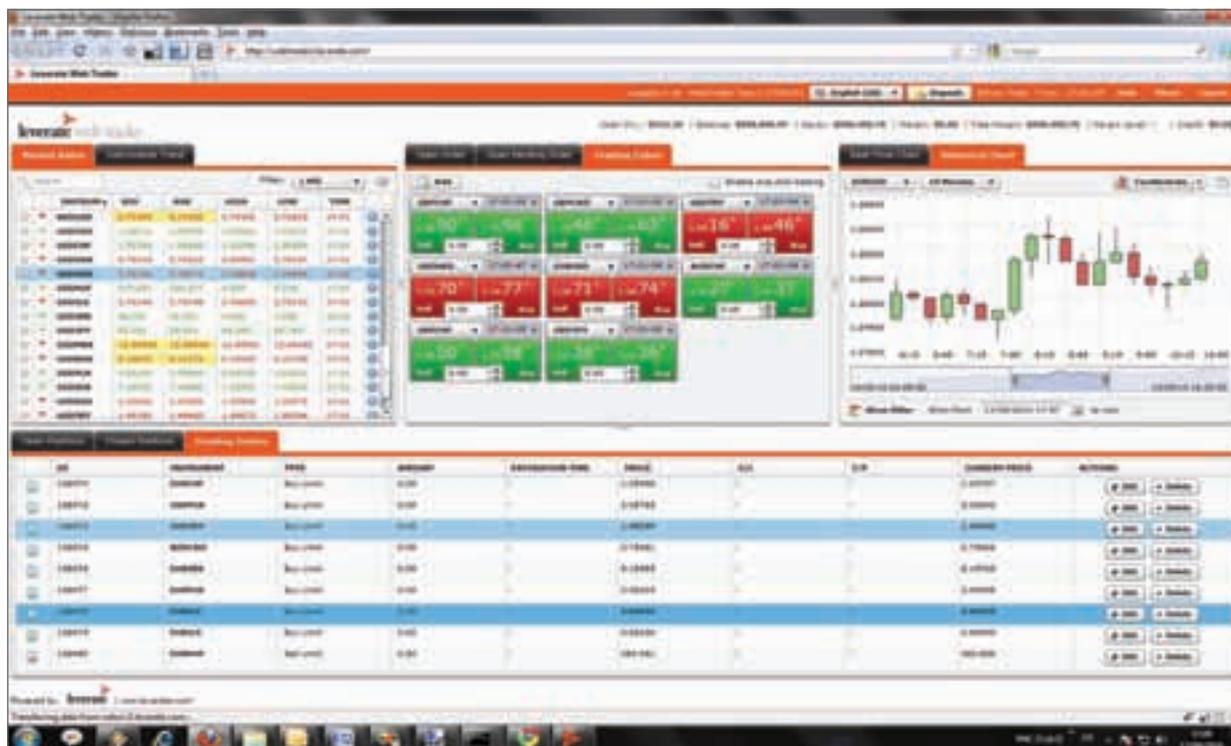
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from arbitragers and errors. Brokers can increase their trading volumes while lowering their risk without losing high-volume clients by hedging via “Instant” and “Market” execution. The Private Label Solution can support trading by robots, experts and scalpers.

Training and Support:

Leverate’s knowledgeable training and support staff are Forex experts with years of experience in the industry. New brokers are provided with a 4-day intensive training session to explain, in detail, the systems functions, configuration, and overall guidance on the best practices for operating the brokerage. Clients also have access to Leverage’s 24/6 support center. Leverage’s professional Support Team monitors clients’ systems on an ongoing basis and provides general and technical support to help brokers address the challenges facing their businesses.

Binary Options:

Through strategic partnerships, Leverage is able to offer a Binary Options trading platform fully integrated with the MT4. Binary Options has become increasingly popular among traders, and Leverage has responded to the demands of the market by offering brokers this platform for their brokerages. The platform is completely customizable and web-based. With a shared wallet, traders can log in with their same username and password as they use to access the MT4. This platform allows brokers to increase their market share while strengthening their competitive edge over other brokers in the market.

Building Blocks for opening a brokerage:

New brokers need look no further than Leverage for all the services necessary to start a Forex business. Leverage offers brokers company incorporation services and all necessary components to start their Forex brokerage operation. Additionally, Leverage assists with developing brokerage websites, which are automatically integrated with Leverage’s solutions. Furthermore, brokers receive a Partners website, an imperative asset when launching affiliate marketing campaigns. Leverage also assists brokers to connect with trustworthy payment service providers (PSPs), offering a variety of international payment methods and currencies, enabling traders to deposit, effortlessly.

For a marketing advantage, brokers can request a fully branded Forex tutorial video for their website, leading to an increase in leads, as new traders feel more comfortable with a brokerage offering the information provided in the tutorial. Additionally, traders of all experience levels benefit from the real-time Market News Feed offered by Private Label brokers. The Market News Feed leads to an increase in trading activity, as it involves traders in the movement of the market and provides them with the up-to-date information they need to trade wisely and actively.

Leverate is the premium broker solutions provider offering a turnkey package for Forex brokers to open their independent brokerages. Dozens of the world’s leading brokers rely on Leverage’s innovative solutions, and the Private Label enables brokers to open their brokerages quickly and economically, and is excellent for those opening a new brokerage and for existing brokers looking to replace or enhance their existing platforms.

About Leverage

Leverate is dedicated to delivering innovative services that enable Forex brokers and financial institutions to increase conversion, minimize risk and reach new markets. Leverage offers cutting-edge solutions powered by breakthrough technology, providing an end-to-end suite of products to open and operate the most successful and competitive brokerages in the Forex industry.

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No sweat: Overcoming the challenges of transitioning to MT5

The new MetaTrader 5 (MT5) platform has been developed by MetaQuotes Software to provide brokerage services for customers operating in the Forex, CFD, Futures, as well as Equity markets. Heather McLean examines the challenges faced by firms implementing the new platform and the benefits MT5 offers them in the competitive FX as well as in equity markets.

MetaQuotes states that the MetaTrader 5 Platform provides a true multi-asset trading experience to traders, by allowing them to execute transactions in retail FX and Equity markets from the same MT5 trading account. MT5 is more versatile than its predecessor, MetaTrader 4 (MT4) in terms of

additional functionality and is flexible and adaptable to any business model that a broker wishes to pursue. Considerable resources and tools have also been introduced to ensure that mapping and transferring operating settings from MT4 to MT5 can be performed with minimal effort, the company claims.

Installation

MT5 has some new and exciting features for routing control, execution handling, and multiple asset class trading. Andrew Ralich, co-founder and CEO at oneZero Financial Systems, says he suspects many brokers will look to utilise this enhanced configurability and manage risk internal to the MT5 platform through a combination of manual dealing, trade gateways and exchange connectivity. “MetaQuotes has advanced the MT5 Platform to address some of the specific challenges seen in MT4”, says Ralich. “By changing to a



clustered server model, MT5 enables brokers to scale much more easily across one single instance of their back office, history centre, web server, and more,” he notes. “This means increased flexibility as a broker grows, but necessitates a well planned deployment.”

“Installation time-frames will vary depending on the extent to which brokers look to build out their MT5 initially. oneZero is working with our brokerage clients to meet their needs for MT5 from an IT perspective by providing a highly scalable, virtualised server model hosted across our redundant data centres, and by designing our MT5 bridge technology to scale similarly to how MetaQuotes has designed its trade server build-outs,” says Ralich.

The installation process for MetaTrader 5 is now even simpler than before, MetaQuotes claims. The system can be installed and become ready for operation in one working day, if all hardware resources are already in place. In terms of configuration and other time lines involved, they solely depend on the specific requirements of each broker and their unique operational business models.

Several IT firms are not fully aware of the functionality and opportunity MT5 provides, and for this reason MetaQuotes is acting proactively informing all stakeholders, through publications and soon through webinars. Furthermore, MetaQuotes is in the process of launching a partnership program to monitor such integrations for their stability and quality, for the best interest of MT5 clients. A separate Integration’s department is already being prepared to lead this initiative.

On other key issues facing FX brokerages with respect to the installation and configuration of the new MT5 platform, Maor Lahav, chief operating officer at Panda Trading Systems, says: “It is important to note that brokerages already using MT4 to provide services in FX and CFD’s will have a much easier time with the installation and configuration of MT5, whereas brokerage firms that are interested in using MT5 to offer Futures and Equities will require more work and thus more time. Technically



Maor Lahav

“It is important to note that brokerages already using MT4 to provide services in FX and CFD’s will have a much easier time with the installation and configuration of MT5, whereas brokerage firms that are interested in using MT5 to offer Futures and Equities will require more work and thus more time.”

speaking and if the necessary hardware is in place, the basic implementation should only take a day or so. However, full implementation, including integration to proprietary systems, may take from a week up to couple of months.”

“At Panda, we are often asked how to best integrate a new trading platform whilst having limited effect on existing architecture and the business process as a whole. There is no simple answer that can fit all possible business scenarios; smart architecture design is very important for the success of the integration and can prevent obstacles during the implementation, which may otherwise unnecessarily extend the integration period,” continues Lahav.

Lahav adds that brokers need to be concerned about the stage after the integration as well, making sure they can monitor the system, including server monitoring, network monitoring and system functionality. “To achieve these goals, it is important that brokerages don’t only monitor the server up time, but adopt a monitoring methodology that should allow them to spot issues before they happen. The issue of monitoring is just as important as with MT4. The only question is what level a company requires. Today, at Panda, we have adopted a work method that allows us to identify problems beforehand and pre-emptively stop them from occurring. In addition to the initial integration with existing systems, mid-size brokers and above may require integration into CRM systems, back offices, and more,” he states.

MetaTrader 5 is equipped with several new automation functions and forecasting capabilities to anticipate potential problems that clients may encounter. The prior experience of MetaTrader 4 allows MetaQuotes to be proactive in this manner, proclaiming MetaTrader 5 to be one of the most reliable and efficient trading solutions in the history of online trading development.

More flexible platform

“MetaQuotes has done a good job of creating a stronger and more flexible platform that retains the look and feel of its very popular predecessor platform”, states Stephen Leahy, principal at Capital Markets Access Partners (CMAP). The only concerns are: a) operational knowledge of running the platform (risk management and operations procedures); b) training clients to use the platform; c) any customisation of the platform or associated technologies.”

“CMAP has been training on MT5 since the beta versions became available and our team has a strong grasp of the risk management and operational processes in the new platform. The administrative tools and routing advancements have been run through and documented. We think the largest challenge will be client acceptance, for which a timeline is tough to guess,” Leahy continues. “Brokers can do their best to create training materials for underlying clients, but mass acceptance is a self-fulfilling prophecy; as more people use the platform, the greater the value of using the platform becomes.”

While Matthew Nolan, business intelligence specialist at Boston Technologies, comments: “The news of the release has generated a lot of excitement with retail brokers, but there appears to be a ‘hurry up and wait’ attitude. MetaQuotes has clearly done a great job of marketing and offering discounts to its existing clients.

“The large user base of MT4 suggests MT5 will have great performance with FX, but brokers seem cautious regarding the other asset classes,” warns Nolan. “We know what the platform is capable of, but some questions remain regarding proven connectivity to ECN’s. Installation time-lines should be relative to the set up of MT4. Look for technology companies to lead the way in developing integrations and offering solutions before brokerages begin to fully adopt MT5,” he says.

“Mass acceptance is a self-fulfilling prophecy; as more people use the platform, the greater the value of using the platform becomes.”



Stephen Leahy



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Easy integration

The architecture of MetaTrader 5 has been specially designed to offer brokers more connectivity options. It includes universal connectivity capabilities to allow integration and operation in different markets through multiple liquidity sources. A special purpose back office API allows seamless integration with any liquidity source (FX, DMA, Exchanges etc), while a general purpose API allows brokers to customise the platform further according to unique requirements and to integrate with third party applications.

Alexander Saidullin, head of the trading platforms department at MetaQuotes Software, states: “MT5 offers unique flexibility in terms of integration, allowing brokers to choose the best integration method that fits their needs. They can choose to perform custom integrations internally, contract with a third party development firm for custom integration projects, or can decide to use integration facilities that are provided by our company within the platform, such as the MT5 to MT5 Gateway for coverage or straight through processing (STP).”

The main issue concerning how brokers should address legacy integration issues relating to their existing structure when transitioning to MT5, is whether or not a brokerage has been using a single trading platform or multiple trading platforms, thus the service of any back office system will differ with both, notes Lahav.

“In addition, there is a substantial difference between brokerage companies and their back end systems, in that there is

a high correlation between the complexities of the existing systems to the complexity of the integration,” says Lahav.

Panda offers a Sync Server that enables brokerages to synchronise, in real time, their existing platform with MT5. This essentially allows the MT4 and MT5 platforms to run alongside a broker’s propriety platform, without affecting the business. The broker can focus on multiple clients instead of multiple platforms, states Lahav.

Legacy issues

Addressing legacy integration issues relating to existing dealing and platform architectures when transitioning to MT5, Nolan says as management evaluates the decision of any new project, one must evaluate the added benefits versus costs. “MT4 has a strong adoption in the FX retail market and I believe that will remain for some time.

MT5’s new server design provides a more flexible approach for large brokers to cater to larger client bases efficiently.





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“The news of the release has generated a lot of excitement with retail brokers, but there appears to be a ‘hurry up and wait’ attitude.”

“Additional tools, such as the EA wizard, will help gain client commitment,” he continues. “As brokers evaluate the pro’s and con’s of MT4 and MT5, each must decide if the time, resources, and capital are worth the migration. Expertise in MT5 will be critical to a successful integration. Firms without MT5 specialists should look towards outsourcing this support. A planned approach for testing, beta customers, and group migrations should lead to a successful transition.”

MetaQuotes’ Deputy CEO Gaies Chreis believes MetaTrader 5 represents a natural progression of the online trading industry. Similar to the success of MT4 and the way it affected the retail FX market, MT5 represents the solution to the ever-changing needs of financial markets in terms of trading capacity, power in operation, speed of execution and unlimited

capabilities, factors that are considered most essential for continuous success in the financial trading business.

On how migrating to the MT5 platform might impact on a brokers existing back office operations, Leahy remarks that for firms that operate using the MT4 platform’s back office for risk management and reporting, the transition will be simple from a technology perspective. “Just offer the new MT5 platform as a standalone platform; invite clients to try it.” he says. “Firms that rely on separate risk management or reporting platforms will need to build a reporting API that links their MT5 to their risk and reporting software, ideally linking both MT4 and MT5 to a single back-office system.”

“At CMAP we intend to offer a ‘turnkey MT5’, where we’ve partnered with oneZero Financial to provide associated technologies. Their bridge and hosting services, combined with CMAP’s operational knowledge of MT5, will give brokers a solid foundation for growing with the new platform,” Leahy states.

Saidullin adds, “MT5 offers rich internal database resources and components, that proclaim the platform self sufficient in operation through its back up servers and reporting API’s, and requires no additional external integrations in database resources.”

Migration from MT4 to MT5

With MT5, existing MT4 brokers have a choice of complete or gradual migration through parallel operation of both platforms, according to MetaQuotes. MetaQuotes says MT5 leads to more business capabilities, by offering more market opportunity to traders, thus expanding brokers’ client bases. Saidullin notes: “Most brokers see this opportunity as a way to expand their services, promote innovation, and further differentiate from other brokers in terms of value and service offered.”

In terms of practical application of the system, the familiar GUI interface of MT5 allows back office staff to utilise their existing knowledge of MT4 and apply the same principles to learn the new system. By doing so, they will be able to focus on the differences of the two systems and explore new markets

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and opportunities, says Saidullin. Mapping and transferring operational settings from MT4 to MT5 is simple, so users can efficiently support the back office while configuring MetaTrader 5.

Brokers using the oneZero bridge have several options when it comes to migrating up to MT5, says Ralich. Its MT5 bridge technology utilises the Gateway interface. This adapter connects into the oneZero standard bridge hub, and utilises the same core routing, trade monitoring and LP connections as its legacy MT4 bridge. “This means brokers using our existing bridge can feed and process trades, manage their spreads and routing logic, and control LPs all from one interface for both MT4 and MT5.”

“Brokers who choose to manually manage risk within MT4 will

“MT5 offers unique flexibility in terms of integration, allowing brokers to choose the best integration method that fits their needs.”

Alexander
Saidullin

need to find a way to couple that risk into an external system, or directly into MT5,” continues Ralich. “I suspect many brokers will look to straddle between the two platforms as they migrate clients. This requires technical solutions for monitoring, covering, and analysing risks from both platforms simultaneously. If a broker isn’t already using a bridge to manage their platform risk in a centralised location, the move to MT5 would be a great time to start.”

MT4 plus MT5?

MT5 is still new in the market and there are only a few brokers that have gone live with it to date, says Lahav. “My prediction is that traders that are already accustomed to using the MT4 will probably keep using the current platform for the time being at least, while new ones will immediately start using MT5.

Brokers who are looking to maintain the two platforms simultaneously can take a few different directions, says Ralich. The most simple, but also least sophisticated option would be to manage risk on the platforms separately. Any client who trades on MT4 or MT5 has their exposure controlled within that system alone, he notes. This would be the more traditional, out of the box way to manage the systems. The second option is to use a bridge technology to offset the risk from the platform into a centralised back office, ECN, or clearing partner.

“By handling risk through a single bridge connecting to both platforms, brokers will be able to monitor their exposure from a single location,” states Ralich. “Advanced features in our liquidity bridges help facilitate the passing of specific client, group and platform data into the centralised clearing source to provide a robust auditing facility.

The last option for brokers is to build out an integration which passes client risk from one platform to another. Known as back to back integrations, the coupling of



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two platforms is a significant challenge, but one that oneZero has accomplished successfully in the past.” However, brokers face duplicating efforts by supporting both MT4 and MT5 simultaneously, explicates Nolan. “MT5 is not an upgrade from MT4. It is a redesigned platform. This means additional personnel, costs, integrations, client support, and overall resources. MT5 creates the opportunity to trade multiple products on a single platform. However, successful FX traders, especially those with EAs, may be reluctant to migrate.”

Nolan continues: “Brokers must plan to support both platforms for the foreseeable future. They will have choices to make concerning additional bridges, back office, plugins, etc. Instead of duplicating support efforts of MT4 and MT5, brokers can turn to IT firms, such as Boston Technologies, to provide support and services. Outsourcing can take the place of hiring additional staff, implementing new policies and procedures, and provide a single contact for supporting both platforms.”

Added storage needed?

With respect to improved storage and data processing capabilities that brokers should consider utilising to support the new features of MT5, Saidullin says: “The architecture of MT5 eliminates the need for any additional software components to be fully functional. The balance of workload for each server means that MT5 is significantly faster and has improved performance in executing all business operations. The system uses internal resources for data storage and offers unlimited back up servers for enhanced security and operational efficiency if hardware fails.”

“MT5 servers can be deployed either on one hardware server, or on several dedicated servers, according to the requirements of the broker. We normally recommend our clients to have at least two dedicated servers for main operations and backup redundancy. The trading servers do not require expensive hardware resources for effective operations, as they feature extreme productivity and processing power - one trade server can effectively serve over 50,000 simultaneously

connected users,” adds Saidullin.

While Leahy remarks: “We have found that cloud computing in the popular sense is not stable enough for running a mission-critical platform such as an MT4 or MT5. CMAP relies on dedicated servers hosted at tier three data centres for our client-facing platforms. We do like using certain VPS software and hardware combinations to get maximum efficiency out of our data centre space and find that to be a more economical way to get peak performance, though it requires a large upfront investment.”

Ralich says that for any trading platform it is absolutely critical for a brokerage to provide 100% uptime and availability to their clients. This means



Andrew Ralich

“The more a brokerage is willing to invest in their clients’ understanding of the new platform, the more clients will show up at the door.”

focusing on three things: performance; reliability; and redundancy. “Though there are some brokerages who maintain their entire IT infrastructure themselves, many are leveraging companies such as oneZero to provide the hardware, hosting and redundancy models needed to keep a platform running 24/7. We have deployed a multi-location, VMWare-based cloud infrastructure for offering high performance, scalable system for our clients’ bridge instances, MT4 and MT5 servers, and reporting tools.”

Future growth

Looking at future capacity requirements, the distributed architecture of MT5 allows for smooth and cost effective scaling and clustering, according to the growth rate of any broker, continues Saidullin. “We can assure you that the future growth capacity needs of our clients will be met without complications. The system is very powerful in nature and can meet the requirements of the most demanding broker. Moreover, the pricing policy of MT5 reflects the long standing commitment of reducing the life time cost for all our products for clients, so associated costs with related future growth is also reduced.”

On what steps brokers can take to ensure they are prepared for future growth and capacity requirements once MT5 becomes more established, Gaies Chreis states: “With MetaTrader 5 our major goal is the future growth for our clients expanding to new markets. Our clients trust MetaQuotes as a provider of reliable and innovative trading platforms that meet the demands of traders. MetaTrader 5 is specifically designed to provide universal compatibility support for running online brokerage businesses simultaneously in all major financial markets: FX, OTC and stock exchanges.”

“Recently MetaTrader 5 received official certification from the RTS Russian stock exchange, a very important first step that demonstrates that the system complies fully with the trading system structure of stock exchanges. We are working closely with several stock exchanges, and more integrations will be offered very soon to our clients,” states Renat Fatkhullin, MetaQuotes CEO.

Interestingly, CMAP’s Leahy says he thinks the industry has relied on the wrong metrics for too long

when judging performance, with regard to brokers ensuring they are prepared for the future growth and capacity requirements of MT5.

Nolan states that the need to increase capacity due to growth is a good problem to have. “Most importantly, the understanding of technology and marketplace, or having a business partner that does, will lead to success with the establishment of MT5. Brokerages should evaluate their strengths, and not overextend their current skill set.”

“There is tremendous opportunity with MT5, but that also comes with equal risk for failure,” adds Nolan. “quality preparation combined with strategic partnerships will lead to successful growth.”

Support from third parties

MetaQuotes Software is responsible for the set up and support of MetaTrader products, as the official vendor. Due to the popularity for its products, various third party companies have emerged in the market offering complementary solutions to its clients, based on MetaQuotes technology. MetaQuotes expects the same trend to occur with MetaTrader 5, but with the difference that now brokers will have more choice of integration methods. “The compatibility issue is always a top priority for our clients and for this reason we will be proactive in approaching this matter,” adds Saidullin.

Ralich states that a key reason for MetaQuotes’ success with MT4 and MT5 is its ability to foster the needs of the end user. He says: “Brokerages need to embrace this same mentality when looking to attract clients to their MT5 offering. Any time a new platform comes about, there are features that clients need to be educated about.

The more a brokerage is willing to invest in their clients’ understanding of the new platform, the more clients will show up at the door.”

Nolan concludes: “This is an exciting time for new opportunities with integration and ancillary products relating to MT5. Look for the leading MT4 integration providers to be the first to market with new and exciting value add products. New ideas should unfold as the early adopters of MT5 begin hearing feedback from customers.”

Making the switch to MT5: A traders perspective

I'm a MetaTrader baby. It's a term I coined for those of us who've 'grown up' in the FX Markets trading on the MetaTrader platforms. Even when I graduated from retail trading, I still found ways to trade using the MetaTrader platform. I was there for the switch from MetaTrader 3 to MetaTrader 4 and although MetaQuotes has pledged to support MetaTrader 4 until the last brokerage stops using it, another switch looms on the horizon. The switch to MetaTrader 5.

MetaTrader 5 is a huge step in the right direction for both trading and MetaQuotes as a company. It's closing in on a more institutional type trading platform rather than the retail platform it was originally designed as. Some of the improvements that I see that will be beneficial to traders are:

- Availability of more timeframes
- Vastly improved programming language
- The ability to utilize LAN and cloud computing resources for backtesting and optimization
- Portfolio backtesting
- Multi asset class trading
- Depth of market availability

MetaTrader has always felt like home to me. From customizing indicators, to writing order management scripts for when I step away from the computer to writing algorithmic trading systems or as MetaQuotes calls them, Expert Advisors. MetaTrader is the platform of choice for not only myself, but for a huge percentage of FX traders. MetaTrader 5 brings a lot of new things to the table, but has also aroused quite a bit of criticism from die-hard MetaTrader 4 traders.

The price of progress

There are basically two much criticized points about MetaTrader 5: The first is the fact that MQL4 will not be compatible with MQL5. This is the price of

progress however. Can you imagine the limitations if we were still programming in BASIC? MQL5 brings in OOP (Object Oriented Programming) which offers up a vastly greater range of analysis and execution possibilities for algo traders. Anyone who's familiar and programming MQL4 currently should be able to pick up on the intricacies of MQL5 with relative ease. For those who don't program but have scripts, indicators or EA's programmed in MQL, MetaQuotes has launched a Jobs Service that will effectively match up traders and developers to facilitate rewriting of these MQL5 files. The second widely criticized change in MetaTrader 5 is the fact that hedging will not be allowed. This I think only requires a bit of education to fully comprehend the fact that hedging is no longer an option, effectively changes nothing when it comes to profit and loss. In an order based system, a hedged position locks in a profit or in 99% of cases where people hedge, a loss. In an order based system like MetaTrader 4, the loss is not in balance, but in equity. In a position based system like MetaTrader 5, this loss is simply in both. A complete video explanation of position based vs. order based trading can be found on Fair trading Technology's YouTube Channel here: <http://www.youtube.com/user/FairTradingTech>

MetaTrader 5 is another great platform, and from a technical perspective a huge leap forward for MetaQuotes. As a trader I'd like to see more charting features such as range bars and Renko charts, but who knows? Maybe in MetaTrader 6!



McLean Van Cleve

Retail FX Roundup

Retail FX Roundup is a regular new feature in e-Forex magazine, which will be analyzing some of the key news items and trends in the Retail FX sector over the previous few months. The column is written by Gerald Segal who is Managing Director of LeapRate, an independent research and advisory firm, covering the world of online Forex and CFD trading. LeapRate's services include its Online Forex Industry Report, an Approved List of online trading firms and regular Forex Industry News analysis and updates.

The first half of 2011 in the online Forex world was a very busy one, with Forex firms showing a nice restart of growth after a somewhat slow end to 2010. Strategically, the past few months can be summarized by two key headlines:

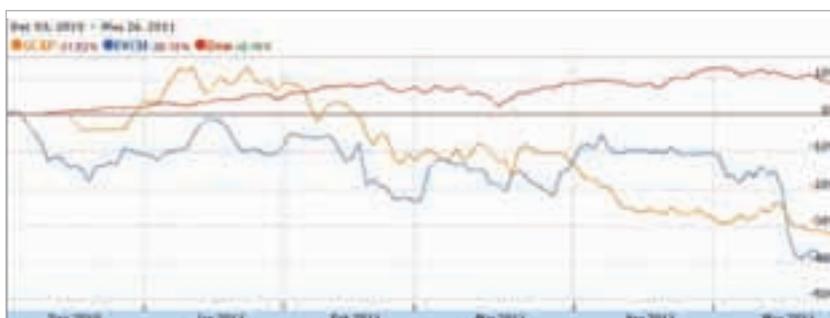
- Wall Street tries to figure out the industry
- Regulatory shakeout continues to reshape Retail Forex

Wall Street and Forex – not a marriage made in heaven?

One would think that the online Forex industry would be one which Wall Street would warmly welcome. Aside from the fact that Forex sector firms such as FXCM and Gain Capital (and their counterparts worldwide) have been generally consistently profitable, an attribute which Wall Street generally likes, it also happens to be an industry based on financial trading, leverage, risk management, marketing, customer service – all things which Wall Streeters themselves should be able to easily understand.

However, the first few months of both FXCM and Gain as public companies have been anything but smooth sailing, disappointing several other firms which have had their eye on an IPO. These low-lights include:

- **Disappointing share performance** – As of the writing of this article, FXCM and Gain shares are down 36% and 32% from their respective IPO prices, while the overall equity market is up (about 9%) since FXCM priced its IPO last December.
- **Difficult first experiences reporting as public companies** – When given the chance to broadcast their results as public companies for the first time to the investing world following a not-so-bad Q1, things could not really have gone worse. Despite top-line and volume results which grew nicely from 2010, Wall Street gave the firms a big thumbs-down, knocking their share prices down by a further 17% and 6% respectively the day Q1 results were announced.
- **Low share trading volumes** – (Almost) nothing scares off serious investors more than thin trading volume. Even if an investor were to like the stock of a company and its prospects, low trading volume would mean that it would be difficult or even impossible for an investor to build up a meaningful enough position to make it worthwhile. Similarly it might be difficult to impossible to eventually sell the position when the time was right to sell, at least without moving the market. With FXCM averaging about 450,000 shares traded per day, and Gain just 150,000 (or well below \$1 million in value traded per day), the volume is just not there - yet - to attract investors. By contrast, consider trading volumes at somewhat comparable firms such as Charles Schwab (10.3 million shares per day), E*Trade (4.5 million), TD Ameritrade (3.6 million), or even smaller firms such as TradeStation (1.7 million) and MF Global (2.0 million).



Not a pretty picture! – FXCM and Gain share price chart from IPO

Source: Google Finance.



WALL ST

- **Analyst zigzagging.** Wall Street research analysts are not always the most consistent types, and are certainly entitled to change their minds about a company or sector every once in a while. However, the “about face” rapidly taken by several of the key equity research analysts which picked up coverage of FXCM and Gain after their IPOs, so soon after selling stock to the public – first recommending the stocks with \$15-\$18 price targets, and then quickly souring on them and lowering price targets as the stocks of both companies continued to sink lower in single-digit territory and all without any monumental new industry-shaking news on the horizon – led many following the industry to conclude that the Wall Streeters simply had not done their homework on the industry, and were having difficulty understanding what is really going on at the Forex firms (good and bad), what is really driving growth in the sector, etc.

It is interesting to note that this is not the first time Wall Street seems to have “turned on its own”. The public market debuts of some private equity firms in 2007, such as The Blackstone Group and Fortress Investment, were resounding flops as the shares of those firms fell sharply soon after IPO. However those firms had the misfortune of poor timing (or good timing from the perspective of the sellers), as the overall equity markets headed into a tailspin in 2008 through early 2009, dragging the PE firms down with them. Neither FXCM nor Gain have that excuse though, as the equity markets have performed well overall since their IPO debuts late last year, and as other internet-based firms have returned to the IPO market with much fanfare and success, most notably the recent listings by LinkedIn and Russian web search and services company Yandex.

Continuing Focus on the Regulators

Clearly, the actions of key regulators around the world – in the US, Europe, Australia, Canada and China – continue to reshape the online Forex industry, creating both roadblocks and opportunities in different markets across the globe.

In the US, we have now seen the first few months of the effects of new maximum leverage rules (initiated as of October 18, 2010), whereby NFA-regulated firms in the US cannot offer more than 50x leverage on the Forex “major” pairs, and 20x leverage on all other pairs. While there was a lot of doomsday talk circulating before the introduction of this new rule, it has not seemed to have had much of a negative effect, if any, on the trading volumes of US-regulated Forex firms. Most of the US firms already had in place relatively modest leverage limitations (typically 100x), and most traders did not avail themselves anyway of the fully allowed maximum.

An interesting regulatory move made recently by the FDIC (or Federal Deposit Insurance Corporation), which supervises the licensed commercial banks in the US, was somewhat overlooked by industry participants but to us speaks volumes about future competition. Specifically, the FDIC proposed allowing their supervised institutions (i.e., the banks) to offer leveraged Forex trading to clients, with very similar rules as already put in place by the NFA and CFTC, which regulate the existing non-bank Forex firms.

As the FDIC’s proposals basically mirrored the existing NFA rules, not much attention was paid to its announcement. However, it has been indicated to us that the FDIC rarely introduces rules without a reason or need, such as behind-the-scenes lobbying by its member institutions which would like to enter a market. And that is the key here – our “reading between the lines” would indicate that there are likely several (major?) US banks which would like to look at launching online Forex businesses, leading to more potential competition in the US market and beyond.

“...led many following the industry to conclude that the Wall Streeters simply had not done their homework on the industry, and were having difficulty understanding what is really going on at the Forex firms.”

Longer term, the holy grail of the Retail Forex industry remains China, which is basically closed to Forex firms but is potentially one of their largest markets. The Chinese authorities seem to be taking baby steps toward opening their markets and currency to more trading and speculation, such as the recent introduction of Yuan options trading and the licensing of several foreign financial institutions to make markets in Yuan options. The Chinese are now also allowing some firms such as Gain Capital to open Rep. offices in the country. However, we believe that we are still a long way away from the Chinese authorities allowing foreign firms to take Chinese Retail client money, or from officially allowing margined spot Forex trading.

Looking Forward

As we head into the second half of the year, we are looking at some issues and trends which we believe are going to continue to reshape the industry, including:

- **MetaTrader 5 launch** – Although it has been out there for a little while, to the best of our knowledge MetaQuotes' MT5 is still in "advanced Beta" form, offered mainly in demo mode. As MT5 goes live in the second half of the year, we are going to keep a

very close eye on its effect on volumes and trading patterns in the industry. e-Forex has been covering this topic in detail recently.

- **Continued consolidation** – With now-public firms such as FXCM and Gain Capital pressured to continue to show growth in a slow-growth environment and some of their privately-held competitors looking to keep up, we believe there will be some interesting M&A deals in the sector over the next few months, which should continue to help reshape the industry for years to come.
- **Asia** – Outside of the potential of China which we discussed above, Asia has clearly been a hot-spot driving industry growth the past few months. For example, in Q1-2011 Asia represented 48% of Gain's Retail volume, up from just 24% last year. Asia is quickly becoming a key battleground in the Retail Forex industry, as competition heats up for existing clients, as well as for positioning for eventual entry into China.

For more information visit LeapRate's website at www.leaprate.com.



Thoughts on Selecting a Technology Provider

Tom Higgins is CEO of Gold-i, a market leader in retail FX trading systems integration. Prior to setting up Gold-i, he was a Chief Technology Officer in the City for over 20 years and used that experience and perspective as a technology buyer to shape the Gold-i offering. He offers guidance on the key areas to consider when selecting a technology provider.

Having spotted a gap in the market for products which would enhance the FX trading process for retail brokers, I developed the Gold-i Gate Bridge – a super low latency bridge which connects MetaTrader to both internal and external sources of FX liquidity. However, I knew that our success would not solely be dependent on having an exceptional product. There are so many other aspects which should be considered by organisations when selecting a new technology partner including: cost, service levels, product flexibility and ongoing innovation. I was keen to address all of these elements in the Gold-i offering.

I would therefore advise buyers to be mindful of the following:

1. Consider the True Cost

Don't just look at the transaction fee when evaluating the cost. Think about the true costs involved. Significant additional costs can be incurred if the product performs poorly – for example, if it has high latency or results in trade errors. If the system is inflexible or allows limited customisation, you may need to invest in additional products before too long.



2. Product Performance

Test the products which are available on the market and assess them in terms of performance, latency, reliability and functionality. We offer free product trials and advise customers to 'try before they buy.' Make sure the product delivers against your needs – for example, does it support large order sizes? Does it support B/A Booking?

3. Flexibility

Don't just think about your current needs. Plan ahead in order to ensure you select a product which suits your current and future needs. For example, the Gold-i Gate Bridge and our real-time back office integration product, the Gold-i Gate Link, are highly scalable. They will work with any asset class in retail and institutional trading, on a global basis. Demand for multi-asset trading is growing rapidly so it's important to select a system which will not restrict you as your business evolves.

4. 24 x 7 Customer Support

Be aware of the levels of customer support. There is nothing more frustrating than needing help but finding that the helpdesk is closed.

5. A Global Offering

Be mindful that providers with global distribution partnerships will be able to provide strong levels of local support.

6. Independence

Opt for an independent provider, not one which competes with brokers.

7. Check out the Company Credentials

Find out about the company you will be dealing with. Ask about their relevant customer experience and speak to some of their clients to gain an impartial but informed perspective.

For further information on Gold-i,
visit www.gold-i.com



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MB Trading: where customer service lives up to its name



e-Forex talks with **Ross Ditlove**, CEO of MB Trading

Ross, you founded MB Trading in 1999. In what ways has your business model evolved since that time and why do you think it's now proving so attractive to clients?

Steve Demarest and I co-founded MB Trading as an equity-side trading firm. Our goal was to provide

customers with a trading experience that leveraged emerging trading technologies yet kept execution costs low. We specialized in “smart” or algorithmic routing of orders utilizing ECNs and other destinations. We added futures and options trading to the mix all while maintaining a low customer trading cost. Along the way we were innovators in offering multiple server-

sided order types, API's for developers, sub-pips to the retail Forex community as well as a host of other new offerings and technologies. In 2006, we added Forex to the company's product mix. From the start we wanted to stay true to our roots and remain an agency type broker. We built an FX system which minimized many of the liabilities that the retail FX client faced at the time, including stop hunting, re-quotes, and an inability to display client orders on an order book for all to see. Clearly, these decisions are paying off. Customers are now learning about FX transparency and how adding liquidity to the system can benefit them and other traders. This is a paradigm shift for the retail Forex marketplace, which comes with large upside.

MB Trading offers customers a truly transparent ECN trading experience with direct access to qualified FX liquidity destinations. Do you think the traditional way that Retail FX trading has been conducted is set to change forever with the arrival of true ECN technology such as yours?

We believe markets, when given the opportunity, will naturally seek efficiency. We further believe that this shift is well underway. We maintain that until Forex brokers immediately display a customer Limit order in their quote for others to hit, that their market is neither transparent nor efficient. The Forex marketplace still has a long way to go. This is very similar to what we experienced in the Equities marketplace with the introduction of ECNs like Instinet and Island back when the US Equities markets had a similar transition. We also observed a similar transition for Options, and we have no reason to believe Forex will be any different.

Market efficiency cannot happen without "best execution." So long as a broker does not allow a limit order to post, the execution of that order remains in the hands of the broker, not the market place. As best execution becomes more important to the retail trader, more brokerages will follow MB Trading in offering the ability to post limit orders. MB Trading is experiencing quantifiable spread reduction as a result of Limit Order posting. We expect to see spreads shrink to as low as a 1/10th of a pip as clients learn that a transparent brokerage is a necessary tool. In the end it's about controlling trading costs. The tighter the spread, the more money that remains in the pockets of retail clients.

Why did MB Trading decide to launch its Pay For FX Limit Order System, how successful is it proving and in what ways do you think this venture will spark changes to the industry?

Having ECN technology is only one piece of the puzzle. A brokerage also needs to have liquidity inside of the ECN. Back during the ECN transition for Equities, Archipelago (ARCA) applied the same approach. They too paid their customers to post their orders on their book so that other customers would have more liquidity to fill against. At the same time, they charged the clients that crossed orders on their book. ARCA eventually became the automated side of the NYSE. We believe the concept is powerful, and thus we are offering a similar structure and technology for FX. MB Trading acts as a hub. It is financially beneficial to us to have more liquidity, via client Limit Orders, resting on the ECN system so that less of our order flow needs to be routed out to banks. This concept is proving successful as our rebates are growing and our spreads are shrinking. We further post on our website a counter which shows how much we have paid in total for posting executions as well as daily amounts paid out. Our daily payment to clients has grown to an average of \$6000 in May. We could not be more pleased with the market's acceptance of this plan. By year end, we plan to display the actual spread reductions per pair for all to see.

MB Trading offers a wide variety of trading platforms allowing investors to trade Forex, Stocks, Futures, and Options. What work have you recently been undertaking to extend the key features and functionality of your software?



Ross Dittlove

That is a difficult question to answer only because there are so many ways that we have been advancing the firm. We introduced Pay for Limits in Forex. We continue to expand our Metatrader integration. We've lowered our fees in Stocks. We recently added spot gold and silver trading. We're expanding our order types for Forex. We have made dozens of improvements in our charts, added wireless products, launched tablet-based applications, and are now adding a web-based product. MB Trading is adding a separate Forex operation in Europe to offer 100:1 leverage and hedging to non-US customers. There is no shortage of work being done at the firm. We have more on the horizon for the second half of the year that will be announced shortly.

Do you believe the electronic trading of Options is set for really significant growth amongst retail traders and investors and if so, why should they consider trading these instruments with MB Trading?

Options are a preferred asset class for professional traders because they are flexible as a trading vehicle. You can limit risk even though you get leverage. The exchanges have really helped to lower spreads on options, which make them more appealing to the masses. MB Trading charges only \$0.95 per contract with no minimum for option trades. We recently launched our advanced options analytics software that helps people see visually what the decay factor of the options means to their trades before they put them on. Additionally, we also now provide clients with an advanced spread calculator. We see a growth future for options, and we do believe that our platform, low costs, and routing algorithms make us a great option for traders.

Do you expect to see continued demand for more powerful and innovative mobile trading services and what steps has MB Trading been taking to make your order entry and account management systems accessible to clients via mobile devices?

We have iPad, iPhone, and Android applications.. The phone-based apps are appealing for customers on the go to track their trades and account balances but the size of the screens prohibits them from being a true trading vehicle. However, the extra screen real estate that comes with both the iPad and the Android 3.0 tablets has real potential to change the ease with which traders can trade on the go, even just around the house. We went the extra mile in these applications. All are interconnected such that pressing an order button in one immediately displays the live order in another. A position or balance update on our servers update all platforms simultaneously, there is no delay! We will continue to focus on these applications, and

we think there is a big shift in accessibility that could come from them. However we do not see our powerful Desktop Pro going away anytime soon.

MB Trading has always placed great importance on providing live customer support throughout all the trading hours. In what ways has the launch of MBT World helped you to better understand the needs of your clients and improve your overall service offering?

There are several aspects to MBT World that help us sense the pulse of our traders. First, we have the MBT Idea Exchange, which allows people to post ideas for improvements in our system and then vote on each other's ideas so we can see what the community wants the most. Second, we have a community experience where customers can share their positions with each other in a variety of ways. Third, we offer an extensive array of webinars to train people on our products, and we get instant feedback into what makes sense to them and what doesn't. Each of those courses is followed by a brief survey that indicates other needs our customers may have. Combined with 24 hour support, access via chat, email, phone, Skype, and web boards we believe MB Trading continues to offer a level of service not available from most brokers.

Despite an increasingly competitive business environment, MB Trading continues to win industry awards. Looking ahead, how will you balance the need to secure and retain customer loyalty whilst growing your business to stay on top of this game?

MB Trading maintains a strict code of support and service for our clients, all while keeping our business expenses minimized. We do not have new offices; we don't even have nice carpet in our offices. We spend the money instead on employees and hardware. We remain committed to offering the best service at the lowest costs possible. Our success is only realized when our clients are happy and refer us to other traders. We leverage our technological know-how and over ten years of experience in order to remain relevant. We are also careful who we market too. Having clients that don't trade but demand a lot of support prevents the clients who are very active from getting the support they need. We are highly specialized in who we serve, and it allows us to remain quick and nimble. MB Trading has plenty of customers with us today that have been with us since company inception. Barron's has recognized us as a winner and one of the leaders of this industry for over six years running, and that does not happen overnight. We simply are committed to our customers on an individual level. No client is a number and every client is critical to our success.



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Developing customised Expert Advisors from bespoke FX trade strategies

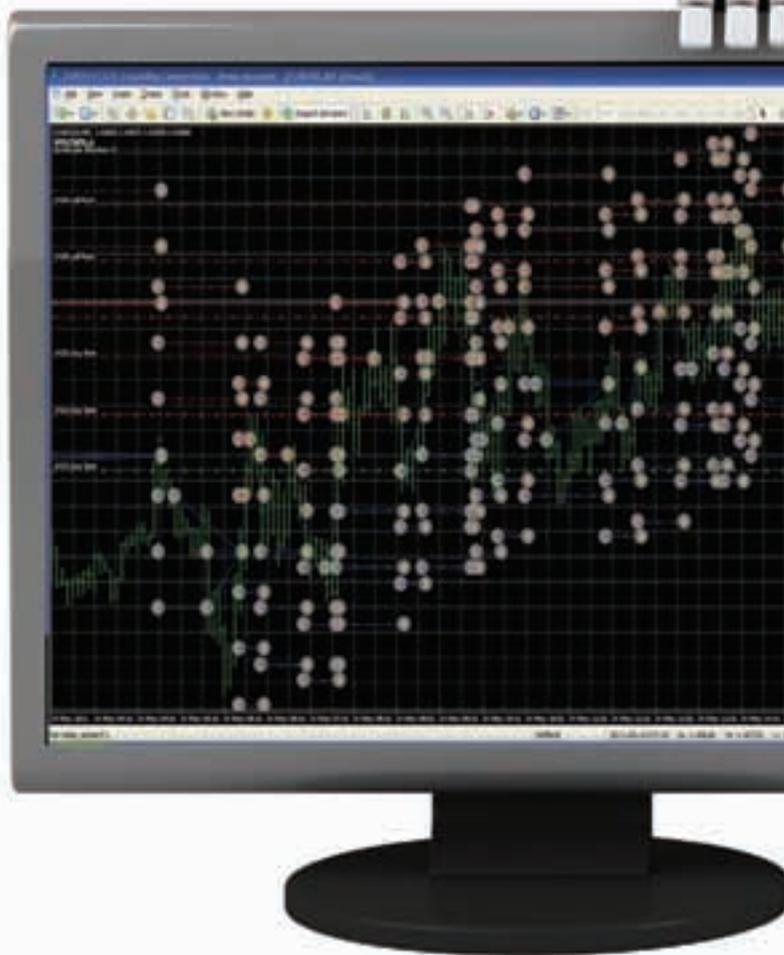


Shaun Overton
soverton@onestepremoved.com

MetaTrader quickly dominated the forex market as the platform of choice for retail traders. Its easy to use interface and wide availability across multiple brokers made it an instant hit. Shaun Overton examines the ease with which traders can use Expert Advisors to facilitate their trading, offering a viable alternative to traders that are unable to trade manually with consistent positive results.

While most traders intuitively understand the benefits of automated trading, they have a hard time quantifying their strategies in mechanical terms. Traders refer to subjective topics such as swing highs and retracements.

Deciding what counts as a swing high, for example, poses a number of challenges. A strategy could review a short number of bars, making decisions based on micro trends. It can also review a larger time windows, only placing trades during attention grabbing price movements. If the strategy uses the big picture, how do





“Take the strategy’s shortcomings as a learning experience. During the process, you may even uncover the weak link that leads to renewed optimism.”

you define the picture in terms of time or bars? Traders can use a fixed time window (e.g., 50 bars) or develop a mathematical rule to decide how much time is relevant.

Getting away from subjective terms

The goal is to get away from subjective terms and to turn the strategy into a flow chart. Once that is done, you have something that you can program.

Consider a simple strategy where you wish to buy moving averages crosses in the opposite direction of the day’s momentum. One way to handle the problem would be to use moving averages and pivot points. If the 12 period SMA crosses above the 25 period SMA and the low of the daily candle is less than S1 and the low is greater than S3, then go long. Exit the trade when the market moves in the opposite direction. Do the opposite for short trades.

The below strategy answers the basic questions of trading:

- How do you know precisely when to enter a trade?
- How do you know when to exit?

It also defines the steps in completely unambiguous terms. Anyone can follow the rules like a pilot following a checklist before take-off. The strategy is now ready to be programmed.

Computers think in absolute terms. Reducing the strategy into mechanical components modifies it into a form compatible with a computer’s black and white



Colour Based Indicators

thinking. Remember that computers think in bytes of zeroes and ones. Something is either true or false; no gray areas exist. The flow chart approach allows the programmer to approach the strategy in the same way as the program itself. Did the fast SMA just cross above the slow SMA? If the answer is yes, then the code needs to do something.

Traders should approach the topic of strategy development with the attitude of a researcher.

Scientists often start out with a hypothesis, only to discover an unexpected result or possibly something totally unrelated.

When developing a trading strategy, spending several hundred dollars to program it and then several weeks waiting and testing, it is quite natural to develop an emotional commitment to the strategy. Failure occurs for a number of reasons and is very likely. Rather than hoping to avoid failure, the more realistic and robust approach is how to handle the failures that inevitably follow trying something new.

The most common reaction to a failed strategy is to assume that “something is missing”. Almost everyone

decides that the next best step is to tack on one more indicator or to make it more complicated. This is a potential waste of time. Instead of expending more effort on something that shows no evidence of working, proving the strategy’s concept wrong makes for a far more productive use of time. Take the strategy’s shortcomings as a learning experience. During the process, you may even uncover the weak link that leads to renewed optimism.

Strategy categories

Retail forex strategies typically fall into a narrow band of categories: indicator based, price action based and Martingale position sizing. The SMA cross strategy depicted above follows the path of a generic indicator. More commonly, traders like to explore the idea of using color based indicators to make decisions. Buying when the Heiken Ashi is white and selling when it’s red represents this idea clearly.

Price action strategies are well known to anyone with more than a year in the market. Most tend to follow a Turtle trading approach with either riding or fading a breakout. Almost all strategies of this type define breakouts as time based extremes or by referencing moving average bands.



Backtester

language's documentation and read how-to articles on developing programs. The site, however, suffers from poor organization and content developed by non-native English speakers.

If you are new to MQL, I recommend browsing the "articles" section of the web site and selecting articles that focus on easy tasks. As you read through each article, play with the code to get a feel for how step in the process affects each part of the whole. The "docs" section is handy for referencing specific functions and classes. It is not, however, very helpful for gaining the big picture. The only way to understand how the pieces fit together is to get your hands dirty with the code and start playing around.

Those without a programming background will be hard pressed to develop custom applications from scratch. MQL does not offer the high-powered functionality of standard programming languages like C++ or C#, but its appearance and syntax certainly resembles them. You need to read a basic programming book if you are unfamiliar with programming. Any introductory book on C or C++ should suffice.

Alternatively, you can hire a MetaTrader programmer to do the work for you. A list of programmers is available on www.eaprogrammers.com. Keep in mind that the quality, cost and English language fluency of the programmers varies widely. Qualities that you should look for when selecting a service is the timeliness of responses, whether or not the person responding seems to understand your strategy and

the cost. My company, www.onestepremoved.com, specializes in programming for MetaTrader.

Verification and Backtesting

MetaTrader 4 offers a nice feature called the visual Backtester. Once an EA is programmed and ready for its initial tests, the easiest way to verify its accuracy is to compare its behavior to what the chart dictates that it should do.

Start with opening the Strategy Tester from the View menu at the top of the screen. The primary tab, which is labeled Settings, contains a check box in the middle called Visual Backtest. A chart pops onto the screen if this feature is selected when the backtest commences.

MetaTrader 5 did away with the Visual Backtest feature, unfortunately. The only remedy for programmers debugging their programs is to either write copious amounts of information to the log file or to use the new compiler feature that steps through the code. An expert advisor is ready for performance testing only when the code works exactly as intended. Once this is done, traders can take one of two approaches. They can either backtest the code or forward testing.

Forward testing is the less well known concept, probably because it requires a lot more time and patience. The idea itself is very simple. Open a demo account in MetaTrader, throw the Expert Advisor on a chart and see what happens. The premise is that if the EA's performance matches your expectations, then it is fit to trade.



Backtesting saves a lot of time but comes with a number of pitfalls, especially in MetaTrader. One of the greatest weaknesses of the platform is that it does not come supplied with quality historical data. Most novices run backtests and examine the results. It never occurs to them that the results might be totally bunk. It is extremely important to examine the data quality metric displayed in the backtested result. The lower the number, the less reliable the outcome.

Backtest accuracy usually corresponds with frequency. Strategies that trade once per day or on hourly candles usually reproduce faithful representations of their performance in backtests. The quality of the tests degrades rapidly unless the user imports historical price data from a known, quality source.

Converting Strategies from other platforms

Most forex traders that switch to MetaTrader tend to have their files in NinjaTrader or TradeStation. All packages offer the same type of general functionality, although their capabilities vary between platforms. MetaTrader, for example, makes it relatively easy to compare the effects of position sizing on the net profit of a strategy. NinjaTrader, on the other hand, requires a lot of custom code specifically geared towards backtesting a historical balance.

One of NinjaTrader's advantages is that it allows for the full flexibility of the C# programming language.

Doing things like taking the exponential moving average of the ATR is very easy to do. Doing so in MetaTrader requires more finesse. The conversion process is not straight forward. The trader really only has two options: explain the idea from scratch and hope that the product turns out the same or find a programmer familiar with both platforms.

Conclusion

MetaTrader is a great platform for retail traders because of its simplicity. Several hundred brokerages support the platform, enabling traders to find a house with whatever unique requirements they have for clearing trades. Like any retail charting platform, it lowers the barriers towards trading with automated programs. Most of the difficult programming components are embedded into the platform. Programmers simply decide how to handle trading decisions and use the pre-built toolkit that MetaTrader offers to wire the pieces together. MetaTrader's retail friendly attitude will most likely assure its continued acceptance as the retail forex platform of choice for automated trading.

An advertisement for 'One Step Removed' services. At the top, there is a blue banner with a white jaguar logo and the text 'ONE STEP REMOVED' and the phone number '(866) 212-1544'. Below this, the text 'METATRADER PROGRAMMING' is displayed in large, bold, blue letters. Underneath, a list of services is shown: 'Expert Advisors', 'DLL Programming', 'Custom indicators', 'Scripts', and 'MetaTrader Security'. At the bottom, a dark blue banner contains the website address 'www.onestepremoved.com'. The background of the advertisement features a green line graph and a blue bar chart.



REAL FOREX - Helping to bridge the gap between Retail and Institutional FX services

e-Forex talks with Yoad Drewes, trading director at leading Non Dealing Desk broker Real Forex.

Yoad, when did Real Forex commence operations and in what ways does your business model help to better align the interests of your clients with the company?

Real-Forex.com was launched in 2007 with the aim of bringing a new level of service to FX traders by bridging the gap between the institutional and retail FX trading world. Real Forex is powered by Finocorp Ltd, a financial corporation specialized in e-trading services for retail and institutional clients. Real-Forex.com is the outcome of Finocorp's partnership with First Derivatives Intl.

The company goal was to replace the traditional ECN based service with a next generation "Direct Bank Access" model providing traders closer access to a true best bid / offer multi-bank liquidity environment. Real Forex full STP outsourcing of risk to the banks provided the added benefit of full transparency. Finocorp's partnership with First Derivatives and use of their RealStream technology provide advanced functionality such as dynamic price replacement. For example: When a bank's price engine rejects an order execution request; our trading platform will

replace it with the same or better price from a different bank, allowing the trade to execute. This technology capability enables Finocorp to virtually eliminate cancel trades and price slippage, resulting in solid fill rates. The result is better pricing, execution and transparency for both retail and institutional clients.

What sort of institutional-level FX trading conditions does Real Forex provide for private and corporate investors?

Real-Forex provides both retail and institutional traders with equal access to advanced functionality; liquidity and execution capabilities traditionally reserved for sell side inter-bank trading. We provide all our customers with a broad range of capabilities, enabling each client to customize their own service by selecting those features relevant to them. Client's can even select their preferred trading venue from options such as Real-Forex's proprietary platform, MT4, or API connectivity.

What options are available for traders to connect up to and trade with Real Forex?

There are 3 ways to connect and trade with us. We work via Real Stream Trading, Meta trader 4 and FIX connections. Each platform has its own unique account settings, including differences in leverage, calculation of margin and other factors. Each venue



has its own unique advantages. MT4 has an exclusive MAM (multi account manager) account with no EA limitations. RSM has advance orders and the API offers simple give up solutions. Traders can choose the venue that fits their profile.

What are the key features and trading tools available with the electronic platforms that Real Forex provides?

Key functionality that we provide includes:

- Advanced orders - like FOK (fill or kill) and IOC (instant or cancel) so the trader can decide how they want to execute the order
- Flexible price range – customers can determine the slippage rate suitable for them and to decide whether to go in the market.
- Depth of market display – shows traders pricing inventory across various trade sizes.
- Layered pricing and sweeping – allows larger orders to be filled by aggregating executions associated with tighter prices on smaller amounts.

What do automated and Black Box traders particularly like about your Real Stream ECN?

The FIX based APIs are easy to implement, extremely reliable and low latency. There are two APIs, one of which comes with an optional supporting GUI. Each API is able to support multiple price streams that can be customized to fit the profile of each client's flow. The pricing and execution work flow between the liquidity providers and HFT client is supported by an extremely low latency technology solution (ie co-location in HFT data center with fiber cross-connections to price engines), allowing liquidity providers to better manage risk and thus provide better pricing. Additionally, the solution provides price providers with a granular ability

to analyse end client trading results to provide them with further confidence regarding risk management. Features such as dynamic price replacement virtually eliminate trade rejections. The API clients experience tighter prices, increased depth and higher fill rates compared with other venues.

What steps have you been taking to provide even higher speed trade execution for clients?

Our price aggregation technology and client trading venues (RSM, MT4 and APIs) have been co-located in the NY4 HFT data center and fiber cross connected to leading bank and

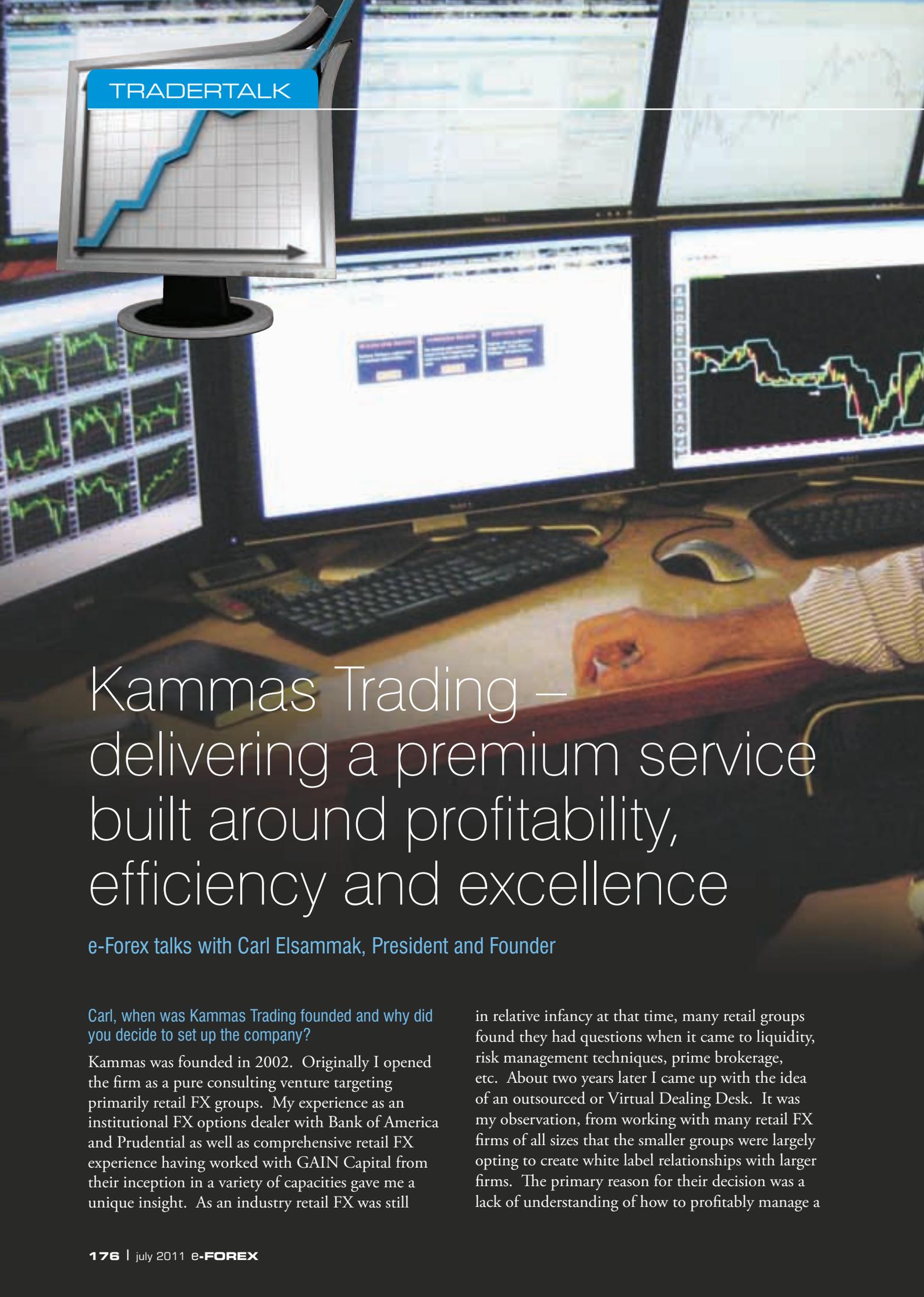
non-bank price engines. The performance through the aggregator, RSM and API is micro-second oriented. The higher speed pricing and execution is one of several key factors leading to enhanced pricing and fill rates. This new high performance environment will enhance the performance of service to both web trading clients as well as those connecting via an API interface. The new low latency environment is ideally suited to support high frequency trading. HFT/algo applications may be remote or co-located within the data center using fiber cross connections.

What partnership programmes do you offer for individuals, companies and other financial institutions who are interested in working with Real Forex?

We offer many options for brokers, IBs and affiliates. Partners can choose to become an IB, white label or affiliate, based on their level of involvement in the market. For IB's and brokers we offer white label branding and a client web based service delivery option.

Looking ahead, what plans do you have for expanding the range of products that Real Forex offers to help further bridge the gap between Retail and Institutional FX trading services?

We are continuously enhancing and expanding the services we offer to our clients across many fronts. Through the remainder of this year we plan to introduce new instruments such as NDFs and support asset classes such as CFDs. We are also expanding our trading venues to include trading using hand held devices. Our mission statement directs us to provide our clients, institutional and retail alike, with the best service & trading support as well as the most technologically advanced trading environment. Real-Forex continuously collaborates with clients to enhance and optimize the technology, liquidity and service we provide.



Kammas Trading – delivering a premium service built around profitability, efficiency and excellence

e-Forex talks with Carl Elsammak, President and Founder

Carl, when was Kammas Trading founded and why did you decide to set up the company?

Kammas was founded in 2002. Originally I opened the firm as a pure consulting venture targeting primarily retail FX groups. My experience as an institutional FX options dealer with Bank of America and Prudential as well as comprehensive retail FX experience having worked with GAIN Capital from their inception in a variety of capacities gave me a unique insight. As an industry retail FX was still

in relative infancy at that time, many retail groups found they had questions when it came to liquidity, risk management techniques, prime brokerage, etc. About two years later I came up with the idea of an outsourced or Virtual Dealing Desk. It was my observation, from working with many retail FX firms of all sizes that the smaller groups were largely opting to create white label relationships with larger firms. The primary reason for their decision was a lack of understanding of how to profitably manage a



Carl Elsammak

market making desk. Further, for those groups not located near New York or London they did not have an available talent pool to hire from and in many cases the cost of retaining a full time trading staff of experienced dealers was simply untenable. My idea was to put together a group of highly experienced FX dealers who can manage these clients risk books independently. Each client only pays for the portion they need making it a much more cost effective solution and all benefit from our decades of dealing experience, the flow information we see in total, our

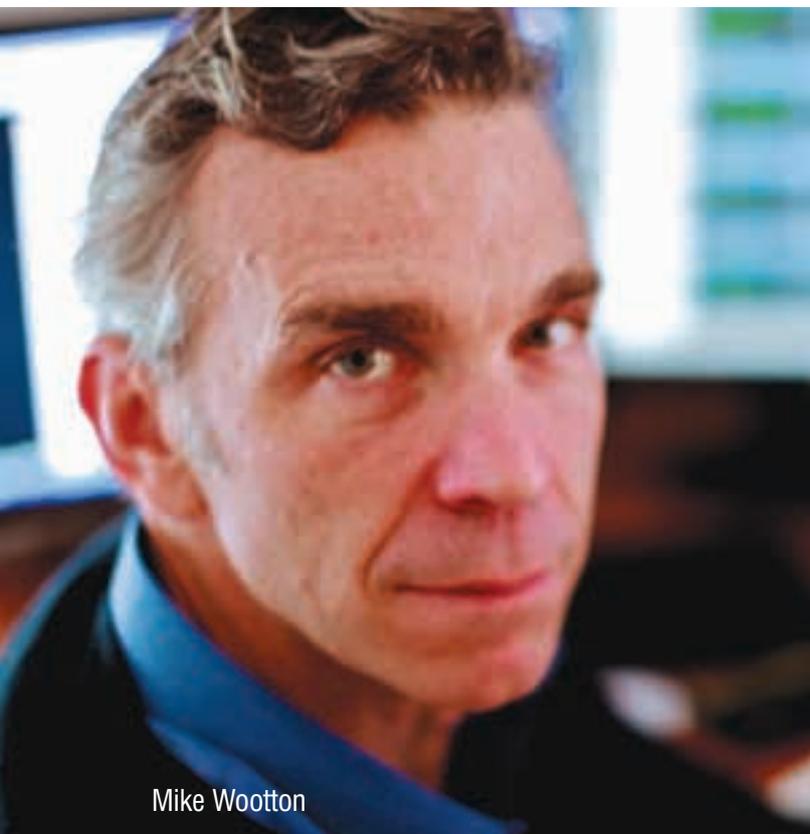
skill at technical and fundamental analysis, as well as our continued connection to friends and contacts within the banks.

What services does Kammas Trading provide?

Our services can best be defined along three separate lines. The first and most unique is the Virtual Dealing Desk service. Through this vehicle we offer a customized dealing desk product with highly evolved risk management practices at a price consistent with the extent of each client's need. Our experience is strongest in FX, with all of our dealers sourced from major bank FX dealing desks, and our understanding covers not only spot but forwards and options as well. We also manage metals, energy and index CFD flow for our clients as most brokers have added these markets to their offering.

Second is an execution service best suited for automated fund managers (hedge funds and CTAs) as well as agency desks. We have experience primarily in the FX and futures markets executing orders. This understanding comes from early in my career when I traded for large CTA groups including some inside of the famed Commodities Corp. For these groups the need to fill orders with minimal slippage and market disruption is paramount. Not only will it enhance return but also allow a strategy to grow assets under management. For these reasons execution is highly valuable to the revenue and sustainability of these managers.

The third line is consulting. Here we cover a large range of topics for a variety of market participants. We work on finding the right technology and clearing relationships for a particular client's needs. For corporate clients we suggest hedging strategies to insulate their multi currency payable and receivable expectations from adverse fluctuation. Considerations for appropriate strategies to corporate clients need to include their financial and accounting framework to ensure they remain compliant and that hedges do not hinder their balance sheet unnecessarily. We have worked as an expert witness on legal cases. We have been a sounding board for the private equity community looking to learn more about certain sectors of FX as they prepare to enter and price new investments. We have created educational packages focused on bringing



Mike Wootton

greater understanding to the retail sector. Our input has been used to develop new trading and risk management platforms in FX. We worked with a Swiss based mutual fund that wanted to better understand their risk / exposure and hedging opportunity that came from holding primarily USD based investments. And a number of other projects too numerous to mention. Our experience is diverse and can be applied in a flexible way across many topics in this field.

Who are the key people involved in the firm and what are their main day to day responsibilities?

I head up the company and am involved in business development, relationship maintenance, and trading. Everyone else is primarily involved in trading with each dealer heading a specific time slot. Geoff Gowey joined Kammass in 2005 and has had a very successful career in the foreign exchange market spanning 30 years as a trader and manager. He successfully and profitably managed the trading operations for some of the largest banks in the world, including Societe Generale and Banque National de Paris. John Hanly joined us in 2005 after a successful 25 year career working for banks such as Bank Austria, West Deutsche Landesbank and BNZ. Mike Wootton joined in 2006 after spending 20 years

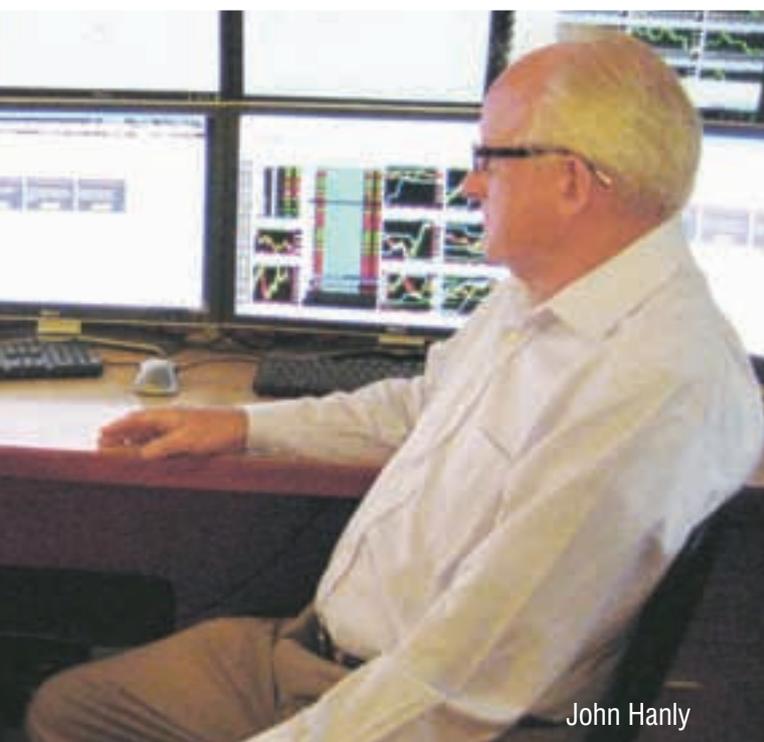


working for Bank of New York managing both sales and global risk management services. Richard Ashe joined Kammass in 2006 and has been in the FX market since 1987, working for Commerzbank in both New York and Frankfurt.

What sort of clients utilize your Dealing Desk Management services and what are their main objectives?

Our Dealing Desk Management clients are FX and CFD Brokers. These are groups who have recognized the opportunity this market provides. Traditionally they are very good sales and customer service groups, often having a background in equities or futures. In

some cases they have a strong technology background and build their own platforms. However, an overwhelming number of these firms are opting to choose many of the high quality platforms available for purchase or lease. They wisely recognize that outsourcing parts of their business they are less familiar with allows them to focus on their core strengths. Their main objectives are to build a solid business around providing a fair market, good tools, and good customer service to the sub-institutional market. Further, as good business people they strive to improve the risk adjusted return they are able to earn. Our service is integral to this goal.



John Hanly

What types of currency instrument are you trading and what execution time-frames are you typically employing?

We manage our client’s flow across a wide and ever increasing variety of currency pairs. In addition to the majors and all related crosses we also see flow in a variety of less liquid currencies including Hungarian florin, Indian rupee, Singapore dollar, Brazilian real, Scandi currencies, South African rand as well as metals priced in USD as well as Euro, GBP and JPY, energy and indices quoted as a CFD. All are quoted as spot and settled in USD. Additionally, we manage option risk on some of the more liquid currency pairs.

For execution clients the amount of time allocated

to each trade can vary. Some want to know their trades are completed within a relatively small window of 10 to 30 minutes. In other cases more discretion is allowed, generally no more than 12 hours. The difference often comes down to the expected life of each trade. Longer-term strategies can afford to take some extra time to help improve the average entry price than a shorter strategy can.

In what ways do you customize your risk management methodologies to suit the individual needs of clients?

I started this firm because I saw a need for experienced risk management by many of the retail FX brokers who were making 1 of 2 general mistakes:

1. Managing client flow internally without regard or understanding for appropriate risk / position levels resulting in exceptionally high revenue volatility (often putting them out of business to the chagrin of their account holders)

or

2. Sending all of the volume STP to another market-maker who either pays a relatively low flat fee (rebates) or whose price they marked up for the same effect. While this method removes the risk component and is certainly more desirable than the first scenario, it also leaves a large amount of potential revenue on the table and makes for a generally undesirable long-term business plan.

One of the first tasks I undertake with a new client is the clear understanding and agreement of risk parameters. There are many fancy methods including VAR for calculating this however, I find the best place to start is by setting maximum exposure limits. This is by far the most practical solution for a trading desk to employ as risk limits are primarily tested during high volatility market situations when there is exceptionally high customer activity and no time to ponder or reach for a calculator. The considerations for determining these levels are a mix specific to each broker and include balance sheet, volume expectations, nature of the client flow, risk appetite, and per trade revenue expectations. Obviously, more liberal risk parameters

should lead to higher “pip capture.” However, revenue predictability will reduce as return volatility increases. Therefore, it is imperative to find a happy medium that meets each client’s expectations.

You have been working in FX for over 20 years. In what ways do you think that long experience has provided you with greater insight into how the FX market operates and helps you to construct and implement more effective risk management frameworks?

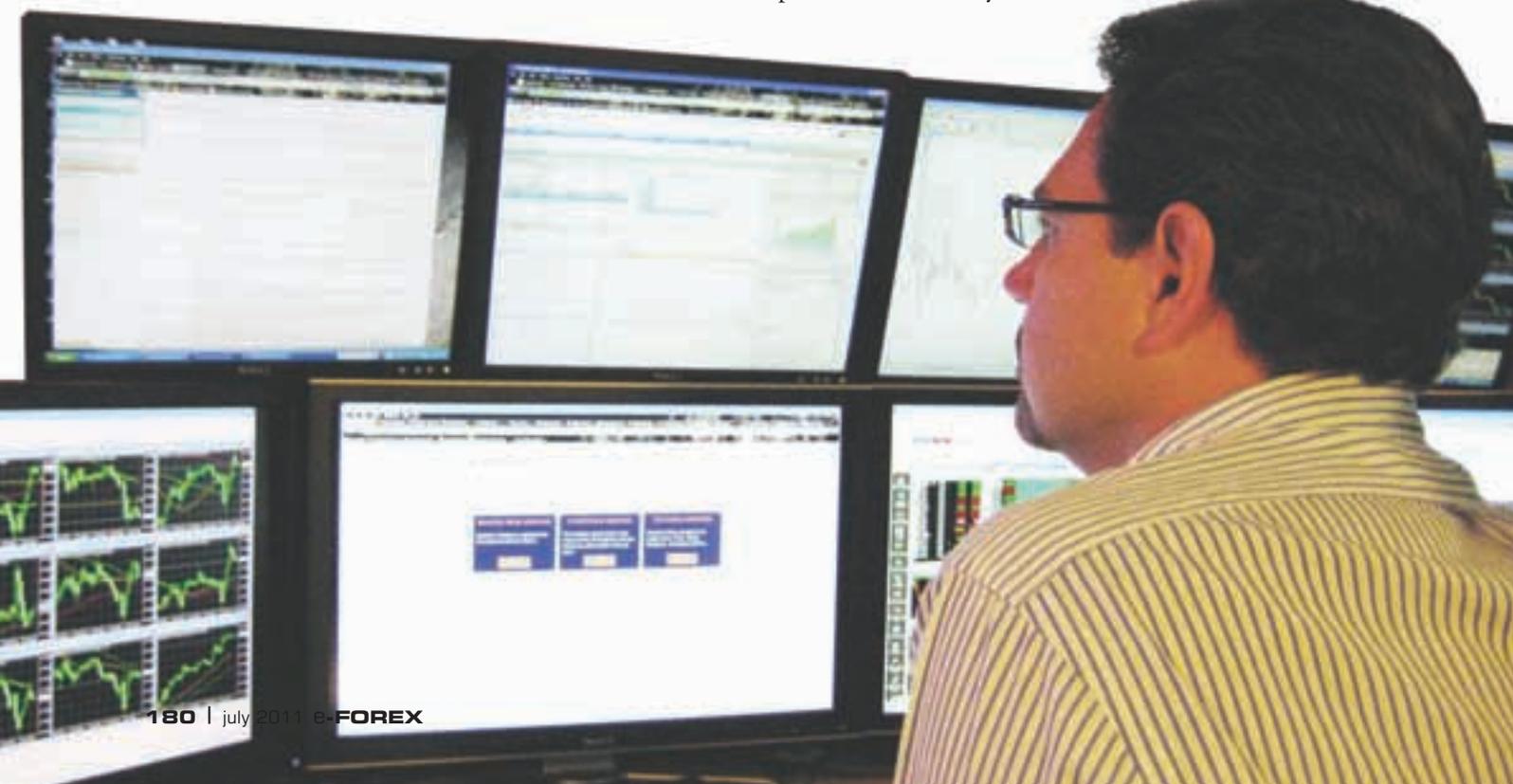
Despite public opinion (or should I say political opinion) it is clear that the OTC framework of open self-regulated markets works exceptionally well in FX. The explosive growth in trade volume among all participants and acceptance of the product among ever smaller participants has proven this. OTC FX has ignited interest and volume in the FX market allowing growth dramatically beyond what futures were ever able to accomplish. Innovations in option structures give hedgers more precise tools to manage their business while allowing opportunity for directional players to expand their interests. All of this produces a highly liquid market environment with very tight spreads. Because of this level of efficiency we are able to formulate solutions for our clients that closely match their needs. Further it has spawned a myriad of new business ventures working within and around FX all adding value. e-Forex has done a great job profiling many of the different participants new to FX and helping them understand their contribution.

Who are your Execution Services targeted at and what are they designed to achieve?

Kammas provides execution services for hedge funds, CTAs and agency desks. With a well-rounded understanding of markets and in-depth experience, Kammas can design a solution for clients to enter market orders with minimal impact / slippage. Each solution differs based on the expectations of duration for each trade. Legitimate managers never want to create market disruption through their orders. Kammas has experience primarily in the FX and futures markets executing orders both with and without discretion primarily for systematic programs (black box).

What are the sorts of problems and inefficiencies you find many trading firms are experiencing as they seek competitive advantages within the high performance FX trading environment?

Speaking from our experience and what I hear from colleagues at other firms I think it has to be technology. Increasingly we are putting together a kaleidoscope of unrelated technology providers, FIX and radiance API feeds, multiple databases, internally and externally developed software, redundant colocation facilities and much more while expecting everything to work flawlessly. To be completely upfront, given the complexity, it surprises me that it runs as well as it does. This may be a testament to the integrity of the IT teams we work with. I know of horror stories that have or nearly put solid organizations out of business. When problems do occur you



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Richard Ashe (Second from right)

quickly realize just how vulnerable and in some cases untenable the situation quickly becomes. In our case we are often dealing with well over 100 thousand transactions a day so as you can imagine without a clear window our position can potentially get away from us quickly.

Do you employ FX algorithms to help some clients minimize market impact when working orders and if so, are these constructed in-house or bought in?

We have a number of customized algos and indicators. All have been built by us or in a few cases as a collaboration with clients of ours. Each of my dealers have over 20 years experience trading FX for major banks. Consequently each has developed their own very specific “toolbox”. I strive to provide them with all of the market insight they need to be successful including a variety of charting services, news feeds (both written and audible), bank contacts, and customized algorithms.

A large portion of our success can be attributed to the experience and insight our team applies to the markets every day and this includes the proprietary algorithms we have developed.

What type of solutions are your FX Consultancy services team called upon to assist clients with?

As you know there are a large number of participants in the FX community. Each one has a different objective. However, regardless of the intended use each relies on basically the same set of tools and to produce the outcome desired. Here is where we make the biggest impact. Whether it is a corporate

client looking to hedge their non reporting currency exposure from future payables and receivables, or a money manager who has exposure in a variety of assets priced in different currencies. We provide advice on how to neutralize the potential effect. Or we may give our opinion of where we expect the range of a currency pair to trade over some period allowing them to determine where to add a hedge at a more advantageous point by allowing a bit more fluctuation and risk limits. Often this can be expressed through various options strategies. We will also suggest liquidity and technology partners, work with Private equity groups looking to make strategic investments in FX, be retained as expert witnesses and a variety of other engagements.

Have you noticed any significant demand for specific FX Consultancy expertise in any particular areas and what impact could proposed regulatory changes to FX market operations have on this side of your business?

It is interesting how the topics we are asked about ebb and flow with changes in regulation. Clearly regulation affects us all. In many cases these changes are for the best, keeping investors safe from unsavory elements that seem to have found their way into FX as well as other markets. However, all too often regulators overstep creating a situation where companies are put at a competitive disadvantage in the US vs. other legitimate jurisdictions. They fail to see the global reach internet trading offers or the potential revenue available to US companies by creating a regulatory environment that is globally fair, attractive, and competitive. They restrict new products in order to protect the exchanges (something we don't see

out of Europe or Asia) and change leverage and net capitalization levels as often as possible. Interpret vaguely written legislation to suit their argument (and often it seems budget as well) while enforcing inequitably. This has created the need for large compliance departments who often try to determine the right jurisdictional mix to facilitate their business.

We operate under the regulatory umbrella of our clients. Therefore, we avoid the need for direct regulation. The effect to Kammas is that we have found most of our new clients coming from outside of the US. As for our US clients all of their growth is non-US based as well.



Geoff Gowey

What trading platforms does Kammas use and what factors influenced that choice?

We generally work from the platform each client provides us. Many FX brokers are choosing to use Meta Trader as a front end or “client facing” platform due to its wide acceptance among retail clients. However, we find MT less attractive as a risk management platform, an opinion that is becoming more widely agreed upon. As such many Bridge and back office risk management systems and companies have been created. A prerequisite for brokers using MT and working with us is to establish a centralized risk management framework allowing for clear efficient viewing and management across any front-end platform they choose to offer. We use many and each has attractiveness to different client types. I would encourage anyone interested in adding these to contact me for a discussion.

How did you go about building your trading desk IT infrastructure and what steps have you taken to ensure that you offer minimal downtime and guaranteed continuity of services?

Our IT setup has been designed pragmatically and I suppose organically based on need at the time with room for growth. Primarily we have relied on outside consultants to assist us with design. I feel it is important to pay for quality as our machines are generally going strong all week with multiple feeds and some decent number crunching, so the average PC will not suffice. Additionally, each machine on average supports 4 monitors so the need for high-end video cards and extra memory is important to ensure performance.

Due to the nature and challenges of running a 24hr trading operation along with my main focus of hiring

top trading talent regardless of location I have decided to create a satellite office structure. As such we are well insulated from power and internet outages. Rarely are we down for longer than a few minutes. Currently the majority of our trading sites are on the east coast of the US however, we have had sites on the west coast and in Europe.

With internet speeds and technology ever improving, the need for a centralized office structure is disappearing across many industries. The key challenge is to facilitate and encourage communication, demand professionalism, and allow for natural selection to form your team... preconceptions are almost always proven wrong.

What do you see as the main challenges facing firms like Kammas who are always seeking to optimize their risk management operations, trading technology architectures and execution pathways?



Definitely strength and flexibility in design of the software. These products need to be designed by traders not programmers. All too often trading tools are built by programmers who have at best a cursory understanding of what is required. Only a few have recognized that collaboration between programmer and trader will produce the best results. As for execution pathways I know of many efforts underway focused on this area from advanced ECNs to dark pools and virtual exchanges. All will help to improve the ubiquity of these markets across various segments.

What do you consider to be the key strengths and operational advantages associated with the Kammas business model?

My concept of the virtual dealing desk, allowing firms to outsource this portion of their business, was built to accomplish a number of advantages and efficiencies. The first advantage comes in the experience of our staff. When we began I was in a unique position to assemble a team of world class traders who understand these markets because they have been infused in them for so long. Further, they work extremely well as a team sharing information openly and willingly (not the easiest accomplishment with traders). Unlike most trading operations we do not compete against each other internally, everyone participates equitably as revenues increase. I am confident that our team is second to none when compared to market making groups at any institution large or small. Because we are able to work with multiple clients simultaneously the cost each client group incurs is dramatically less than hiring a dedicated team and setting up in house trading desks. We further reduce their risk by charging a large portion of our fee as a percentage of the revenue we create. I strongly believe everyone needs to have "a dog in the fight" ...it keeps you focused on a common goal. In the end all parties win.

As the FX market continues to grow where will you be looking to explore new business opportunities for Kammas Trading in the future?

We are looking to expand by offering liquidity. Our opinion is there is an under served market segment that would benefit from greater high quality access to the OTC FX, metals and CFD markets. Of specific interest is option pricing, partially given my background I suppose. However, I believe packaged properly and in effect providing unique and reliable wholesale products for distributors to offer to their clients and managers to use with confidence. Currently we are speaking with a number of market participants to partner with for this opportunity.

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