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FX • Week

Forex trading won't get cheaper

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CHICAGO - It is still more expensive to trade, delegates were continually reminded at last week's (April 7) FX Invest USA conference in Chicago.

Despite a return to more stable spreads and improved liquidity in the past two months, wider credit issues are still affecting the market, according to a panel discussing opportunities in foreign exchange. "The basis risk that entities are willing to take has diminished as market entry-exit cost has exponentially expanded," commented Derek Sammann, global head of FX at CME. "No-one is talking about latency any more; it's 'Will my counterparty be there in six months' time?'"

Daniel Goldman, chief executive at Ketch Capital Management, a currency-only hedge fund, confirmed that fees from investors were down, but transaction costs were up. He said this market cocktail could create two hangover effects: "You'll have supersized hedge funds and an increase in people trading proprietary capital."

In a similar vein, Tom Murphy, FX application specialist with Bloomberg Tradebook, is anticipating a concentration of players and electronic communications networks within FX. Other consequences of the reduced volumes and liquidity discussed by the panel were a short-term return to vanilla products, which provide a greater depth of book, and an increased focus on the short end of the market: Goldman suggested the market "sweet spot" is now within the six-hour to two-day range.

Sammann confirmed that CME volumes for the first quarter of 2009 were down 21% from 2008, with those at EBS down 31% for the same period. This represents a return to volumes seen at the end of 2006. Sammann wondered whether this might ignite a renewal of the growth pattern from that period, when volumes grew 35-40% year-on-year. He said this would only be achieved by tackling the credit concerns in the market. "Will we address that ourselves or wait until someone imposes it from the top?" he asked.

Another regulatory issue raised was that of compensation. Josh Levy, managing director at Tactical Asset Management, said the popular discontent over large bonuses could potentially lead to a situation where a sell-side market-maker has less incentive to offer best price to investors "because they will be paid the same regardless".

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