



It's sales trading, but not as we know it

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Mark Northwood



Dan Miller

While some may innovate and develop electronic trading technology and solutions, others get on and use it. The buy-side dealers, sell-side traders and sales traders are 'living the electronic trading dream' and have first hand experience of the changes brought about by the various forms of electronic trading. They are also the ones looking at the changing landscape and trying to identify how they may fit into it in the future. Edward Mangles from *FIXGlobal* and Christopher Prosper from executive search firm St.George's Harvey Nash ask a group of senior dealers and sales traders what their thoughts are on their current responsibilities and how they see their job roles developing in the future.

Today's professionals have had varied early experiences with electronic trading; some positive, others frustrating. As Dan Miller, Head of Sales Trading for Global Emerging Markets at Deutsche Bank comments, "I started electronic trading back in 1998. The firm I was at was quite keen to develop an execution only DMA platform for the region. Unfortunately, they were four years too early for the bulk of the buy-side client base." Mark Northwood, Director of Trading, Asia Pac, at Fidelity Investments recalls that his initial forays into using electronic trading were driven more by expedience. As he comments, "I did my first buy-side 'DMA' trades through Instinet back in 1998. This seemed a great way to implement my own active strategy without the need for external communication." Similarly, Johnny Heng, Head of Global Equities Trading at Government of Singapore Investment Corporation (GIC), found he could create efficiency through early adoption of electronic trading; "I started working in the world of electronic trading when I began my trading career in the foreign exchange spot market with my previous firm. That was in the mid-90s. So, when I moved to GIC to trade equities, using the Electronic Communication Network (ECNs) was something very natural for me." He further recalls, "I was the heaviest user of ECNs, especially when I was running North American trading in our New York office. That also coincided with the NASDAQ bubble where I found it more efficient trading electronically on my own than depend on the NASDAQ dealers."

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Since those initial forays into the use and exploitation of electronic trading opportunities, effective implementation of technology and standards such as FIX have become accepted as part of everyday life for dealers and traders. This adoption of electronic execution has led to buy-side clients forcing a change in the priorities and responsibilities associated with the sales trader's role. Dan Miller comments, "clients want the benefits of electronic execution. They want live electronic updates, DMA, algorithmic trading, and faster electronic confirmations. We

on the sell-side need to stay in front of our clients' changing execution needs. In my role, I now spend much more time in IT meetings determining priorities of connectivity and order management projects." As a Regional Head of Sales Trading from another global investment bank also comments, "Traders now spend a lot of time talking to clients. With the automation of the execution process, time-consuming tasks, like performing downloads from the OMS, are eradicated. Electronic trading technology and FIX have finally brought about a transformation in the way we do business that's been necessary for a while now." GIC's Johnny Heng agrees, "For our counter parties, our use of electronic trading helps to reduce the number of 'touch points' we have with them. That way, they can have their limited resources focus on areas of coverage that adds most value to us." As another Regional Head of Sales Trading from a global sell-side firm adds, "With the nature of electronic trading in sales and execution, we are seeing a much higher level of efficiency in the market place. People involved in manual processes are being forced to justify their methods and processes. In comparison to those using electronic trading, they are definitely seen as lagging behind." Implicit with these manual processes (versus automation), is a higher operational cost. Johnny Heng comments that he sees electronic trading as an important component for maintaining sell-side execution service profitability; "our greater use of electronic trading helps our counter parties maintain an acceptable level of profitability with our firm, against the backdrop of falling commission rates and revenue across the industry."

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Naturally, many of the sell-side benefits equally apply to the buy-side. Johnny Heng makes the point, "Harnessing electronic trading has allowed our traders to focus less on the mechanical aspects of trading. Our traders can better focus on providing value-added services to our portfolio managers and analysts. More time can now be afforded for trading of large orders as well as those that demand greater attention."

That said, there are obviously some implications that the buy-side may not be so comfortable with. Fidelity's Mark Northwood explains, "Electronic trading is a double-edged sword for me. On the one hand it offers increased productivity, lower explicit and (we believe) implicit costs, as well as greater stealth in trading. However, this is offset by greater execution and regulatory risk being borne on the buy-side of the pitch, together with the need for increased spend on resources and systems if DMA is contemplated."

So how is this all going to impact the work that dealers and traders will be doing in the future? From a buy-side perspective, Mark Northwood is clear. "My role becomes more focused on technology, risk management and evaluating new product offerings as they become available. It is also more involved with working with regional regulators and exchanges to ensure the playing field suits the requirements of large institutional investors. Our relationship with brokers will evolve as well, with the roles blending further, and new services becoming more important: block trade facilitation, derivatives as well as FIX based systems interaction." This shift in the relationship between the buy and sell-sides requires that traders will continue to adapt their job roles and skill sets. Mark Northwood continues, "Clearly a high level of comfort with technology is central to traders on both sides. We are all spending less time on the administrative part of the trade process as the communication of order and settlement information from Portfolio Managers to Custodians happens electronically over FIX and other electronic systems. Traders will be expected to utilise this 'free' time to monitor activity in their stocks even more closely and direct order flow down appropriate channels while setting trade strategy even more actively." Others would seem to agree that the impact of electronic trading will necessitate buy-side traders having even more dynamic skill sets. Johnny Heng goes into detail, "Looking ahead, a GIC trader will be able to fully embrace straight through processing, right from pre-trade to post trade settlement. The GIC trader would have an order management system that can generate pre-trade analyses of all orders. He would use the analysis to choose the appropriate trading strategy for each order. Orders fitting the size profile for direct market access will by-pass the traders to be auto-executed through DMA while mid-size orders will be directed by the trader to the appropriate algorithmic trading platform. What will be left would be the remaining 10 - 20% of the orders that typically make up

close to 70 - 80% of the value of all orders. I expect liquidity to be further fragmented as the advent of algorithmic trading will see orders migrating upstairs. The trader would be spending time sourcing liquidity for the latter type of orders as well as providing more value-added services to our PMs and analysts."

Deutsche Bank's Dan Miller sees the sell-side trader's future in a similar light, "Actually, a good electronic trading platform will help sales traders spend more time on productive work. Order clerking will diminish while selling trading ideas and giving better timing advice will become a bigger part of the day. The quality of service to both mutual and the increasing number of hedge funds will improve."

That said, this may present a major challenge to some of those involved in the world of securities trading. One sales trading veteran comments, "this will leave a lot of people behind. Our jobs are traditionally more process oriented. Electronic Trading completely changes the way traders do their job. DMA now allows clients to manage small orders by themselves, while traders are more focused on the big investments. Sales traders roles to do both sales and research will blossom."

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A harsher reality may await those who don't or can't adapt, or as a Regional Head of Sales Trading based in Hong Kong puts it; "as clients start taking up much greater responsibilities in their trades, a lot of middlemen are either going to have to move to a more sales oriented approach or get booted out of the industry." Dan Miller offers more a detailed set of required skills, "Sales traders will be expected to analyse global macro shifts in equity, fixed income, forex and be able to understand the country/sector impact on their markets. They will also be expected to understand and trade single stock as well as indexed derivatives. Clients will not only expect advise on stock picking and timing, but which instrument (cash

equity, swap, option, structured product, credit default swap) gives them the best exposure to the name.” When considering his sell-side counter parties’ future roles, Johnny Heng comments, “I would add that gone would be the days when we have cash sales traders, derivative sales traders, etc. Each sales trader is expected to possess multi-product competence. Each client is likely to have access to just one, no more than two human touch points. The sales trader is also expected to be equally competent in inter-market events. Program trading sales will be taken over by algorithmic trading platforms which clients can access directly.”

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Of course, there are many possibilities for a shift in the Sales Trading function. As one Regional Head of Sales Trading suggests, “traders will go to the buy-side. With the way the methodologies and processes in the business are shaping up, traders will be able to pull the trigger while being on the buy-side.” Others would seem to agree with this shift in the function from sell-side to buy-side. Johnny Heng comments, “I expect the distribution / sales channel of the equities business to shrink over time. This makes it necessary for the buy-side trader to additionally play the “sales trader” role to his internal PMs and analysts.”

The implications of all these changes are far reaching. The ways in which job functions have and continue to change are naturally all in the context of the market as a whole. Fidelity’s Mark Northwood predicts, “As Asian markets become more institutionalised, trading styles will change. Block trading will become more common, embracing book-builds and (I hope) ECN crossings. The use of algorithmic trading tools will likely be a specialised area, probably embracing derivatives and other quant disciplines. A significant proportion of trades will use this channel in pursuit of the most cost-effective ways to capture exchange liquidity. There will be a move away from VWAP trading and ‘broking’ will re-emerge as a core function of sales-traders, as the buy-side uses more discretion on liquidity/price priorities. Regulatory pressures will mean execution becomes an increasingly specialised function with the cost structures under scrutiny. Work towards understanding how unbundling of the different elements of the sell-side service could occur has already begun.”

In this context, the sales traders of today are increasingly being forced into a race with their counterparts in competing firms and possibly with his own clients, to provide more advanced (and cheaper) trade execution, timely market insight and a clear understanding of clients’ ever evolving requirements. Too much to ask? In the fast moving and unforgiving world of electronic trading, it is likely to be ‘shape up or ship out’. **FIX**

Any thoughts on this or other articles?

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