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THOUGHT LEADERSHIP

GAINING AN EDGE IN DERIVATIVES MARKET ACCESS IN ASIA PACIFIC

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As global trading strategies are brought to local APAC markets, firms will need to optimise their market access connectivity and execution technology infrastructure.

Trading in Asia Pacific is becoming intensely competitive as larger global brokers try to step into an expanding derivatives environment. The capacity to employ leading-edge automated trading strategies in local exchange ecosystems will be paramount for both local dealers, international dealers building presence in the region, and the clients that use their market access tools.

In the first half of the year, Asia Pacific saw futures and options trading volume increase by 31% over the same period in 2018, making APAC the largest region by trading activity with a 40.8% share of global volume. By comparison futures and options traded on North American and **European derivatives exchanges** fell by 5% and 7% respectively in the first half of 2019.

This dramatic gear change is interesting both for its cause and its effect. India's National Stock Exchange (NSE) saw a massive rise in equity index options, with Bank Nifty Index Options increasing 138% in volume (and 28% in open interest), and other emerging markets also seeing **equity derivatives volumes** shoot up. These equity instruments offer buy-side firms a broad range of avenues through which to express investment ideas, which are particularly useful as trade wars create short-term volatility in the stock markets. It's also a very competitive field; the Singapore Exchange (SGX) had a legal spat with the NSE in 2018 over the launch of Indian contracts, and the lack of a regional regulatory approach creates the potential for arbitrage between countries within APAC. Particularly as the NSE and SGX now plan to offer trading in Nifty contracts (amongst others) at GIFT City in Gujarat.

Futures and options trading volumes

The growth in derivatives volumes on Asian exchanges is being received enthusiastically by brokers. Analyst firm Coalition found that a 1% drop in futures and options trading revenues for sell-side firms globally in H1 was in part helped out by the stronger APAC regional performance.

Amongst larger international brokers, moving into APAC markets through acquisition of local brokers is a good route to increased revenues. Providing liquidity for buy-side counterparties in the region not only taps an existing growth story but gives firms a strong regional presence that can be expanded into markets which are yet to mature. These bulge-bracket brokers are improving market access by acquiring the exchange memberships, trading teams, operational resources and customer bases of local competitors.

Enhancing trading strategies

Local sell-side firms will need to ensure they have the right tools to compete against these service offerings. International firms are bringing in some of the best practices they have developed to enhance trading strategies, ensuring that their engagement is profitable, efficient and also effective for clients. In flow products, that includes the support for algorithmic trading strategies. These are very dependent upon the market access protocols supported by an exchange, market structure and often local regulations which may determine limits on ownership, leverage or positions.

For sell-side firms that are able to bridge these issues the capacity to open up these markets to their existing customer bases using the most advanced and versatile trading strategies will require them to have the right technology platforms in place. This may be local banks who are able to offer market access through their membership and regulatory approvals, or it may be international brokers who have developed or acquired access to a specific market.

Direct market access (DMA) tools will allow sophisticated clients from the US and Europe – as well as new APAC customers – to engage with **local exchanges** in order to trade on their own terms. Application of more **sophisticated algo strategies** can offer clients more intermediate access but with advantages previously only seen in the US and Europe.

Speed will be of the essence in these conditions; not only will direct and algo trading require co-located market access to exchanges in order to execute trades at the speed needed to minimise any implementation shortfall, but also the data needed for automated trading requires a fast feed in order to ensure decisions are processed efficiently, giving brokers and their clients an edge in these highly contested markets.

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