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Moving the OMS Beyond Order Management

GREENWICH ASSOCIATES

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NOW AN ESSENTIAL PART OF THE TRADING DESK, MOST SELL-SIDE FIRMS ARE USING PRE-TRADE, REAL-TIME AND POST-TRADE ANALYTICS WITHIN THEIR OMS

36% OF SELL-SIDE FIRMS SUPPLEMENT OMS TOOLS WITH PROPRIETARY MODELING AND ANALYTICS TO DELVE DEEPER INTO TRANSACTION DATA

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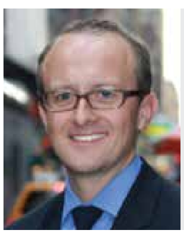

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Executive Summary

The role of the sell-side Order Management System (OMS) has moved beyond simply receiving and routing client orders. Today its functionality has grown to encompass all facets of the trade lifecycle, and it's an essential part of any sell-side desk. With such an important role to play, the OMS can have a big impact on the efficiency of the trading desk.

At minimum, a sell-side OMS needs to support multiple asset classes to be considered a candidate for the entire brokerage firm. Compliance functionality and TCA are also considered must-haves. For certain proprietary analytics, the sell side will often rely on exporting data out of the OMS. For now this is acceptable, but vendors who can support flexible analytics and reporting within the OMS may have an advantage the next time buying season comes around.

METHODOLOGY

During the months of January and February 2016, Greenwich Associates conducted in-depth interviews with 11 professionals globally at sell-side firms to understand how sell-side sales desks are utilizing technology in today's market. Respondents were asked about the markets and asset classes they traded, the tools and analytics they use and their satisfaction with their OMS.

This paper also includes data based on in-person and telephone interviews with 258 buy-side traders across the globe regarding trading desk optimization conducted between August and September 2015. Respondents answered a series of qualitative and quantitative questions about trading desk budget allocations, trader staffing levels, OMS/EMS/TCA platform usage, and ATS satisfaction levels.

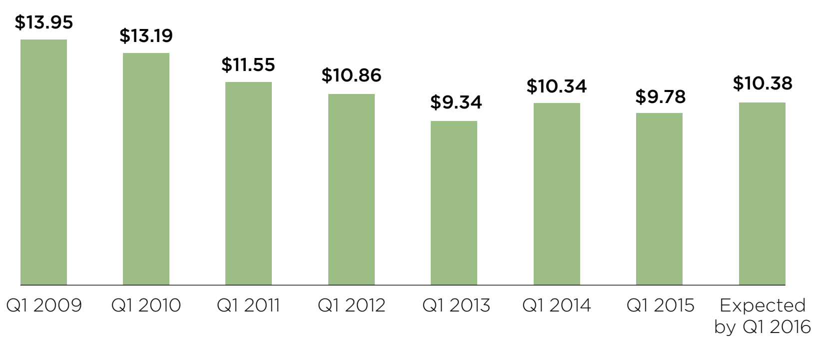
Additional data was sourced from the 2015 North American Equity Investors Study, the 2015 North American and European Fixed-Income Study and the 2015 Global Foreign Exchange Study.

Introduction

An order management system (OMS) is the backbone of a sell-side equities trading desk. In addition to its role in the execution process, the OMS plays a part in order routing, trade monitoring, compliance, risk management, TCA, and operations, making it the most vital piece of technology for any brokerage operation.

But OMSs aren't cheap. At the same time, commissions have remained flat at best, and technology costs on the desk have risen due to market complexity, new regulation and increased compliance scrutiny, thus squeezing desk margins. Choosing the right OMS is therefore a critical element in today's marketplace.

TOTAL U.S. CASH EQUITY COMMISSION SPEND



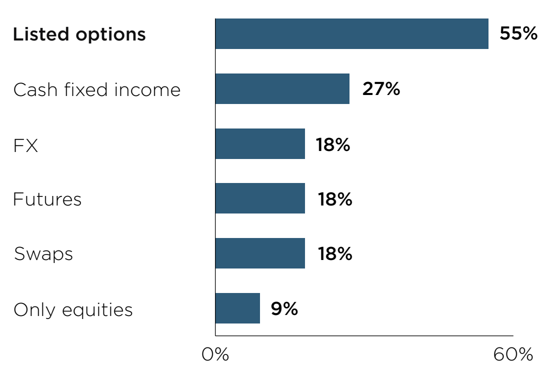
Note: Based on the average reported spend of $16.7 million per account, the total estimated commissions for the Greenwich Associates universe is $9.78 billion for the 12 months ended Q1 2015. When projected to trading universe of 585 accounts in 2015 study—stable on a matched sample basis from last year.
Source: Greenwich Associates 2015 Order Management Systems Study

Multi-Asset Efficiency

The typical sell-side trading desk uses just one OMS. Some bulge bracket broker-dealers maintain more than one, depending on their requirements in other geographies or asset classes. One such study participant currently utilizes four OMSs within the equity business—a situation born out of legacy with clear cost repercussions.

The majority of respondents noted that their OMS has the capability to support multiple asset classes, even if their actual trading activity is limited to just one asset class. Traditionally, sell-side trading desks focused only on a single asset class and product—U.S. cash equities, for example. As a result, most sell-side OMSs were also born out of a single asset class. But in an effort to expand their target audience, OMS tools have since diversified into related derivative instruments and increasingly into new asset classes altogether. While this strategy has been slow to bear fruit, times are finally changing.

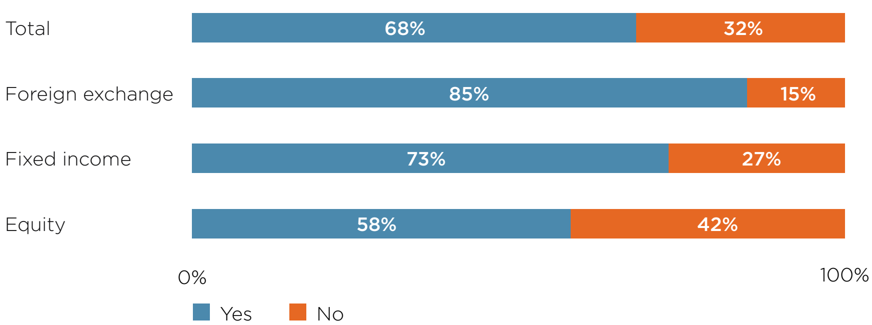
SELL-SIDE ASSET CLASSES TRADED BY DESK IN ADDITION TO EQUITIES



Note: Based on 11 responses.
Source: Greenwich Associates 2015 Order Management Systems Study

With the sell side now more focused on profitability than revenue, spending technology dollars more wisely is top of mind. As such, trading desks for related products, such as cash equities and equity derivatives, are becoming more intertwined. The buy side is also moving in the multi-asset direction, with nearly 70% of buy-side study participants stating they trade both cash and derivatives on the same desk, further encouraging the sell side to structure their desks to reflect those needs.

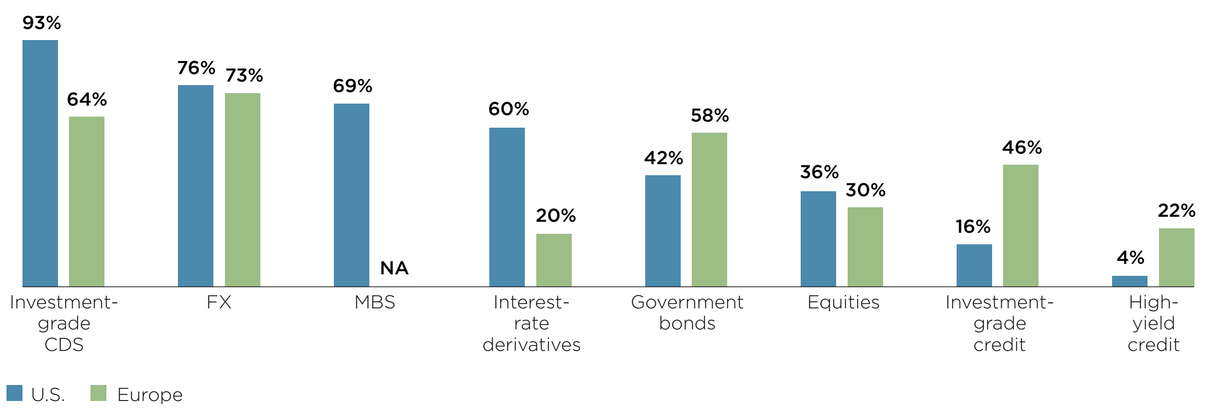
BUY-SIDE DESKS THAT TRADE DERIVATIVES



Note: Based on 224 respondents including 95 equity investors, 96 fixed-income investors and 33 FX investors.
Source: Greenwich Associates 2015 Trading Desk Optimization Study

Furthermore, electronic trading continues to spread across asset classes and regions, with fixed-income markets catching up with equity and FX in certain cases. This all encourages the use of a single OMS able to handle multiple products and asset classes, giving OMS providers the payback they've been working toward for years.

PROPORTION OF TRADING VOLUME EXECUTED THROUGH ELECTRONIC CHANNELS BY ASSET



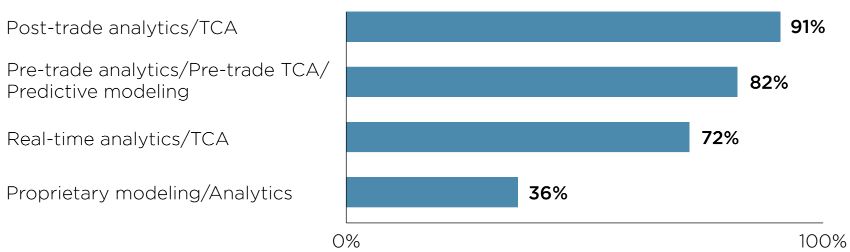
Source: Greenwich Associates 2015 North American Equity Investors, North American Fixed-Income, European Fixed-Income, and Global Foreign Exchange Services Studies

Managing Risk, Not Just Orders

Risk and cost analytics are also now an essential part of the trading desk, with the majority of sell-side firms stating they use pre-trade, real-time and post-trade analytics within their OMS. Thirty-six percent supplement those OMS tools with proprietary modeling and analytics to delve deeper into transaction data.

With the buy side increasingly focused on transaction cost and venue analysis, a sell-side trader needs to be able to quickly run a pre-trade analysis, identify the expected impact of the order and suggest a trading strategy all within seconds. While the trade is in flight, the OMS should then be able to measure performance against multiple benchmarks and be configurable, so that underperforming trades can be quickly identified and corrective action taken.

TOOLS USED TO ANALYZE MARKET RISK



Note: Based on 11 responses.
Source: Greenwich Associates 2015 Order Management Systems Study

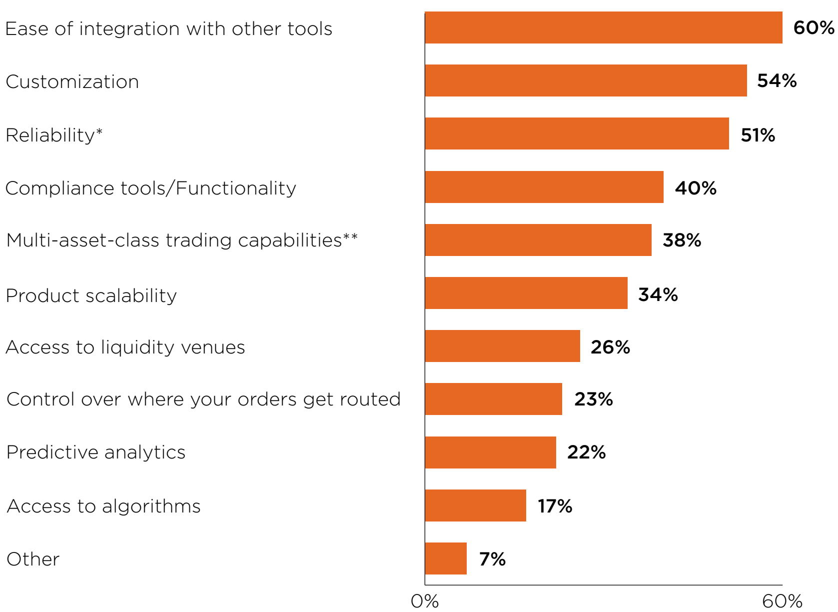
Once the order is completed, a post-trade report must be generated to communicate and summarize the day's performance. A few years ago, the buy side would rely only on their broker for this type of analysis. Today they increasingly use their own tools to measure TCA. In fact, in 2015, our equity TCA research found for the first time that every one of the more than 200 investors we spoke with was utilizing TCA. This makes it all the more important for the broker to have insightful analytic tools that stand out from the pack.

Despite the fact that sell-side desks are increasingly handling multiple products and asset classes on a single desk, risk analytics remain separate and distinct. This implies that different desk heads may not be speaking the same language when assessing risk. In times of market stress, a large sell-side firm may not have a holistic view of real-time market risks across asset classes—something 2008 showed the industry it clearly needs.

For any additional or proprietary reporting and analysis not supported by the OMS, brokers continue to export data from the OMS into Microsoft® Excel or other third-party applications. This behavior is widespread, with 91% of respondents reporting that they export data from their OMS, and that they are generally comfortable with this process.

Excel is here for the long term, but given high-profile failures like the London Whale, we expect sell-side compliance teams to push for more thorough and auditable processes. Robust and customizable reporting within the OMS would reduce points of failure, streamline the workflow and prove more scalable over time as the business evolves. This ties in with our analysis of buy-side OMS usage, where customization and ease of integration with other tools ranked highest on the buy-side trader's wish list.

OVERALL OMS FUNCTIONALITY THAT NEEDS IMPROVEMENT



Note: *Speed of response, run-time/up-time. **Including derivatives. Based on 144 responses.
Source: Greenwich Associates 2015 Trading Desk Optimization Study

More than "Fat Finger" Checks

All sell-side OMSs now include pre-trade compliance checks, thanks to SEC Rule 15c3-5. The "Market Access Rule" requires brokers to implement pre-trade risk checks on a per-client basis, designed to identify potentially erroneous or market-moving trades. Even with the ubiquity of pre-trade checks in the OMS, less than half of our study participants currently utilize native OMS post-trade compliance checks, including Regulation NMS price validation, for instance.

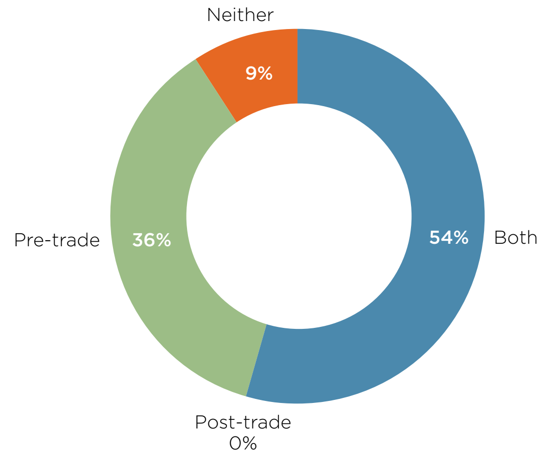
Tools to weed out longer term patterns of market abuse—such as breaking up round lots into odd lots—are also infrequently used, with only 30% of our respondents employing them. Broker-dealers have a compliance obligation to carry out such analysis, but currently do so utilizing technology outside of the OMS. With the regulatory focus now on market abuse, embedded tools that alert traders to this kind of behavior could be a differentiating feature for sell-side OMS providers and reduce risks for large broker-dealers.

Satisfaction

The sell side is reasonably satisfied with the ability of their current OMS to meet their business needs. In fact, they not only rely on their OMS for managing orders, risk and compliance, but also many of their technology initiatives. Three-quarters of respondents indicated that all or a majority of their technology initiatives were completed in 2015, often via enhancements received from third-party providers.

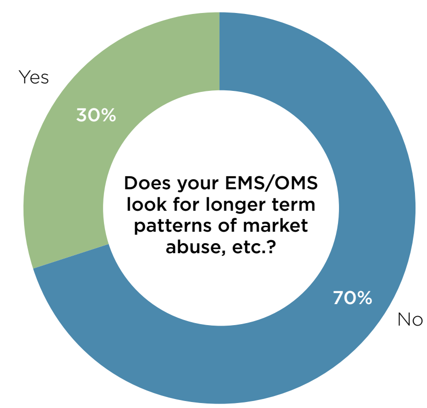
This may seem surprising, but as one trader explained, "I don't have a big technology dependency internally, as I rely on my vendor for upgrades." As such, a majority of sell-side respondents have no plans to change their OMS in the next 12 months. There is also likely an inertia factor—replacing a sell-side OMS is a big and lengthy project. To embark on a change of this size, there must be clear benefits in terms of cost savings or functionality that outweigh short-term costs.

EMS/OMS COMPLIANCE CHECKS



Note: May not total 100% due to rounding. Based on 11 responses,
Source: Greenwich Associates 2016 Order Management Systems Study

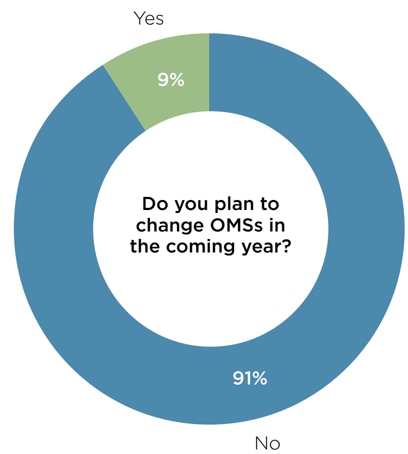
LONGER TERM PATTERNS OF MARKET ABUSE



Note: Based on 10 responses,
Source: Greenwich Associates 2016 Order Management Systems Study

One head trader we spoke with indicated that her desk was using the "firm's OMS," and she would be open to replacing her OMS in the medium term if there was a more cost-effective option that could be integrated into other parts of the brokerage operation. This highlights another dynamic that impacts OMS usage on the sell side: Technology departments do not want to support multiple OMSs, so the OMS selected is the one that has broad functionality for the firm, as opposed to specific functionality for individual desks. For example, OMS "A" may be the best choice for the FX desk, and OMS "B" is the best choice for the equities desk, but OMS "C" is chosen because it can support both asset classes, even though it is not the best.

OMS CHANGE IN COMING YEAR



Note: Based on 10 responses,
Source: Greenwich Associates 2016 Order Management Systems Study

Conclusion

Broker-dealers are in the technology business. The modern sell-side firm literally could not do business without an OMS, which today does so much more than just manage orders. The crucial role it fills makes it all the more important that brokers select wisely for their business needs and budget.

In some ways, the sell-side OMS market is a winner-takes-all situation—the typical brokerage firm will choose a single OMS for all asset classes it trades and will likely stick with that choice for a number of years. To win the prize when the opportunity comes around, the vendor needs to go beyond basic functionality in each asset class, incorporating risk and cost analytics throughout the trade lifecycle, embedded compliance tools and flexible data-export functionality with a price structure that makes sense in today's competitive trading environment.

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