

# Why Anonymity Matters When Trading FX

## Introduction

The United States Department of Justice and other regulators announced settlements with five global banks on May 20, 2015, related to criminal charges involving misconduct in their foreign exchange trading activities. This anticipated but still shocking result is certain to impact the FX marketplace for not only the providers of liquidity (sell side) but more importantly for the liquidity takers (buy side). As a result of their guilty pleas and settlement agreements, the banks have been compelled to issue disclosure statements that clarify their future activities and behavior when acting as principal or market maker, and which provide a window into their past practices that led to criminal charges. When Cürex examines these documents, we come to a singular conclusion: anonymity is critical when trading FX. The buy side must accept the fact that in every disclosed trade they enter into, the institution that is working their order, if it is not acting strictly as an agent, has no obligation to act solely in their best interest. Given that simple truth, what steps can the buy side take to protect itself, pursue best execution and honor its fiduciary obligation to its clients and constituents?

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## Having and Making Choices

The prevalent practice of buy side FX customers is to trade bi-laterally with a banking institution with whom it has a credit relationship. Most buy side customers in fact maintain several such credit relationships to allow them to manage their credit exposure among multiple counterparties as well as to compensate their banks for other services they receive. In certain circumstances, these buy side customers execute their FX needs by using third party service providers that offer “request for quote” or “request for stream” order types. In all of these practices, the buy side customer’s identity, transaction size and interest are known to its counterparty or potential counterparties.

Over the last two decades, electronic execution networks (ECNs) have emerged as a choice for FX execution. Most traditional buy side customers have shunned the ECN execution choice because of the need to establish Prime Brokerage relationships and post credit to allow them to deal with multiple counterparties. While the traditional buy side has shunned the ECN option, hedge funds and high frequency trading firms have embraced those venues as have market makers. A minority of buy side institutions have adopted the ECN approach in the hope of achieving better pricing and anonymous execution. The majority, however, have maintained their historical market approach. The point is that the buy side has choices when executing FX but has in large part continued its status quo practice of executing its FX needs on a disclosed basis.

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## The Price of Maintaining the Status Quo

The bank settlements and disclosure documents give some sense of the potential price that the buy side has paid as a result of trading directly, on a disclosed basis, with a bank counterparty acting as principal. The cost has included undisclosed mark-ups, partial fills and orders remaining unfilled even when there were prices in the marketplace available to satisfy those limit orders. Perhaps as unsettling is the going forward disclosure that makes it clear that the banks, when acting as principal, may continue to engage in many of the same actions. In essence, the protective disclosure going forward is “buyer beware” in any circumstance when the bank is not acting as a clearly defined agent. When the bank is acting as a principal or market-maker it will and should be expected to act in its own interest. Frankly we support this disclosure and hope all buy side customers understand this market reality. The buy side has choices and an obligation to understand the impact of its trading decisions and banks, acting as principal or market maker, have the right to manage their books and make a profit.





## Cürex's Solution Delivers a Best Execution Opportunity and Ensures Client Anonymity

In ViewPoint Volume 1, we discussed the Preamble for the Codes of Best Market Practice issued by committees of the eight central banks. In their message, they warned the buy side to pursue diligence when executing FX. They also highlighted the importance of maintaining strict confidentiality and avoiding conflicts of interest. We think that it is clear that the buy side pays an economic price when it does not follow the central banks' advice, executes FX as an administrative function, and works its orders on a disclosed basis through one or more banks that are acting as principal. At Cürex, we have performed significant TCA for large buy side entities that has documented this economic cost.

### Executing FX on the Cürex ECN delivers numerous benefits to the buy side:

- The Cürex ECN is a robust market place, with more than a dozen liquidity providers streaming live quotes;
- Every order and execution is completely anonymous;
- Every price on the Cürex ECN is executable – there is no “last look;”
- Every execution is time-stamped and auditable; and
- Every trade on the Cürex ECN is a print on the FTSE Cürex FX Index Series and therefore compliant with FTSE's third party governance.

### When a buy side customer chooses to execute via the Cürex ECN, it knows that it has achieved:

- ✓ A “best price” fill in our multi-contributor marketplace;
- ✓ An auditable, benchmark execution validated by FTSE;
- ✓ A price that has not been spread, with a disclosed brokerage fee; and
- ✓ Complete anonymity.

Given the banks' disclosure statements, mandated as part of their criminal settlements, we think it is time that the buy side make the clear choice that is available to them and avoid paying the potential economic price of disclosed FX execution with any bank acting as principal.

At Cürex, we believe that anonymity is a critical and necessary element in the pursuit of best execution.

“View Point” provides Cürex's insight on relevant topics to institutional users of foreign exchange. Its mission is institutional FX user benefit and information. Cürex's goal is to provide fairness, transparency and unparalleled efficiency to the FX marketplace for the benefit of our partners and customers. Visit us often so we can share our View Points with you.



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