FX TCA and Benchmarking

July 7th 2014
Agenda

• TCA overview
• Role TCA plays in the execution lifecycle
• Benchmark overview
• Benchmark developments
FX TCA Overview

• Why is use increasing in FX?
  − Investor pressure responding to market developments e.g. WMR
  − Aggregation of central dealing desks, often managed by Heads of Trading with equity backgrounds
  − Pressure on returns
  − Response to potential regulatory developments

• What is available in the market?
  − 3rd party independent providers, e.g. ITG, FX Transparency, New Change FX
  − Platform providers, e.g. Bloomberg, Trading Screen
  − Bank services

• N.B. main focus is on post-trade TCA, limited availability of pre-trade analytics
Role of TCA in Execution Lifecycle

Individual Transaction
Pre-Trade

Feedback to improved pre-trade analysis, changing execution approach and more informed decision making

Execution
Real-time monitoring

Multiple Transactions
Historical Analysis
Post-Trade
Strategic

Individual Transaction
Immediate Post-Trade
Tactical

Source: Morgan Stanley QSI
Benchmark Overview

1. Theoretical
   - Fair value risk transfer

2. Observed
   - Interval based, e.g.
     - TWAP
     - VWAP
   - Point in time, e.g.
     - WMR
     - Arrival Price

3. Experience based
   - Peer group analysis

Issues:
- Data source
- Underlying trade objective
- Representative
- Independence
- Revaluation point vs execution benchmark

Source: Morgan Stanley QSI
Benchmark Developments

- Key to align benchmark with trading objective
- No one size fits all solution, multiple benchmarks required
- Clients broadly segmented as follows:
  1) **WMR** with limited or no discretion (i.e. passive managers who are tracking indices such as MSCI which use WMR)
  2) Asset managers trading FX as a utility to buy/sell international securities, increasingly moving towards benchmarks such as **TWAP/VWAP** where the interval approximately matches the trading period of the underlying security
  3) Asset managers trading FX as an asset class, increasingly using **Arrival Price** as key benchmark
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