

MSET

Morgan Stanley Electronic Trading

Cross-Asset and Portfolio Trading

Technology for the Sell Side, 14th October 2008

Morgan Stanley

Cross-Asset and Portfolio Trading - Overview

- Multiple trading strategies exist requiring cross-asset capabilities, e.g.
 - Pairs Trading
 - Contingent Trading
 - Option Delta Hedging
 - Balanced Portfolio Trading
- Increase in “trader tools” means investors want to execute these strategies themselves
- Can these tools be delivered now to the buy-side?
- What changes do we need for this to happen?

The Problem

- Issues clients face when self-trading:
 - How can I enter the order?
 - How can I monitor and control the order?
 - How does the trade fit into my TCA?
 - Can my prop or 3rd party EMS/OMS handle these tools?
 - Can I use a single-broker platform to execute these trades?
 - Single name analysis – pre-, intra-, and post-trade does not cope with multiple name contingent trades

Case Studies

- Examine 3 Case Studies
- 3 client requests for contingent or cross-asset trading strategies
- How do they satisfy the 3 key requirements of DMA:
 - Cost
 - Control
 - Anonymity

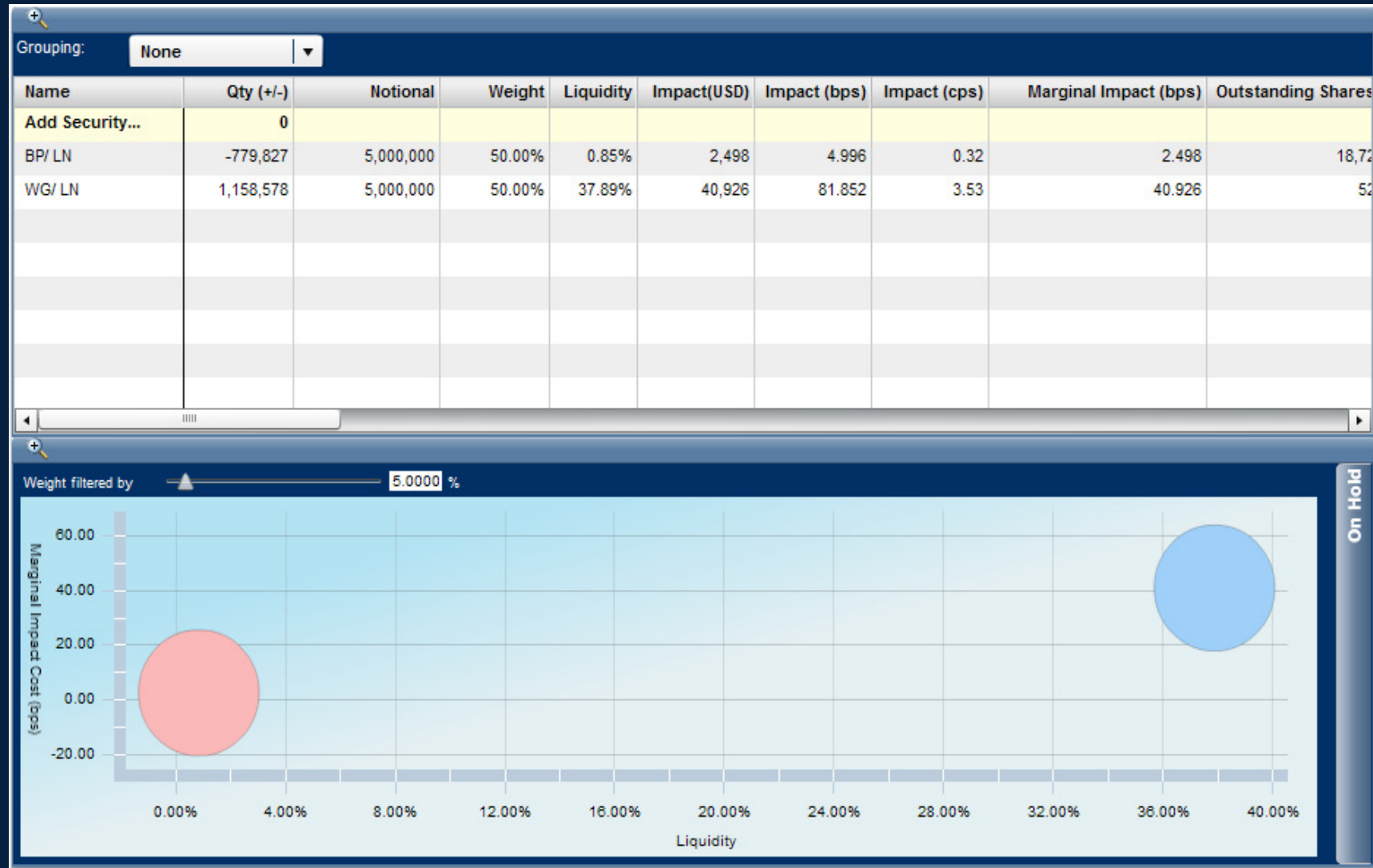
1. Automated FX Hedging

- Smart Order Routing across multiple venues with different FX
 - e.g. Unilever, Royal Dutch, RIM
- Smart Order Routing for ADRs – trade underlying and flip
- Executing broker needs to run cross book where non-fungible
- Trading engine must be able to access an electronic FX quote
- Seamless to client
- Cost should be reasonable
- Satisfies Control and Anonymity concerns
- SOR summary can be shown in conventional post-trade

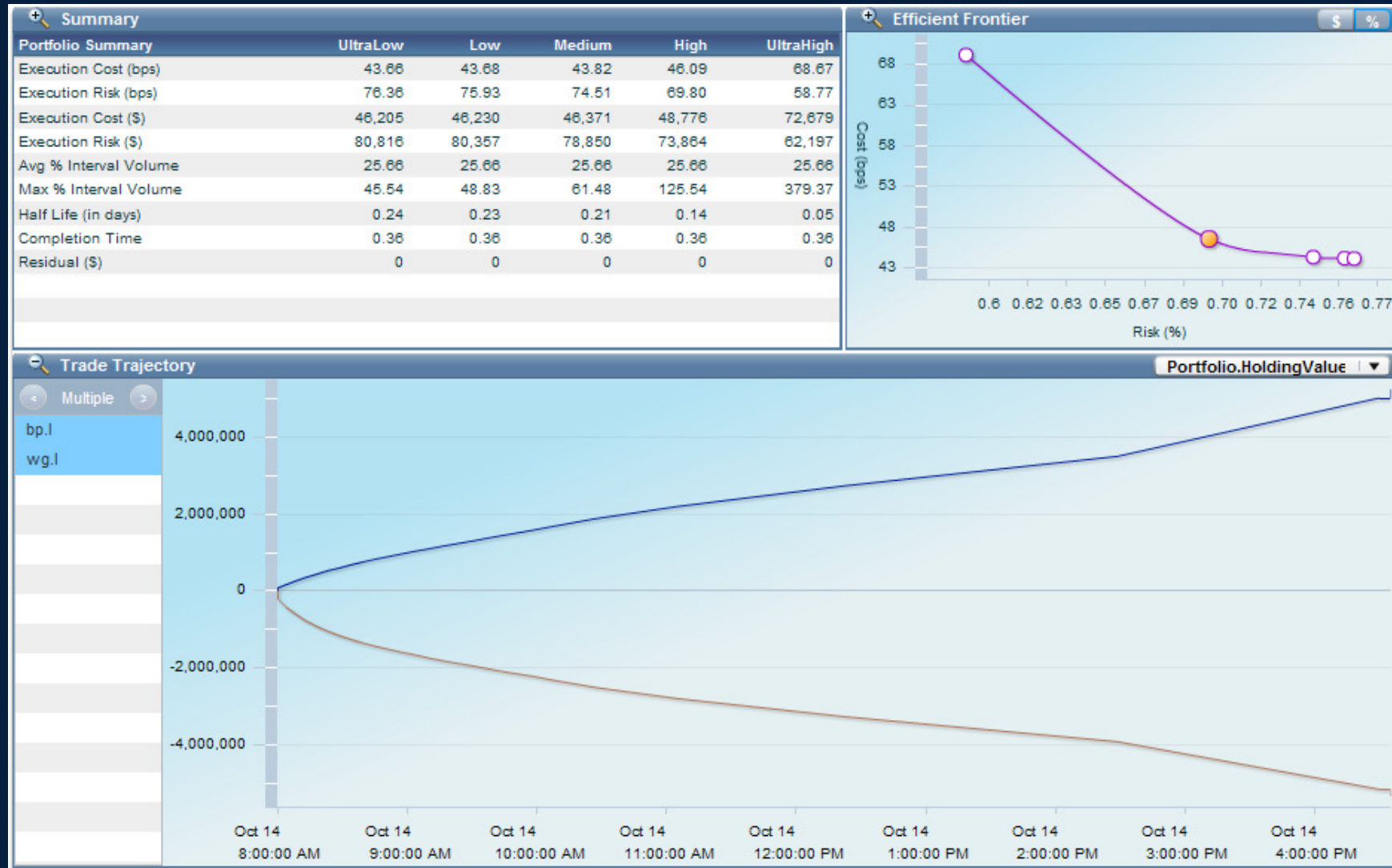
2. Portfolio Algos

- Client wishes to execute a two-way portfolio, keeping it country, sector, or risk balanced – possibly even at an account level
- Could send to sell-side PT desk to manage this – loses anonymity
- EMS/OMS integration trivial:
 - send to portfolio algo
 - this loses control and feedback
 - stocks begin to execute along contingent benchmarks
- Need enhanced intra- and post-trade analysis to monitor trade
- PT algos will take more risk on some names to reduce overall risk

Example – WG.L v BP.L – Pre-Trade Summary



Example – WG.L v BP.L – Trade Trajectory



3. Contingent or Spread Trade

- Client wishes to execute two names at a particular ratio, or execute on leg contingent on another
- Execution of the child leg is random in the single name space
- Client still has control and anonymity
- Needs to use enhanced post-trade to analyse price and fill ratio

Solutions

- Broker controlled EMS can provide enhanced cross-asset trading tools, with integrated intra- and post-trade analytics
- Executing broker can provide web based staging or intra-trade monitoring tools
- Control is key – trader needs real-time intra-trade analytics to monitor for excessive impact or exceptions

Conclusions

- Many of the trading tools and algos required for cross-asset and portfolio trading already exist
- Enhanced TCA is key to understanding the implementation of the chosen strategy
- Most clients use 3rd party, broker independent TCA, if any
- Intra- and post-trade analytics needs to be aligned with the traders implementation benchmarks

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