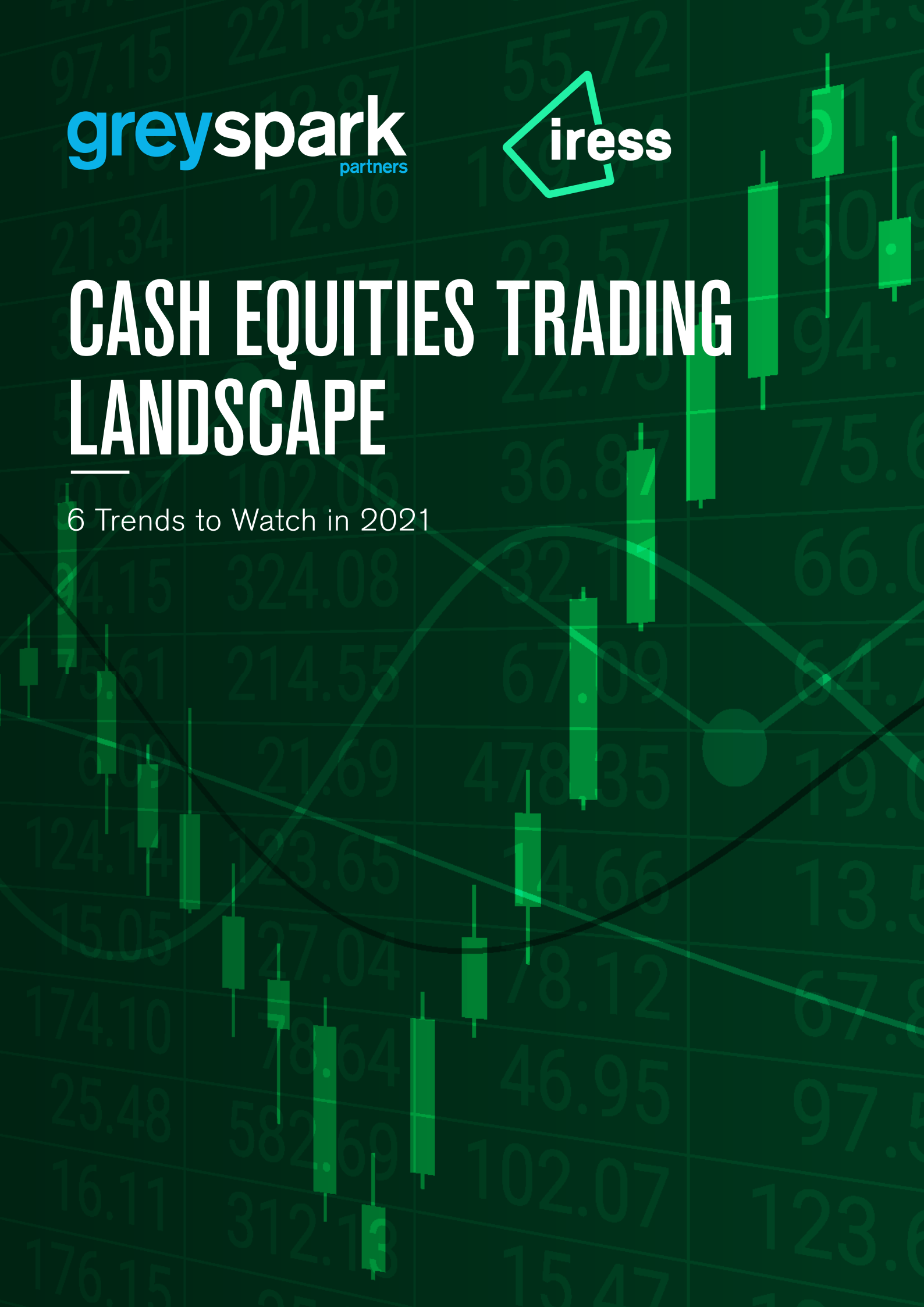


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CASH EQUITIES TRADING LANDSCAPE

6 Trends to Watch in 2021



Cash Equities Trading Landscape: 6 Trends to Watch in 2021

Over the last decade, cash equities trading has experienced a high degree of technological and business consolidation, driven by the downward pressure on margins in cash equities brokerage. Consequently, trading in cash equities is becoming progressively more competitive and less profitable. To remain viable, agency-brokerage franchises have been forced to commit to a more judicious and proactive technology strategy. Historically, it has been relatively common for agency-brokerage houses to run numerous OEMS and middle office instances across the organization, and for many, addressing the splintered nature of their front-to-back cash equities trading stack is now an important business imperative.

One major reason for the widespread development of fractured trading technology stacks was the emergence of the low-touch trading desk as a distinctive entity from progenitor high-touch trading practices. The low-touch trading approach offered agency-brokerage franchises the opportunity to automate trading and reduce trader headcounts. Automation of flow subsequently led to the emergence of a separate, more technically sophisticated set of functional and business requirements for OEMS products.

The effectiveness of high-touch trading practices is more dependent than low-touch on the end-usability and configurability factors of an OEMS – especially, across the sales trader workflow. Functionality of critical importance can include blotter filtering capabilities, manual order capture and the allocation of trades from proprietary books to client orders to name but a few. However, while many of these functionalities are technologically simple from a contemporary perspective, taken in their totality, they can weigh heavily on the usability of the OEMS by a high-touch trading desk.

Whereas high-touch trading desks place greater emphasis on configurability factors, low-touch trading desks prioritise more advanced order-routing capabilities that enable the franchise to offer automated and white-labelled algo services to clients. Indeed, the ability to construct and manage order-routing workflows and algo mapping in the front-end is a sought-after capability by agency brokers and is a key differentiating factor amongst OEMS vendors.

The different approaches taken to connectivity services by high- and low-touch trading desks also meant a distinct splintering of processes. By design, low-touch platforms have required connectivity services to manage FIX-enabled order flow and so

have adopted FIX connectivity for inbound order flow earlier than high-touch trading desks. Although high-touch desks do use FIX-connectivity, a non-trivial portion of inbound order flow is still received on spreadsheets in cash equities.

Six Ways in Which the Trading Platform Landscape is Changing in 2021

Now they are past the most challenging year in living memory, buy-side and sell-side firms can begin to consider accelerating trends in the trading technology landscape. GreySpark has identified six trends that buy-side and sell-side firms need to have front of mind at the start of 2021.

Trend 1: High- / Low-touch Technology Stack Consolidation

The duality of technology and processes for trading, the development of which is described above, is in full-scale retreat in 2021, as cash equities and equity derivatives broking franchises move to consolidate trading desks onto group-wide front-office technology platforms. It is worth noting that this consolidation does not appear to be happening cross-asset class – between cash equity and equity derivatives, for instance – but rather within asset classes. The driver of this technology stack consolidation is simple; margins are tightening, making cash equities broking businesses progressively less profitable. As such, there are renewed efforts to force down fixed costs, specifically technology and market data expenditure.

Trend 2: The Acquisition and Assimilation of Competitors

In part, to combat diminishing margins, the largest broking franchises have in recent years been pursuing aggressive expansionist policies and are acquiring smaller brokers in similar markets. In tandem, a strict technology consolidation strategy is being followed that can be broken down into three stages:

1. Expand market share by acquiring smaller broking franchises trading in the same asset class but whose client bases are strongest in regions new to the acquiring broker.
2. Reduce costs by jettisoning the acquisitions' middle- and back-office trade processing divisions and replacing them with the shared trade processing utilities of the acquirer.
3. Middle- and back-office integrations are followed by the integration of the acquisitions' front-office trading platforms (OEMS, deal capture systems, etc) onto a solitary vendor product.

Given these two trends, to consolidate high- and low-touch trading technology and the unification of technology across parent organisations, it is unsurprising that OEMS platforms are becoming more multi-purpose in their orientation.

Trend 3: The Push-Pull of Partnerships

Two factors have played a strong influence in the state of the technology landscape in 2020: First, the decision by Bloomberg to decommission SSEOMS, its OEMS offering; and second, the high levels of disillusionment that many firms are experiencing with their current provider, both from a commercial and functional perspective. These two factors have led to numerous firms reconsidering their front-office trading technology architecture. In this context, vendor products that can deliver both strong functionality across different cash equities trading functions and middle-office trade processing capabilities are likely to be in high demand.

Trend 4: Automation, Automation Everywhere

One of the sustained trends over the last decade is for cash equities trading to become increasingly automated. In practice, this means there will be a growing demand for more sophisticated front-end configurability of algo management, smart order routing and DMA flow. And yet, even though high-touch desks are an increasingly rarefied presence in cash equities brokerage, they continue to be non-trivial from a revenue perspective, often retaining a few remaining high-volume / high-revenue clients with which they have long-established relationships. So, despite automation and consolidation of trading processes and technology, it appears that high-touch trading desks will continue to be a consideration from a platform provisioning perspective for the foreseeable future.

Trend 5: Post-trade Processing: Your Time is Now

Post-trade processing is a realm that many OEMS vendors have neglected in favour of investment in front-office trading functionality. The Omgeo central trade manager (CTM) has become the de facto utility that buy-side and sell-side firms use to communicate and allocate cash equities trades. The integration of OEMS' with CTM will increasingly become a hygiene factor in 2021, a point that OEMS vendors discount at their peril. The slow tipping of the power balance away from the sell-side toward the buy-side has allowed the latter to become more expansive in their demand for post-trade services. Consequently, agency brokers are being forced to invest in more sophisticated trade-processing middleware, including greater functionality for trade confirmations.

Trend 6: Pre-trade Risk Management in the OEMS

Another area that has seen a resurgence of interest – from the buy-side and sell-side – and investment – by OEMS vendors – in recent years is the risk management / trade controls spaces. OEMS platforms have not historically incorporated the capabilities to undertake pre-trade risk assessment or to manage and view real-time risk analyses and, as a result, trades are done without a full view of the implicit post-trade, particularly settlement risk involved. Most sophisticated OEMS platforms have risk management functionality limited to the ability to set risk controls on a variety of different parameters or to take feeds directly from credit management systems. Given the rising portion of automated trading flow that contemporary OEMS systems manage, there is an increasing need for competent risk frameworks that provide more effective and timelier alerts for relevant stakeholders. Given that OEMS are already able to integrate with credit risk management systems, an area of future exploration for vendors will be the development of functionality to view and manage intraday settlement risk with specific accounts from the OEMS.

Roll On 2021

Given the consolidations of cash equities brokerage franchises and the trend for high-touch and low-touch desks to share front-office technology, vendors that offer a balanced OEMS product, with deep functionality in all low-touch, high-touch trading and middle-office functions have the most to gain in 2021. The industry-wide pressures to embrace front-office trading technology consolidation are forcing market participants to confront stark trade-offs. Namely, which features and functions are to be prioritised as a larger share of cash equities trading forms – market making and liquidity provisioning, high-touch agency trading, basket order trading and pairs trading – are subsumed onto the same platform. Very few vendor products excel in all these areas, not least when the rising importance of middle-office trade processing is also included in the assessment.

Given the compromises and intersecting business requirements that bear on vendor selections, it is likely that agency brokers will have to embrace longer platform implementations with more intensive functionality remediation programmes. Costs associated with implementations can spiral; temporary dual-vendor costs and consultancy and contractor fees, for instance. However, if cost-saving consolidation programmes are to bear fruit, market participants must ensure that their selected vendor partners can credibly deliver the functionality to bridge the increasingly wide terrain that OEMS products cover today.