Buyside Looks to Shift Currency Trading onto Exchanges

John D'Antona Jr.

The $5.3 trillion dollar foreign exchange market, which now mostly trades among a smattering of banks and dark venues, could migrate to the exchanges if the buyside has its way.

The growing 24/7/365 forex marketplace has seen growth as more asset managers look to the asset class as a source of alpha and hedging, thus the push for more public trading of currencies, according to a recent Reuters article. More public trading, like in equities, is hoped to bring more transparency, liquidity and better pricing to the now opaque market.

Like the fixed-income markets which also have traded non-publicly, currencies have seen more recent regulatory scrutiny with regards to pricing, fees and manipulation. The buyside, much like in equities, wants to see a fairer marketplace where they can get best execution.

"We are talking to people who are planning to shift 10-20 percent of their portfolios to some form of exchange-based or cleared trading if only to see how it goes," Peter Jerrom, who has launched a new broking operation matching orders for certain types of derivatives at London-based Sigma Broking, told Reuters. "There is a shift that is a reflection of how much people have become tired of a variety of issues with the banks."

As a sign of this move away from the darker trading venues and banks was the recent purchase of FX trading exchange Hotspot by BATS Trading from KCG for $365 million. The deal is expected to close this spring. NASDAQ and Eurex are also making moves into the forex mart.

Sellside traders have told Traders that the $2 trillion spot trading markets will likely continue to be traded via telephony or through other high-touch methods.

"All of the big exchanges are looking at this space now," David Mercer, chief executive officer of LMAX, a "multilateral trading facility" (MTF), told Reuters.

Pragma Securities recently told Traders that it was developing algorithms for currencies, further evidence of the sector's growth and move towards organized exchange-based trading.

Traders have told Traders the tough part of moving forex trading to exchanges would be the brokerages and banks, as they control so much of the order flow. One trader said that five banks control upwards of 65 percent of forex trading and for them to release their grip on trading would be akin to "getting a baby to give up its bottle."