

An exchange of views

IT WAS AN EDUCATIONAL DAY FOR ALL AT THE ACT AND BBA SEMINAR ON FOREIGN EXCHANGE HELD ON 14 JULY 2005. RICKY KNOX REPORTS ON THE MAIN DRIVERS OF FOREIGN EXCHANGE (FX) TODAY.

Market participants from corporate treasury, banks, central banks and technology providers gave polarised views and heated debate on such diverse topics as Continuous Linked Settlements (CLS), eFX, straight-through processing (STP) and IAS 39 *Financial Instruments: Recognition and Measurement*. For an event which has historically focused on the eFX debate, it was interesting to note that one of the issues which may be on the minds of many treasurers is the ongoing debate about single versus multi-bank trading systems.

The event began with an introduction to the main drivers of FX today, given by one of the leading FX figures in the Bank of England, Paul Fisher, Head of Foreign Exchange Division. Fisher discussed his interactions with the market through the FX Joint Steering Committee and discussed some of the macro trends in the FX markets today. Interestingly, he had a unique viewpoint on the volatility of sterling: "Volatility? What volatility?" Having looked in detail at sterling against a trade weighted index of currencies he concluded: "Sterling is one of the most stable currencies in the world." He also took a view which has not been borne out by recent events – namely, the devaluation of China's currency, the renminbi. He argued that: "A lot of the speculation around the devaluation of the renminbi is just that – mere speculation."

COMBINATION The eFX panel was an interesting combination of treasurers at differing stages of eFX adoption plus a representative from the multi-bank platform FXAll. The session was chaired by James van den Huele, Global Head of Liquidity Services at Barclays Capital, the sponsors of the seminar. It seems that eFX continues its progress in the market. James van den Huele said: "The FX business done by Barclays online as a percentage of total business is 65% by tickets and 35% by volume" – an impressive proportion of their trades.

While all on the panel agreed on the benefits of price, speed, management information, automation, instant access and liquidity, the rationales and views on the drivers behind eFX adoption were varied. Philip Dyke, Dealing Room Manager, BAT said his company was becoming more centralised in London and therefore there were many more deals and the size of those deals was getting smaller. Hence BAT was looking for end-to-end processing. Automation was key and price transparency secondary. Interestingly, BAT was prepared to look at 'unattended dealing' so that small deals coming up from subsidiaries were dealt automatically and then charged back to subsidiaries with a margin. Martyn Smith, Director of Tax and Treasury at Dyson had a different rationale, since his company had to deal with rapidly growing FX volumes with a small team, so work efficiencies were vitally important. However, the changeover to electronic dealing was viewed as a "low risk decision" and taken quickly. Once on the system, Dyson found "the management information available is stunning".

SINGLE VERSUS MULTI There was a dichotomy between the proponents of multi-bank portals such as Dyson, BAT and FXAll, and

support for single-bank portals from Travelex and Barclays Capital.

Steve Grossman, Chief FX Dealer, Travelex put the case for single-bank platforms being preferable to maintain bank relationships and because there was no charge, a view backed up by Barclays Capital's James van den Huele. Dyson's Martyn Smith replied with the argument that some of their banks maintained relationships even via multi-bank systems by having information as to their dealing record at their fingertips – and some did not. Of the latter category he joked: "I don't think they were watching our business very carefully – either that or they were dead".

Mark Warms, General Manager Europe, FXAll pointed out: "Many customers use our system for single-bank transactions. In fact about 20% of our trade tickets are transacted that way." Even more remarkably, he said that 40% dealt other than on best price! He argued this was usually when there was little difference in prices and they wanted to allocate the trades either for relationship reasons, ease of settlement or to help STP.

Some limitations of multi-bank platforms were discussed. Mark Warms of FXAll mentioned that they are not so useful if you have one or two banks, while Travelex's Steve Grossman was more bullish on the disadvantages, pointing out the additional cost and even going on to say they would "drive keying errors" and "if I had one large transaction to do I would do it with one bank over the phone". Even Philip Dyke of BAT agreed that high-value, low-volume trades would stay off the system, adding on the relationship side that "not only would I hope to speak to my banks but I'd also hope to still meet with them from time to time!"

A potential issue with many of the multi-bank platforms is the fact that they are owned by the banks. If the thesis that multi-bank platforms give better pricing (and hence smaller bank profit) were true, they would therefore have contradictory incentives. FXAll is owned by the banks, but Mark Warms did not see any conflict since it was not a market maker. FXAll sees the banks as its customers, but sees competition as effectively ensuring pricing. This did not address whether the quotes which banks were feeding through to FXAll were deliberately skewed in any way to maintain the direct business or for some other motive, since FXAll does allow the banks to see who they are quoting, if not who they are competing against.

While opinion was divided about the domination of multi-bank platforms, it seems all at the panel agreed that they were here to stay. Philip Dyke of BAT said: "Within five years time I can see us having the option to automate effectively from subsidiary orders right through to confirmation and settlement".

Ricky Knox, Senior Consultant, Clarity FX, Specialist FX Treasury Consultants.

ricky.knox@clarityfx.com.

www.clarityfx.com

See Economic Exposure, page 30.