

# Have we underestimated the growth potential of anonymous ECNs?

With Paul Arnold, EMEA Head of Sales, Euronext FX  
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**Do you think the bad press that anonymous FX trading venues have had from some quarters in the past has been unfair?**

**PA:** There may well be a mis-interpretation of the type of client sectors that traditionally use ECNs, and that there is a certain (incorrect) stigma attached to that. Certainly in days gone by, market participants were able to behave in certain a manner without fear of reprisal, and I think the FXGC and platforms like ours have done a lot to tighten up functionality and oversight processes to restrain the use of the platform for such behaviors and hopefully prevent a repeat of what's gone before. Historically ECNs have shared

strong relationships with the more technologically advanced members of the FX community who depend on the sort of robust architecture and swift response times that an ECN provides. We have the ability to exercise vigilance in monitoring behavior on our venue, and exclude any market participants (by removing them from a client's custom liquidity pool) who are not meeting the standards set by their counterparties. This is something that a CLOB would have a far harder job in doing.

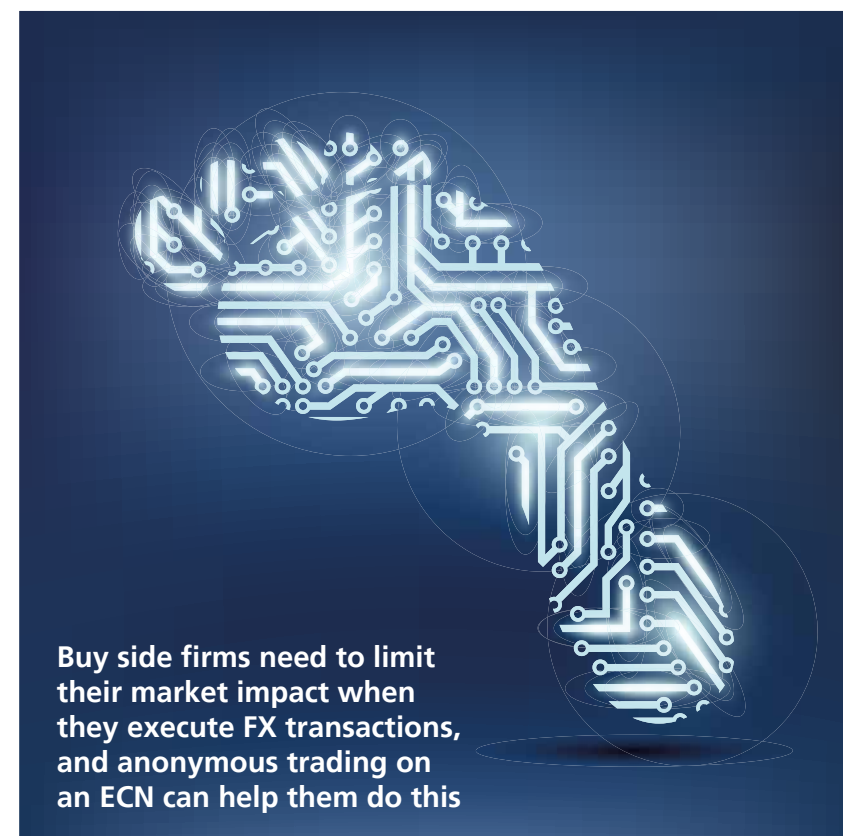
**How would you describe the clear benefits that FX ECNs can deliver?**

**PA:** Our technology is incredibly easy and quick to deploy. We may no

longer be called FastMatch, but the matching technology still carries that brand, and is still recognised to be the fastest in terms of order to ack times, but is also very flexible and reliable. We offer a fully customised trading experience for each client, tailoring much of our functionality to their individual needs, whether that's a bespoke liquidity pool for the client, only adding LPs that have certain criteria (for example, low hold times / high fill rates), to specially tuned matching logic. Our flexible matching SOR directs flow to certain LPs depending on the takers' hierarchy of execution objectives - speedy execution, high fill rate or low market impact. We understand the need for clients for a fully scalable solution,







with optionalities of a GUI or API, Firm or Last Look pricing, Full amount or Sweepable execution, and Anonymous or Disclosed interactions. By offering a full suite of choices, we can target a large cross-section of the FX community to provide cost-effective trading.

**What could alter the traditional factors for determining the relative merits of ECNs vs. disclosed pricing?**

**VS:** If the question is actually about the relative merits of anonymous versus disclosed trading then we could talk all day on the subject! But perhaps for the sake of brevity I'll focus in on one particular issue here – market impact. Buy side firms are more conscious than ever about the need to limit their market impact when they execute FX transactions, and anonymous trading on an ECN can help them do this, depending on what liquidity counterparties they may or may not have versus disclosed. Related to this is the fact

that ECNs allow market participants to access and price uncorrelated flows which they might not be able to see elsewhere because of credit restrictions.

**Why do you think that FX ECNs have not proved far more popular than they should have been given all those benefits?**

**PA:** Due to the high levels of customisation that ECNs can bring, speed of execution and the flexibility in their suite of solutions, we have witnessed a very high adoption rate from the banking community and non-bank LPs, and we find that ECNs are incredibly popular. We see that demand continue to grow as more regional banks/specialists look to ECNs and the cost benefits (in spreads, market impact, etc. ) that we can bring.

Of course, there is a reason why other sectors of the FX world have been slower to adopt ECNs, and this is due mainly to credit, since only

certain types of participants have either reciprocal credit arrangements with each other or a prime broker relationship. We are starting to see some asset managers employing prime brokers for certain funds. We may well begin to see an increase in this as regulatory challenges change the requirements to post margin. Traditionally, asset managers and large corporations, whilst keen to access the diverse liquidity only available in the ECN world, have not really been able to.

Thanks to our Sponsored Access product, clients can interact with Euronext FX by accessing a bespoke pool of liquidity via a sponsoring partner bank. Technology can be another factor - a lot of buy-side firms have complex EOMS embedded into to their daily workflow, and use GUIs to interact. Unwinding this, or adding an ECN into the mix, can add a level of complexity for the buy-side that is difficult to manage in some quarters.

**Can firms who may believe they are getting best price by trading disclosed know this with any certainty?**

**VS:** Knowing whether you're getting the best price has less to do with whether you are executing via a disclosed or anonymous channel, and more with the specific profile of a given firm and how they're executing. For example, are they trading full amount or top of book? Are they trading TWAP or RFS? There's a multiplicity of factors that need to be considered when firms are analysing whether they got the best price available, and the execution channel is just one of them. So ultimately, with carefully conducted analysis it's possible for firms to be confident that they're getting the best pricing available on both anonymous and disclosed channels.

**In theory, ECNs should be an ideal partner for the FX Global Code. Given their unique position could they have a role in helping boost disclosure of dealing standards across the LP community?**

**VS:** ECNs certainly can represent a good way for market participants to execute their FX transactions whilst also ensuring that they are completely adhering to the principles contained within the Code. But when it comes to dealing standards, I think that what's most important is that ECNs have the right liquidity management in place along with appropriate policies and procedures to ensure that all participants on the platform are adhering to the standards that have been set.

**The state of TCA and credit intermediation within the FX industry are both ripe for change. How could this play into the strengths of anonymous ECNs?**

**PA:** Client demand for transparency as well as pre- and post-trade data is definitely growing and constantly evolving with newer more innovative ideas to enhance client analytics coming to market all the time, and the recent market turmoil will only serve to accelerate this. We work closely with a number of the leading TCA and analytics firms, all of which have a slightly different (but equally effective) way of interpreting data for our mutual end clients. As we pride ourselves on our transparency, we can provide vast amounts of data to these providers, to assist in their client analytics. I'm confident that the way our clients execute their FX business, and whether their primary driver is low market impact or high fill rate – our execution data would show the benefits that using an ECN can bring. There are no hidden costs. Our clients a very low execution fee and



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a price. There is nothing 'baked in'. With regards to credit intermediation, we are still seeing the real impact of the regulatory changes around uncleared margin. Coupled with creative solutions that companies like Capitolis and Cobalt are offering in using technology to affect change in the post trade world, this could have a positive impact to place ECNs on a more level-playing field with other types of execution platforms.

**We all know that currently there is an imperfect TCA process in FX. In what ways has this reinforced the belief that the best way to get best execution is to trade disclosed?**

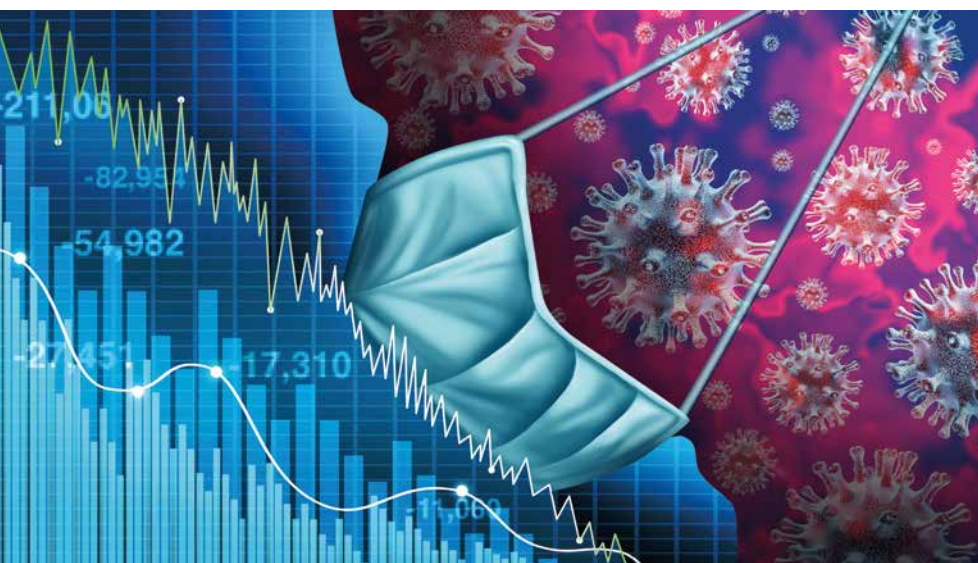
**VS:** I'm not sure that I agree the imperfect nature of TCA for FX has led to a perception that disclosed trading is more likely to result in best execution than anonymous trading. It's important to remember that the actual cost of a trade is just one aspect of best execution, and furthermore, what constitutes "best execution" can vary from client-to-client, and even from trade-to-trade, depending on what the execution objectives are to begin with. TCA is a useful, albeit imperfect,

tool for laying out the costs associated with trading via different execution channels, but ultimately it is the client's individual profile and trading objectives that will dictate which channel is the best one for them to use for a given trade. And I think that clients using TCA generally recognise this, and that's why we see so many of them wanting to have access to both anonymous and disclosed execution channels – so that they have the option to execute via either, depending on the trade that they need to get done.

**The FX market has a hugely diverse range of market participants. Why are some likely to be drawn to using FX ECNs rather than others?**

**PA:** As ECNs, to a large extent, cover only spot FX – institutions who are happy to separate their spot flow from swaps/forwards/NDFs – tend to favour ECNs as their primary destination for sourcing and distribution of liquidity. We are referring mostly here to banks, non – bank LPs, systematic funds and brokerage firms. Other participants, such as asset managers and corporates, have requirements beyond simply hedging their spot FX





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exposure, and with FX maybe not part of their core investment strategy, they will require a 'one-stop-shop' for all their FX needs. Historically these are markets where ECN solutions have been lacking, hence their preference to source pricing bilaterally directly from their panel of LPs, where fees may be incorporated into the price they pay. Again, as we've alluded to already, there is the question of credit provision. Many market participants have an appetite to receive the type of diversification and depth of liquidity that an ECN can provide but they do not have a prime broker in place to intermediate access, either for cost or workflow reasons.

#### What impact could tackling key issues such as liquidity recycling have on the popularity of ECNs?

**VS:** Liquidity recycling leads to information leakage, and so obviously the more that ECNs can do to reduce this the better the trading outcomes are likely to be for the end-users and the more popular these platforms will become. When it comes to liquidity recycling though, the challenge for ECN operators is that we simply cannot control the behaviour of market participants outside our platforms.

Which is not to say that there's nothing that can be done to improve the liquidity that clients interact with on ECNs. For example, we've invested heavily in the liquidity management services that we provide to clients, offering them analytics and the expertise of our in-house team to curate and manage custom liquidity pools. Working with the clients, we're able to analyse their trading patterns and then suggest the removal or addition of LPs in order to optimize the liquidity that they see and ensure the best possible trading outcomes for them.

#### Are there any easy ways to clearly differentiate between FX ECNs?

**PA:** Whilst there are certain similarities across many ECNs – ownership by large global Exchanges being one – we each have our own unique advantages. Our main one is well known – our speed – and our ECN remains powered by 'FastMatch Technology'. More so, our ability to offer a multitude of execution options, and a liquidity pool built specifically to client demand is something that sets us apart. We are the first spot ECN with a matching engine located in Singapore, so giving the third largest FX community the ability to access

liquidity locally with reduced round trip times, is a huge benefit. The next logical step for us is to focus on NDFs. We are in the process of seeking regulatory approval to become an RMO (Regulated Market Operator) in Singapore, and believe offering our clients the ability to access ECN NDF liquidity will hopefully continue to help differentiate us from our peers. Through the registration exemption available to MAS – approved RMOs (equivalency) - we expect that eligible U.S. companies will be able to access liquidity on our platform, notwithstanding that trading will be 'off SEF'.

#### Is the FX market saturated with ECNs or could it support even more venues?

**PA:** Fragmentation of liquidity is increasing, this is true – and we could be facing a tipping point in spot FX – especially as we now (broadly speaking) all have a similar group of clients. Fragmentation also costs money, and we've seen some large banks cut back on the amount of platforms they're connected to for distribution and consumption of FX liquidity.

Anyone new to the spot market would have to be offering a truly new USP, just offering a low transaction fee is not going to be enough on its own. I do believe there is room for competitors in other FX products. One might argue the OTC derivatives world (FX swaps/forwards, NDFs, Options) is eager for new technology solutions. Peer-to- peer is another area that is starting to gain some traction in certain quarters.

#### Volatility has recently returned to the FX market. Is this a good opportunity for ECNs to demonstrate how well they perform and how resilient they are

#### especially during periods of stress?

**PA:** I think it's fair to say that from late February through to March, volatility returned with a vengeance. FX volumes were understandably a lot higher. We saw a record quarter, record month and record day. Whilst the reason for this volatility is immensely upsetting for all, and will no doubt have a lasting impact on everyone, it has been important for us to be 'business as usual' for our clients.

Despite all of our staff working remotely, our platform has shown immense resiliency even with a huge increase in market data loads. We witnessed a slight change in the makeup of our volumes, with both anonymous and sweepable sessions gaining a greater percentage of our overall numbers. With some LPs stepping back, it can become more difficult for liquidity consumers to source their pricing bilaterally, so they seek anonymous ECN liquidity. This shows that in times of extreme volatility, a strong and robust anonymous ECN with speed at its core has a fundamental and important part to play in providing liquidity and stability to the FX ecosystem.

#### What other steps can be taken by the operators of FX ECNs to make their venues more attractive?

**VS:** To make their platform more attractive ECN operators need to create the best possible trading environment for both the liquidity providers and consumers. But what does this mean in practice?

For LPs, this means building out a diverse pool of flows for them to interact with. On 360TGTx our top 10 clients by volume include: regional banks, hedge funds (both macro and systematic), tier 1 banks, non-bank market makers and retail/HNWIs.



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This is broadly representative of the makeup of our platform, and we've exerted a lot of effort to ensure that we offer a truly diverse universe of participants for LPs to interact with. On the flipside of the equation, the differentiating factor for the consumer is how they're able to interact with the liquidity on ECNs.

There's no on-size-fits-all solution so it's important to offer clients flexibility in this regard, which is why, for example, 360TGTx allows firms to access both last look and firm liquidity on our platform, either via distinct or commingled liquidity pools. And as mentioned earlier, ECNs also need to help firms manage the liquidity that they see on their platforms – our clients have seen real benefits to our pro-active approach to creating the best liquidity streams

for them based on their individual trading objectives and requirements.

#### The 2019 Triennial Survey data illustrates the great diversity in FX trade execution choices.

#### Is it a case of lead and they will follow or do ECNs need to do much more to educate the market about their benefits and value proposition?

**VS:** Generally speaking, the people who live and breathe FX everyday as a core part of their business are very familiar with the ECN value proposition, but there is definitely a broader universe of market participants that could benefit from a greater understanding of how ECNs work, and the ways in which they might help them improve their FX execution.