



# The push-me pull-you machine

Electronic trading is hardly new. Nor for that matter is multi-asset class trading. What then has prompted the rise in popularity of stand-alone systems that claim to offer the buy-side control over the execution process?

Richard Schwartz

The EMS acronym has become so popular over the past two years that it is now falling out of favour in some quarters – a victim of its own success. But the set of functionalities that it covers remain in high demand on buy-side trading desks.

To some extent, the market for EMS or execution management systems is flourishing as a result of the buy-side's growing comfort with technology in general. "The initial spur for an independent EMS sector was the advent of FIX, which made it cheap and easy to do it," says Eric Goldberg, CEO, Portware. "People realised that by controlling the order themselves they could reduce market impact." At the

same time, having come to appreciate the advantages of an order management system (OMS) in facilitating internal information flows, the idea of automating execution management was less daunting than it might once have been. Once the trend was under way, regulatory initiatives giving value to notions of best execution could only accelerate it.

## The multi-asset spectrum

How far it has escaped individual instrument silos is another question. "If you look at the early electronic traders, many of them were from the hedge funds and prop trading groups," says Goldberg. "Since arbitrage trades were their bread and

Multi-asset EMS

butter, they could be described as multi-asset class.”

They were a clear minority, however. “There is no question that there is a cost reduction benefit from having multi-asset capabilities integrated into fewer platforms,” says Michel Finzi, global head, sales, account management and marketing, Townsend Analytics, (TAL) “but until recently the majority of buy-side strategies have been single asset class. In conversations I’ve had, the rationale for a multi-asset class EMS is more of a search for workflow simplification. Firms are willing to allow traders easy access to whatever services suit the transactions they need to undertake.”

While there are competing schools of thought on the prevalence of multi-asset class trading today, there is more obvious agreement among system vendors on the benefits of investing in future need. “We felt that what people really wanted was tight integration between asset classes,” says Stephen Grob, director of derivatives at Fidessa. “We launched an internal investment programme that looked at re-

architecting everything we did to make it multi-asset capable. We ended up with a project that was both multi- and cross-asset.”

Multi-asset and cross-asset functionality are often confused and the former is more widespread. “In the multi-asset world, you’re looking to trade different asset classes separately, but leverage one set of ‘plumbing’ and infrastructure to get operational and post-trade efficiencies including P&L and risk,” says Grob. “Cross-asset trading involves the combination of different asset classes to create synthetic products.”

Those firms with a large hedge fund client base will almost certainly aim to provide a degree of cross-asset capability. “It is quite common for our traders to trade cross-asset class,” says Nathaniel Orr-Depner, global portfolio and North American collateral manager, Lionhart, a global multi-strategy hedge fund. “We want to give ourselves protection on the downside, but also exposure to the upside.” With so many participants in similar areas across the globe, comments Orr-Depner, there’s only so much to be achieved through simple equity plays.



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*Eric Goldberg, CEO, Portware*

The sell-side meanwhile is experiencing soaring volumes and decreasing commissions, says Grob. “They are having to peddle faster and faster to make the same amount of money on each client relationship. They want to market more and more product through each relationship and leverage all the different asset classes they trade.”

This strategy is not without its operational challenges, however. One widely acknowledged problem with implementing a single multi-asset class system across an entire firm is fixed income. “It’s still a stretch whether fixed income in general can be done electronically,” says Portware’s Goldberg. “Once you get past govern-

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ment bonds, many fixed income instruments are very illiquid.”

Tom Driscoll, vice president, sales and marketing, Charles River agrees. “A number of single-asset class systems are building out multi-asset capabilities,” he observes. “I would suggest that many are underestimating the complexities. Even at a basic level, you’re talking about a vastly greater number of security types that you have to support.”

In trading different asset classes, workflows also differ. “Often the equity dealer receives an order from someone else and their job is to execute,” Driscoll explains. In the fixed income world, the same person could be responsible for

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both, changing the way compliance and audit trails are configured.

### Conceptual review

“Fundamentally, what the buy-side wants is something functionally rich, but relatively intuitive to use that allows for access to relevant execution venues,” says Finzi at TAL. The trend to multi-asset class trading is building for competitive reasons, he suggests.

“Traders’ behavioural patterns are ‘baked in’ to some extent, but they always need to respond to competition,” he says. “As the tipping point is reached, adoption will accelerate.”

The most challenging client today is often the small hedge fund, says Driscoll, “They want all the tools of the largest organisation, they want it fast, they want it inexpensive and they often lack a supporting IT infrastructure,” he notes. As a result, the vendor is expected to provide greater levels of support.

“The question we spend a lot of time on is how to simplify something that is essentially complicated,” says Finzi. “Aggregating an increasing number of data points on a blotter in a useable way is a challenge, for

example. We have to balance functionality and ease of use.”

Buy-side desks considering the introduction of an EMS should consider a further factor, says Richard Balarkas, head of Advanced Execution Services (AES) sales at Credit Suisse. “If I were giving general advice to a buy-side client, I’d say, get something you can remove without too much difficulty.”

That may seem a strange way to approach a purchasing decision. However, he suggests, a lot of desktop technology for the buy-side, EMS is provided by small companies, often in phases of impressive growth, being pulled in many directions. “They can experience rapid expansion, which they do not have the resources to sustain,” says Balarkas. “If you see something that works for you today, that’s great, but think about replacement scenarios.”

### The network route

The dilemma of being locked in to a specific execution technology can be eased by exploring API solutions, argues Scott Kurland, senior managing director, ESP, an institutional broker and applica-

tion service provider with both buy- and sell-side clients. While ESP does not offer its own EMS, the firm has integrated 16 EMS with its network. By utilising ESP's Central Counterparty Clearing™ Service in conjunction with an EMS, institutional clients are free to stage an order from their OMS without needing to pre-specify a particular executing broker or strategy, says Kurland. EMS platforms can be accessed either remotely or via an onsite installation with or without an OMS. "Most of the EMS supported by ESP are compatible with both leading and proprietary OMS systems," he explains. "Clients can choose to use more than one EMS system from ESP, tailored to each trader or trading unit's particular needs; there are no switching costs, set-up fees, or long-term contractual lock-ins for any one particular EMS."

**Broker neutrality**

ESP's network is broker-neutral, insists Kurland, providing routing to over 23 brokers for algorithmic, DMA, dark pool and cash desk trading. "All of the EMS vendors integrated with the ESP network are

able to offer ESP's multi-broker, neutral routing access," he says.

The emphasis given to 'multi-broker' and 'broker-neutral' approaches will vary among providers and the terms are not interchangeable. One does not necessarily imply the other. Even broker-owned EMS increasingly offer multi-broker connectivity, however. Goldman Sachs, for example, recently extended the functionality of its REDIPlus multi-broker EMS in Europe to allow users to route orders to other brokers' algorithms – a feature its US clients have enjoyed since late last year. "We added the algorithmic functionality into the REDIPlus multi-broker service, as our objective is to enable clients to route and trade from a single front end," says Brad Hunt, managing director and head of Electronic Transaction Services in Europe for Goldman Sachs. Clients are increasing the amounts and types of business they trade electronically, he notes, and although they maintain multiple broker relationships, it is simply not efficient to use multiple systems.

At the same time, says Grob, a buy-side desk does not want to be beholden to



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one broker receiving all its flow. "As their trading styles become more sophisticated, traders want to have one monitor on their desk that's multi-channelled. This opens the way for broker-neutral networks like ours that are completely agnostic as to which buy-side firms are connecting to which sell-side."

The extent to which broker-neutrality is or should be an explicit feature of a multi-broker EMS remains a subject of debate. "Brokers subsidise their software, since a key component to any system is to get flow into their prop pipe to allow internal hidden liquidity pools to take advantage of flow," one head trader at a buy-side firm told The TRADE. This is not necessarily an obstacle to achieving



best execution, he acknowledges. “It is just that there are many different providers of alternate pools of liquidity and it is difficult to access them efficiently through a single broker system. It also invalidates your TCA somewhat; you cannot say your slippage report applies to the market in general as you don’t execute with a wide enough cross-section of market participants.”

### Pricing models

The less a buy-side firm wants to pay to install and maintain an EMS with the requisite integration to its internal systems, the more willing it may be to rely on broker-provided systems. Whether or not such a system is ‘neutral’ may be less of a concern.

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Even third party independent systems have different cost implications for the users. Given the buy-side’s lingering aversion to paying for functionality, there are, broadly speaking, two models of revenue collection for third-party EMS. Either the sell-side pays what is essentially a subscription to the EMS provider for screen space, regardless of related transaction flow or they pay an *ad valorem* fee on flow channelled to them through the EMS.

The latter approach rangles somewhat with Balarkas. “How would you feel if we did business over the phone and the telecom provider’s charges were based on a cut of the business we do?” he asks.

Given the range of sophisticated options now available from EMS systems with apparently similar features, a buy-side firm’s choice of execution tools may ultimately depend on the faces behind the name. “There’s no shortage of technology and electronic tools available to traders, but I also think you need to have the personal relationships in place to leverage that,” one cross-asset trader told *The TRADE*. “I would never rely purely on technology.” ■

