



The Development of Trading Technology for Latin America

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Increasing political stability, greater levels of consumer affluence and international interest in the potential value of its natural resources and commodities are placing the countries of Latin America (LATAM) on the trading map. Research from Kimsey Consulting has shown that between 2009 and 2012, the region can expect the largest global increase in firms with trading operations, on both the buy-side and sell-side. Of course, the relative lack of development in the LATAM financial markets to date, as compared to North America and Europe, highlights why there is proportionally such a potential for growth.

Since technology takes such a central role in the development of wholesale markets, the rate of growth in the market value of trading technology is similarly expected to be significant in LATAM. A rise in the number of positions on the trading floor will almost certainly be accompanied by an increase in demand for platforms to facilitate the rapid implementation of electronic trading, coherent risk management and distribution of market data.

Fidessa's firsthand experience from other regions of the world is that as markets mature, technology plays an increasingly critical role in reinforcing wholesale markets and attracting foreign investors. This drives demand for Execution Management Systems (EMSs) and Order Management Systems (OMSs), as well as tools to facilitate more advanced practices such as Direct Market Access (DMA), pairs trading, algorithmic trading and Smart Order Routing (SOR). The savvy market participants will be those that seize this opportunity and implement

sophisticated solutions that will support their trading, connectivity, market data and compliance needs, and help them gain competitive advantage. But more on that later..

The LATAM Market

An expanding middle class with attendant pension funds combined with a positive population growth trajectory, has encouraged the establishment of an investment management community and the consequent growth in both buy-side and sell-side institutions. From 2000 to 2010, access to financial services in Mexico increased from 25 to 59 percent, according to a survey conducted by the Ministry of Finance and Public Credit (SHCP).

But this is not the whole story of the region's market expansion. Another driver behind the growth in LATAM markets is the interest of foreign investors keen on seeking out new opportunities and seeing potential in the emerging region.

As one of the BRIC nations (the related economies of Brazil, Russia, India and China), Brazil has long been regarded as a potential economic powerhouse of the future. Chile has joined Mexico as a member of the Organisation for Economic Co-operation and Development (OECD)—another indication that the region is able to offer an appropriate environment for investment and investment businesses. Commodities and commodity derivatives remain a strong growth area for global trading. The lure of markets rich in natural resources combined with the reassurance offered by political and economic stability has opened up the region in the eyes of multinational banks and their investors.

If the political and economic structure of these countries is now considered stable and safe, then so too are their capital markets. The final factor in the growth of foreign interest is the improved regulation and supervision of

markets. Mexico's banking and securities regulators, including the Comisión Nacional Bancaria y de Valores (CNBV), Bolsa Mexicana de Valores (BMV), and Asociación Mexicana de Intermediarios Bursátiles (AMIB), have worked to bring the nation's corporate-governance guidelines in line with international norms. Additionally, both the banking and securities regulator of Brazil, the Comissão de Valores Mobiliários CVM, and the BM&F Bovespa are implementing regulatory and market-structure changes that will have an impact on the way exchanges and brokers operate.

That general trend has been given extra impetus by the region's weathering of the financial crisis. Broadly speaking, countries in LATAM had high levels of international reserves, manageable current account imbalances, low debt, and minimal exposure to "toxic" assets and foreign funding. Weaknesses in the US dollar, rapid growth in commodity prices and the consequent influx of capital have undoubtedly helped. Growth rates in national ETFs are an indication of recent success: The iShares MSCI Chile Index (NYSE Arca: ECH) was up 83.9% year-to-date in January 2010, while the iShares MSCI Mexico ETF (NYSE Arca: EWW) was up 57.7% over the same period.

Ratings agency Fitch also calculates a regional growth of 3.6% in 2010, after a contraction of 2.9% in 2009. The recovery is expected to be supported by a better global financial and economic environment, increases in commodity prices and more capital inflows. Fitch projects an even-faster rebound in Brazil and Chile, where growth will likely reach a minimum of 4% in 2010 as a result of recovery in consumer and business confidence. If the economic crisis can be viewed as an example of what economists term "creative destruction," then LATAM is regarded as a solid foundation for the next period of growth.



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Consequently, local brokers are looking at two distinct groups of potential customers. The first is, inevitably, foreign buy-sides who need access to local markets in the traditional manner. The second, and equally important, is foreign brokers who choose not to set up their own local establishment nor join the exchanges themselves. Their wish is to route orders to partners who are member brokers, and by so doing, gain access to LATAM markets for their clients. In addition, these local brokers are also keen to expand and enhance the range of services they can offer to other local players as well as to the international community.

In this market it is clear that technology plays a critical role. An EMS that enables traders to work on orders directly and interact with liquidity in the market is the minimum technological requirement, along with FIX (Financial Information eXchange) connectivity to both the exchanges and to buy-side and sell-side customers. But as the countries of LATAM take their place on the global trading stage, and the pool of competitors gets broader and deeper, greater levels of sophistication will be required.

Brazil, Mexico and Chile

Of course, these broad brushstrokes about the LATAM region hide some important differences in the capital markets of each Latin American country, as well as the level of technological adoption seen.

In Brazil, where local firms are well-established, the use of at least a basic EMS is fairly common. But following the merger between the BM&F and Bovespa exchanges, the new firm BM&FBovespa is focusing on unifying its two disparate technological platforms into one. In general, old technologies and platforms are being replaced with more modern and often FIX-based alternatives, and a new unified gateway and market data feed are planned. High-frequency and algorithmic trading are of the most

interest and importance in Brazil, as compared to Mexico, where pairs, basket and algorithmic trading is growing. Mexican markets also see the highest number of market makers in ETFs in the region. The penetration of truly comprehensive trading platforms in Mexico is limited at present, but the demands of foreign investors are likely to change this going forward.

Both countries are now facing new regulations and market-structure changes. In Brazil's case, there is a high demand for DMA for equities and derivatives, which highlights the need for pre-trade compliance checks. Mexico's Circular Única de Casas de Bolsa, which contains the Comprehensive Review of Standard Operations (RINO), will significantly improve trading operations in line with international practices. It introduces new commands, agility in price formation and faster insertion and removal from positions to create an environment that is more conducive to program trading and algorithm-based operations. It will adopt standards for DMA trading and enable brokers to adopt multiple pipes to the exchange.

The new RINO changes include the:

- elimination of classification of ordinary and extraordinary orders
- use of classification of qualified and non-qualified clients
- addition of new crossing rules
- implementation of new controls for client instructions
- modification of rules regarding order prioritization and folio numbers
- establishment of rules regarding the use of specialized technical systems
- effective implementation of the role of a compliance officer on the desk

The demand to put powerful and flexible trading technology in place is

further driven by the need and desire to be able to adhere and prove conformance to these new regulations, as well as take advantage of any opportunities that they and other changes in trading practices may present.

In contrast, despite growing trading volumes, the capital markets in Chile have little reliance on technology. However, the exchange has now upgraded its electronic trading engine to accommodate increasing volumes resulting from new DMA and algorithmic flow. Fidessa has recently worked with Celfin Capital, one of the country's leading investment banks, and as part of the Celfin deal Fidessa has built a direct electronic link to the Bolsa de Comercio de Santiago, a move that will help open up the market to more international investors.

The Technology Imperative

It is here where we can return to broad brushstrokes. The LATAM markets may have their own particular features, specific regulatory issues and cultural practices, but the development of technology use will almost certainly follow the same trajectories seen in the more mature markets of North America, Europe and even Asia. We can expect the internalization already seen in foreign markets to spread, and markets to fragment as they have elsewhere. Trading between countries and cross-listing will inevitably increase. Systems for powerful, resilient order management—which can handle inbound/outbound international order routing, seek out and hit appropriate liquidity, offer comprehensive algos and basket functionality upstream of the EMS, and aid compliance—will penetrate further into the market.

If the EMS can be considered the necessary minimum for participation in electronic trading, an order management system is the requirement for sell-side firms that wish to cement their place at the



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forefront of the market.

An OMS offers users a unified platform that can collect, aggregate, cross and route international order flow, and manage multiple positions simultaneously. It enables sell-sides to issue and manage responses to IOIs (Indications Of Interest) and advertise trades—an important tool for finding both liquidity and clients.

The Fidessa OMS delivers seamless straight-through processing from order inception to trade confirmation. Its fully integrated front- and middle-office technology combines real-time electronic order management, routing and execution, trade allocations, risk/position management, compliance, reporting, market data and connectivity, allowing firms to manage their clients' orders electronically from receipt to confirmation. The Fidessa OMS also has fully integrated advanced trading tools, including pairs trading, basket trading, DMA and sponsored access tools, along with Fidessa BlueBox, Fidessa's Algorithmic Management System. Lastly, through the use of FIX and/or Fidessa's API, the OMS can be fully integrated with proprietary and third-party applications.

An OMS also supports an efficient allocation of human resources. As is becoming apparent in North America and Europe, "vanilla" trades that require little or no handling by an individual trader are increasingly dealt with automatically on a zero or low-touch basis. By leaving straightforward, non-contingent trades to the technology, traders have greater capacity to apply their skills and expertise to working up more complex and more valuable program or strategy orders.

But perhaps most importantly, there is greater harmonization with international standards among order management systems. The OMS, therefore, is an indication to prospective buy-side clients that the

sell-side firm is a well-run, well-regulated, and forward-thinking firm; a safe and trusted partner for investment. As scrutiny from regulators increases hand-in-hand with more stringent risk management requirements, this is a critical factor.

It is also the foundation of the return-on-investment calculation that must accompany any investment in technology. The simple fact is that in Mexico, Chile and Brazil (the most advanced markets in LATAM), investment in sophisticated technology pays dividends in terms of the number and value of the customers it will attract.

One notable effect of the financial crisis has been buy-side firms assessing their sell-side rosters and looking at how best to deploy their commission dollars. There may well be more international and local buy-sides operating in LATAM, but they are unlikely to have lengthy lists of broker-dealers.

In this climate, firms that can offer comprehensive functionality and a choice of algorithmic trading options, as well as the necessary membership to the appropriate venues, are inevitably more attractive. Returns can be measured in the increased volume of trades being handled. In fact, it is possible to extend this idea and state that without the technology and the functionality it offers, simply participating in the markets will become more difficult by degree.

Vendors like Fidessa are now extending functionality to adhere to regional market requirements, incorporating local market data into their trading platforms, building local market gateways and providing tools enjoyed by counterparts in other regions such as Europe, Canada, Asia and the US. Flexible technology providers are working with firms in LATAM to develop systems to meet their needs, to facilitate electronic trading and to ensure that technology plays its part in

the development of capital markets. Costly and time-consuming in-house development of proprietary systems is no longer necessary. And so the question is no longer whether a firm can afford to invest in technology, but whether it can afford not to.

About Fidessa group

Fidessa is the leading supplier of multi-asset trading, portfolio analysis, decision support, compliance, market data and connectivity solutions for firms involved in trading the world's financial markets.

Fidessa's products and services are built on the simple vision of making it easier to buy, sell and own financial assets of all types on a global basis.

Headquartered in London and with regional operations across North America, Europe, Asia and the Middle East, Fidessa supports 25,000 users across 850 clients, serving a broad spectrum of customers from major investment banks and asset managers through to specialist niche brokers and hedge funds.

Fidessa group is listed on the London Stock Exchange, has a turnover of \$380m and employs 1,500 people globally.

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