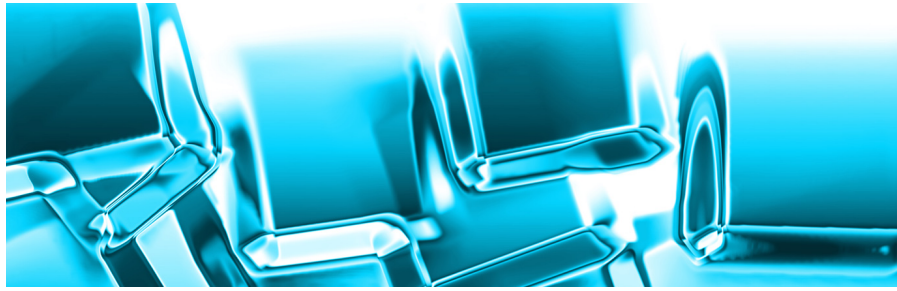


FIX & FX



By **Jay Hurley**,
Vice President Fixed Income, Morgan Stanley

The FPL Global FX Committee was formed a year ago in response to the needs of the FX community to enhance the FIX Protocol to fully support FX as an asset class. The efforts of the FX community recently culminated in the approval of the Phase I FIX FX Technical Gap Analysis. The primary purpose of Phase I was to enhance FIX 4.4 to improve support for FX products and produce a standard implementation as a reference for the buy side, sell side and vendors. This will assist those who are already using FIX for FX with versions ranging from 4.2 to 4.4 and for those who are planning to move from proprietary protocols to FIX.

The Phase I FX Technical Gap Analysis covers the FX products that are most commonly being traded electronically:

- Streaming Prices for spot and outright forwards.
- Quotes for spot, outright forwards and FX Swaps.
- Orders and Executions for spot, outright forwards and FX Swaps.
- Vanilla FX OTC spot options (post trade) Trade Capture.

The gap analysis was conducted with the interaction between clients and banks/dealers as the primary model, therefore, interaction models between clients and FX marketplaces or trading platforms have not yet been fully explored. This is an area that will be covered in more depth as part of Phase II. The focus was on the two primary interaction methods: Request For Quote (RFQs) and Dealable Streaming Prices (DSPs).

Request for Quote

RFQs mimic the traditional phone trading model. A client asks one or more dealers for a one or two way price for a specific currency pair, size and date, for example, a two way price for 10 million EUR/USD for spot. The dealer(s) respond with a quote which the client can deal on or pass. During the short time frame of the interaction, the market price may move causing the dealer to update the quote to the client. The FX community decided that this was best represented using the quote message set: Quote Request (35=R), Quote Request Reject (35=AG), Quote (35=S), Quote Response (35=AJ), Quote

Cancel (35=Z) with New Order Single (35=D) and New Order Multileg (35=AB) being the request to deal and Execution Report (35=8) for order status information. This model also fits in with retail customers who are often given a "one off" quote for a fixed period of time which is not updated. This model is implemented by omitting expire time in the quote request which implies that a single quote is required rather than quotes for short periods of time.

Substantial additions were made to the Quote message to support the trading of swaps including four new tags:

- | | |
|-------------------------|---------------------------|
| 1) BidSwapPoints, | 2) OfferSwapPoints, |
| 3) LegBidForwardPoints, | 4) LegOfferForwardPoints. |

Matching additions were made to New Order Multileg - SwapPoints and Execution Report - LastSwapPoints and

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Leg Last ForwardPoints. These changes will allow swaps to be fully supported and removes the need for custom tags.

Streaming Prices

High frequency clients often want a continual stream of prices that they can trade on rather than making a lot of request for quotes. There was a lot of debate regarding the modelling of this flow which has only become possible with the move to electronic trading in FX. This model is called Dealable Streaming Prices (DSPs) or Executable Streaming Prices (ESPs) and the community decision was to represent this using the Market Data message set. One advantage that market data messages have over quote messages is that there are several FX trading platforms that currently disseminate tradeable prices using FIX market data messages and this can be easily combined with FIX market data direct from dealers to give clients a consolidated view of a fragmented market. Market data also has efficiency benefits

where the correct use of incremental updates will greatly reduce network bandwidth, which is especially important for clients using VPN connectivity. The FAST(sm) compression, which is targeted at market data messages, will provide further efficiency gains in the future as this becomes more common.

Brokerage charges in FX are often different for liquidity providers vs. liquidity takers i.e. whether the order was passive or aggressive. For example, providing liquidity is often free or lower cost than taking liquidity because this creates greater market depth which encourages clients to trade on the platform. A boolean Aggressor Indicator tag has been added to the Execution Reports message type so that trade costs can be calculated.

Phase II FX Gap Analysis

The Global FX Committee recently voted on the priorities for the Phase II FIX FX Gap Analysis. The preliminary results indicated that the top priority is the post trade workflow to enable the buy side to efficiently send allocations to the

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sell side. At the recent EMEA quarterly meeting, there was a comment by a member of the audience from operations regarding the low operational efficiency of FX post trade which is often handled manually, or in a semi-automatic way by emails and spreadsheets. In the high volume, low margin spot and forward businesses, operational efficiency will have a big impact on the bottom line and the GFXC will continue to focus on areas considered most important by the FX community.

Negotiation for FX swaps and multileg products is the next item on the list. This will support complex work flow where there may be automatic negotiation of, for example, the spot rate of a swap where the outright rate may not change but the spot and forward point components may be negotiated. Non-deliverable forwards (NDFs), that were part of the list for Phase I but were delayed, will also be part of Phase II. The increased significance of some currency pairs, for example, Chinese Yuan and Korean Won, which are important for trade, but have restricted trading, means that it is important for FIX to fully support electronically trading of NDFs. NDF trading will be covered using the quote model including negotiation and using the streaming prices model for simpler flows.

Clients, especially those that trade in the high frequency space, normally have prime brokerage relationships which provide credit for taking positions. This workflow of prime brokerage allocations and give-ups between customer, executing broker and prime broker will be included in the FIX Protocol to expand its post trade capabilities for FX.

ECNs, exchange style platforms and portals for trading FX

and their workflows will also be covered in more depth in Phase II. The Global FX Committee membership has recently expanded with representatives from several ECNs, an exchange style platform and a portal joining. This increased participation will enable the committee to go beyond the client to dealer interaction model covered in Phase I.

The final item for Phase II is Single Spot Portfolios (SSPs) which is part of the TWIST collaboration. This enables a corporate client to lock in a spot rate and then split the original deal into a collection of forward trades which are all priced by the original dealer.

The remaining items on the plan will be delayed to Phase III which will be tackled in early 2007. These are:

- Further discussion of one-cancels-other functionality and whether this belongs in the protocol specification and if so, whether it should be part of the FX gap analysis or the Algorithmic Trading Working group.
- Blotter or list trading and how to convey groups of FX orders which could be priced more efficiently as a group rather than individually.
- Reference data including static price dissemination for exchange sourced settlement prices and for spot, forward and swap instrument definitions.
- In the post trade area, there is a proposal for a new message type to represent settlement obligations which is under active discussion.
- Also, as part of the FPL's FX collaboration with TWIST and ISDA/FpML, an investigation into the use of FIX for confirmation of terminations or increases.

A recent survey showed that FX trading volumes have surged by 39% in the past year with turnover in New York up by 31.5% in the same period. The surge in volumes has been attributed to the continuing emergence of foreign exchange

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as an asset class in its own right, the onward march of the hedge fund, higher volatility across all asset classes, rising global imbalances and the expansion of electronic trading platforms. I expect FIX to be a major contributor to the growth in FX electronic trading as the FX community pushes forward with implementing the Phase I enhancements and increases its involvement as Phase II gets underway.

Any thoughts on this or other articles?
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