

Dukascopy Bank collaborates with FXDD and Alpari (US)



Alain Broyon

Dukascopy Bank SA has entered into collaboration with FXDD and Alpari (US), who are now offering Dukascopy Bank's trading technology, rapid execution and liquidity to U.S. residents.

Alain Broyon, CEO of Dukascopy Bank SA says: "Thanks to our white label solution we are able to offer our trading technology to partners and to continue our growth. All U.S. clients who are not eligible contract participants are welcome to continue trading on Dukascopy Bank's trading system through one of our U.S. Partners."

Join the professionals –

maximise your trading and investment potential with a Retail FX ECN platform

Electronic Communications Networks (ECN) have revolutionised the Institutional FX market and many commentators believe ECN-style trading platforms are likely to do the same in Retail FX. Heather McLean explores the options available to Retail FX traders who might be looking to switch from a traditional market-making broker to an ECN platform provider.

Most FX brokers are Market Makers (operating Dealing Desks) who “make” both the bid and the ask prices on their trading systems and display them publicly on their quote screens. They undertake to execute transactions at the prices they have quoted to their customers. As counterparties to each FX transaction Market Makers must therefore take the opposite side of a customer's trade. So whenever a trader sells, they must buy from them, and vice versa. This traditional DD trading model is the most commonly practised throughout the Retail FX trading marketplace.

ECN platforms on the other hand pass on prices from multiple market participants, such as banks and Market Makers, as well as other traders connected to the ECN, and display the best bid/ask quotes on their trading platforms based on these prices. ECN platform providers make money by charging customers a fixed commission for each transaction. Authentic ECNs do not play any role in making or setting prices. This means the risks of price manipulation are reduced for retail traders.

Once again ECN-style brokers serve as counterparties to FX transactions, but they operate on a settlement rather than pricing basis. Unlike fixed spreads, which are offered by some Market Makers, spreads of currency pairs vary on ECNs depending on the pair's trading activities.

Why ECN?

Wael Salem, head of business development at FX Central Clearing, says the traditional market-making broker models offer higher leverage, lower deposits, up to 100% bonus, and the ability not only to trade micro, but nano lots. So the question always rises, why would a trader chose to switch to an ECN broker?

“In the past decade, the ECN model was only within the reach of banks, hedge funds, and proprietary traders, where account sizes had to be in millions of dollars to get access to such liquidity pools, price streaming and execution models,” comments Salem. “Now ECN brokers utilise the latest technology and clients can trade in fair and realistic market conditions, trading on tier one liquidity provided by some of the biggest liquidity providers in the FX business. In addition to that, ECN brokers have no conflict of interest between their clients and themselves.”

The number of non-dealing desk (NDD) FX trading facilities, either straight through processing (STP) or ECN plus STP brokers, has notably increased in the recent years, claims Vladimir Kisiov, head of business development at Deltastock. He says the shift from the dealing desk (DD) to NDD business model has accurately addressed the growing demand of the forex trading community for greater liquidity and best execution, so explaining the migration trend of retail clients from Market Makers to ECN-STP brokers.



Wael Salem

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He adds: "Nonetheless, retail forex Market Makers are still in business. The DD is still a sustainable model and that is not without a reason. In that regard, the debate about DD and ECN seems to be diverting the attention from the real issue; how brokers are executing client trades. To be able to quickly enter or exit a position or trade at the requested price, such as where your order is filled, is what matters most to retail clients."

Combined offering

Deltastock offers both DD and real ECN-STP facilities under one roof, in the company's in-house developed trading platform, Delta Trading. The integration of an ECN-STP (Level 2) module in the proprietary Delta Trading platform is complementary to the option of trading at fixed dealing spreads, significantly widening the scope of trading opportunities for clients, who benefit from the advantages of both DD and NDD trading models, says Kisiov. Clients can open a position by placing a trade at the fixed dealing spread and later on close that same position by choosing to have their order executed through the ECN-STP (Level 2) panel of Delta Trading.

Kisiov states: "Ultimately, it is the trader's decision on whether and when to deal with a Market Maker

or trade in a pure ECN environment. This process has been further streamlined for the convenience of clients. They do not have to meet any additional requirements or criteria whatsoever to freely cross-utilise trading at fixed spreads and dealing at ECN variable spreads which often go down to 0.1 pips on FX majors. They just access both facilities through one trading account, in one platform."

However, Kisiov contends that Market Makers' (DD) business model is to be the buy side of the FX trade, when the client is the sell side. "Conflict of interest and trading against clients are speculations which are nourished predominantly by the marketing departments of the newly fledged ECN-STP brokers, former Market Makers that are now providing an anonymous ECN environment," states Kisiov.

"It is not serious (and far from professional) to regard the DD model as synonymous with a service offered to the detriment of clients. Market Makers manage net client exposure on an aggregate basis. They clear and offset portions of it in the interbank market by strictly following their risk management policies. They are by no means trading against individual clients. Let's not forget that the Market Makers are on the top of the pyramid, and they are the major liquidity providers of the tier one and two prime brokerages, down along the chain to the STP (NDD), ECN-STP brokers," Kisiov remarks.



Vladimir Kisiov

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Two basic broker services

George Xydas, director of international operations at FXPro, comments: "There are two basic services offered by FX brokers. The first is a service whereby a broker makes a market in currencies, and the second is the broker providing an agency service. In the first instance, the broker has to provide a constant price and liquidity flow at which clients can trade, and charges a spread between the bid and ask price. If pricing is not competitive and liquidity is not sufficient clients will be swift to change service provider. The provider must also have sufficient capitalisation to be able to accept the increasing client volumes and must have a good risk management system to be able to hedge its exposures with the broker's prime brokers."

"In the second instance, the broker provides an environment through which different Market Makers, be it banks, hedge funds or other liquidity providers provide the price and liquidity flow. In this environment the broker provides an agency service and charges an agency fee such as commission," says Xydas.

Xydas continues: "The retail trader has to carefully review the terms and conditions of each broker and the environment it offers to fully understand how each environment works. Usually the trader has to compare the bid-ask spreads offered by the Market Maker to the spreads offered in the ECN, plus the commission charged by the ECN broker. In addition there are different types of orders that can be placed in each environment, as potentially there are different leverage and margin requirements. So it is up to the trader to decide which conditions better meet his or her needs before making a final decision where to go. At FxPro we offer both environments and we have tried to make both offerings as similar as possible, using our relationships with global banks, as well as implementing technological solutions that allow the trader to use either environment."

Key factors to consider

There are three factors that should determine whether a retail forex trader should transition to an ECN Broker, states Mushegh Tovmasyan, global head of sales at Alpari (UK). The first is minimum trade size. "Historically banks have been reluctant to process small ticket transactions and that is why ECN brokers have implemented a minimum trade size for their ECN accounts. Advances in technology now enable many ECN brokers to allow mini lot trading (10k notional value) and micro lots (1k notional value)." Tovmasyan says the second reason is trade commission. He explains: "Traders should consider



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the total cost of the trade and not only the spread. To give you an example: \$50 per one million commission charge is equal to 1 pip spread markup on a round turn trade."

And finally, Tovmasyan points to latency. "The benefit of ECN execution is that trades are executed at available market rates. If there is latency between the client and the broker's server, the trade might get executed at different rates from what was requested because markets can change in the time it takes for the information to reach the server."

While Joan Droguett, research, monitoring and brokerage officer at Dukascopy Bank, enthuses: "In our current highly volatile market, I can easily say there are only advantages in choosing an ECN broker. Apart from the dramatic difference in available liquidity, having Market Makers compete to offer their best prices can only be an advantage to the retail trader, provided they are not penalised by any order size limitations. For retail traders, micro lots are also a must, and any worthwhile ECN would make sure their execution is on par with the execution of institutional traders."

A note of caution

However, Samantha Roady, Chief Marketing Officer, GAIN Capital, warns: "On paper, the concept of a



Mushegh Tovmasyan

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retail ECN sounds great; access to unlimited liquidity from multiple institutions, super tight spreads, fast trade execution, no conflict of interest, and the rest. However, it's not guaranteed that the retail ECN offerings available today offer significant advantages for most retail traders over the direct offerings available from the large, regulated retail FX brokers.

"For sophisticated retail traders who think they would be better off trading on an ECN, it's important to compare ECNs to regular broker offerings in five areas: liquidity; spreads; execution, tools and services; and safety of funds," she says.

She continues: "Retail ECNs are only as good as their liquidity relationships. Therefore, it's important to choose a provider that can provide you with access to a deep pool of liquidity to ensure your ability to see and trade on tighter spreads than you would see on a retail platform."

Improving investment performance

On the question of how retail traders can use FX ECN platforms to improve their investment performance, Xydas comments: "I will start by Level II pricing. In

an ECN a trader can see the entire depth of all the liquidity providers that are connected to that ECN. For small orders this may not make much difference, but for a \$20 million order, the trader must be able to see if he can execute such an order and how much of the order book they will fill by placing that order, as well as the price that the order will be executed. Level II pricing helps the trader decide if they will place a market order or a limit order. If there is sufficient depth and the prices offered for such depth are acceptable to the trader, then he can place a market order to be filled instantly. Otherwise, he will need to place a limit order and wait for the order book to build at that price,"

Xydas continues. "Most of the ECN environments that are offered to retail traders do not offer expert advisors (EAs), as most EAs were and are developed for the Metatrader platform which is mostly a Market Maker solution. So if a trader wishes to use EAs he may need to trade on MT4 or MT5 rather than an ECN. As the use of automated trading increases (50% of volumes executed by clients of FxPro are through the use of automated trading or EAs) ECN brokers will have to provide such solutions. FxPro launched cTrader ECN in April 2011 and we are fast developing a solution to allow clients to write and use EAs." Tovmasyan adds that MetaTrader provides a very flexible programming language to integrate news and third party market data into automated trading strategies. "Traders can then use MetaTrader to execute via ECN venues via brokers such as Alpari. Our MT4 Pro accounts are integrated into ECN liquidity and execution via a highly optimised bridge developed in-house."

Aligning interests

Perhaps one of the greatest benefit of ECN platforms is that the interests of the broker and the client are aligned, comments Tovmasyan. He says the broker provides all the tools available to facilitate a client's trading, and orders via ECN platforms are routed to the best price provider in the liquidity pool which is comprised of top tier banks and hedge funds. "It is possible for one order to go to one bank and the next to another bank," he adds. "To the trader this means that no single price provider receives all of the trades, essentially masking the trading strategy. This facilitates the usage of high frequency and news trading." For ECN brokers, the accessibility to real market conditions are unlimited, states Salem. "The main difference between the two models is the 'no conflict of interest'. As ECN brokers work based on volume generated through their platforms, they strive to

provide the best and latest technology to their clients to ensure highest standards of execution and pricing.

"As an ECN broker, FXCC provides spreads on all its currencies starting from 0.1 pips with an average on majors varying between 0.4 pips and 0.7 pips," continues Salem. "Comparing Market Maker models with the ECN model, some of the spreads can reach up to 5+ pips on majors. This means that a client is better off \$50.00 per one standard contract (100,000.00). Additionally, due to the 'no conflict of interest', ECN brokers allow all EAs to trade. Contrary to Market Makers high volume, profitable EAs are more than welcome. In fact, high frequency traders (HFTs) and EAs are one of the key to our own success with this business model. In Market Maker models, these EAs are banned or are given a very high risk categorisation on their books. Depth of the Markets can give a trader or a HFT a true view on where other trading portfolios have placed their pending and current orders. Many market analytic tools depend on this feature to build their strategies and analyse trends and predict price action models," Salem concludes.

EAs, Add-ins, Level II pricing and market depth are tools among many others that, if used correctly, can help traders maximize performance, claims Droguett. He says Dukascopy Bank's Jforex platform allows



Samantha Roady

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traders to run any strategy or custom-made add-in based on Java, and to provide access to market depth. "While developing their strategies, traders can utilise the market depth as an additional resource, providing information about the current market," he notes. "The special option for placing of Bids and Offers to the market allows traders to act as a liquidity provider by placing individual bids and offers directly to the market. As Bids and Offers are placed, they can be matched by other liquidity consumers, thus avoiding the spread costs."

Pricing issues

On how traders can exploit increased price volatility experienced in an ECN trading environment, Tovmasyan states: "Traders are able to utilise EAs to take advantage of these fluctuations to engage in high frequency trading. Traders need to be extra sensitive about the latency between their trading station and the broker's ECN server. It is recommended to use a VPS service or co-location to maximise the potential of these strategies."

Liquidity in an ECN is provided by a number of sources, usually global banks, states Xydas. As each bank has its own book to manage, it can change the pricing and size of liquidity that it offers in an ECN. "This leads to greater volatility during news times, as banks tend to widen spreads just before major news events or during the night when liquidity is low," explains Xydas.

"A trader first of all needs to know that such events happen, and so design his trading strategy and execution tactics accordingly. If a trader is using a strategy of trading the news he must design such strategy having in mind that spreads may widen, so he must design his take profit/stop loss orders accordingly so that he doesn't get stopped out accidentally in an order that is proving profitable had not the stop out been triggered," notes Xydas.

One of the major differences between ECN brokers and traditional type brokers is the filtration of prices, says Salem. He states that ECN brokers could have volatility over one minute up to five times the volatility on the same pair within the same minute with a Market Maker. Market Makers provide this filtration in order to eliminate traders taking advantage of mini spikes that range around five to 10 pips on average. "With ECN brokers, predicting these spikes or using a very well written HFT or EA, traders can take advantage of such trading conditions that could only be provided through a true ECN broker."

Improved transparency

Another important feature of how ECN-STP systems benefit clients compared to the traditional trading model says Kisyov, is that each participant can act as a Market Maker, so that the other ECN participants compete for his offers. This allows clients to place orders within the spread. The limit orders submitted by the clients in the order book are immediately visible to all. Thus traders can place trade orders among themselves; Avoiding intermediaries, as there is no dealing desk and execution is fast and error free; the identity of retail clients is not visible to other market participants, which ensures that they receive the same conditions as institutional players; since there is not only one company that provides quotes (offers), but a few large institutions, there is much higher liquidity and therefore better pricing and lower spreads, even during high market volatility.

Kisyov adds: "ECNs are a transparent way of trading as clients can see market depth, which gives them much better market insight. They also receive post trade information to the detail. One feature we provide that is not typical for most ECNs, is the ability to choose a specific counterparty to trade with (valid for market orders only)."



Joan Droguett

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Market volume

Depending on the type of order, available market volume can influence the execution, states Droguett. "Banking holidays, or the overlaps of regional market opening times, can affect certain instruments. But the biggest drops in available volume are almost always the result of extremely volatile markets. In highly volatile markets, the few milliseconds separating the market orders from reaching the ECN servers can have great influence on the execution. Thanks to the possibility of selectively controlling slippage, a trader can adapt to any possible market condition."

Salem states: "When we talk about retail clients, in which 90% of the trading tickets vary between 10,000 and 5 million, volume is not an issue; clients will always get executed and what matters the most is the technology behind the execution of large orders. The question is what a broker would do if the order requested is higher than the volume available through liquidity on the specific price. In the traditional broker model, the order will be rejected or could be re-quoted three to five pips away from its current price."

Salem continues that in the example in which a client has requested an order of 20 million (200 lots), and the liquidity available from Bank X is only 5 million, FXCC will execute the first 5 million on the requested price, and take the next 15 million to the next depth of level, and so on, to fulfill the full order, and once the order is fulfilled and fully executed the average price is given back to the client. "In many cases that next best-offered price could be better than the requested price," contends Salem. "Therefore the average price could be better than the requested price. In short the client could be slipped in his favour or against his favour when a requested volume is larger than the available in one tier in the current market depth. This process is done within milliseconds. With our current structure, 99% of our orders up to 20 million (200 lots) have been executed within a range of less than 1.0 pips."

Market execution

In highly volatile markets, banks pull out their liquidity during high volatility or trading news, spreads are slightly increased and the volumes drop, says Salem. Clients that experience pending orders or try to trade during that period or event, will trade based on market execution. He adds: "Market execution is the ECN market in its simplest form; a client order is put into the system and the client will receive the best pricing available through all our liquidity pool. Clients may get slipped, although getting slipped in an ECN market is

not always bad news. Clients may experience slippage to their favour, as well as against, depending on the market conditions."

Xydas notes: "Usually for small orders execution is not an issue at the prevailing top of the book price. But for a \$30 million order on a minor currency pair, execution may take minutes and spreads may widen much more than the trader anticipated (if he places a market order). So the trader must first monitor an ECN environment offered by a broker, make sure that there is sufficient liquidity and volume executed in the currency pairs that he is interested before choosing that broker and ECN."

"ECN environments work best with medium sized tickets such as \$500,000 to \$1 million," continues Xydas. "Small tickets are not favoured by liquidity providers, as there are clearing fees involved with different counterparties, and the clearing bank charges settlement fees per ticket irrespective of ticket size. On very large tickets, the liquidity may not be there. So it is up to the broker providing the ECN environment to build solid relationships with the liquidity providers and the technology providers to manage this. FxPro has managed to be able to provide order sizes as small as 10,000 without additional charges, and usually the book offered on the FxPro cTrader is up to \$25 million each side allowing for the execution of large market orders."

Going user friendly

ECN Brokers have been taking massive steps to make sure that ECN platforms are more client friendly, claims Salem, including ease and availability of the technology, demo account accessibility, manuals, webinars, seminars, platform orientation and the integration of third party systems and tools to smooth their usage. "In addition to that, with the abundance of technology, platforms now are easy to integrate and access either through PDA and mobile devices," states Salem.

Tovmasyan comments: "Traditional ECN technology providers have been adding retail elements to their platforms such as charts, interactive buttons, technical analysis, mobile and web access and much more. Brokers in turn have been integrating popular retail platforms into ECN liquidity and execution."

Xydas comments: "An ECN broker must first understand that a retail trader has different needs than an institutional trader (for whom the ECN environments were developed). Retail traders need to have charting and technical analysis tools embedded in the platform to allow them to back test strategies. In addition they need to be able to see margin requirements and status of their portfolio. FxPro cTrader offers all those tools favoured by retail traders. In the current world of social networking, retail traders like to share strategies between themselves and comment on each other's trading techniques. FxPro offers a snapshot tool that automatically takes a picture of the trader's screen and posts it on social networks such as Facebook or Twitter."

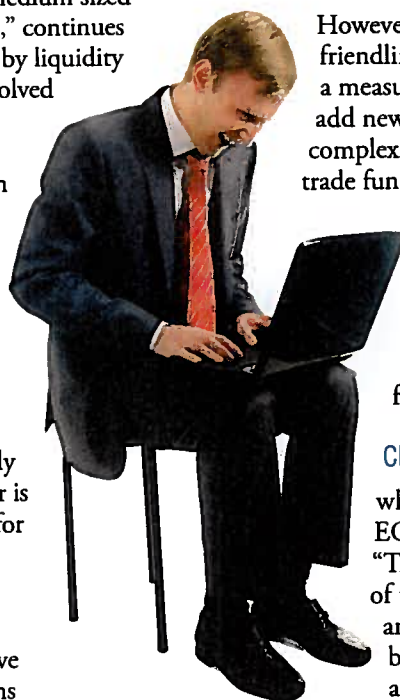
However, Droguett contends: "The user friendliness of an application is not necessarily a measure of its popularity. As the platforms add new features and tools, the level of complexity also increases. The basic click-and-trade functionality will always remain, but any use of fundamentals or technicals to create a working system will require a modicum of skills. The focus for Dukascopy Bank is to ensure the continuity and ability to meet client's demand in order to develop new functionalities and trading tools."

Choosing the platform

when it comes down to choosing an ECN platform, Tovmasyan notes: "Traders should examine the total cost of trading and not only spreads. Spreads and commission fees are important, but traders also need to be aware of accessibility (web, mobile, Windows, Mac, API language, etc).

In addition to this, it is important to analyse the broker offering access to the ECN platform, such as quality of service, counterparty risk and global presence. Low latency is essential to ensure the trader gets the full benefit of the ECN platform and execution."

On what issues should influence a trader's choice of ECN platform, Rody has several recommendations. "Be sure to compare full transaction costs. For many ECNs, the commission can be \$50 per million, which is the equivalent of .5 pips. If the USD/JPY spread at a regulated broker is 1.5 pips, you'd have to consistently trade on spreads of less than one pip to realise a saving."



Happy is super tight spreads and fast trade execution

"If you're looking at an ECN because you like to make larger traders, say around \$5 million, check the fine print to understand if your margin requirements will be higher for larger trades, or if the amount of liquidity on the ECN is sufficient to allow you to trade size at the tighter spreads. In some cases, the depth of liquidity is not always there for larger trade sizes, or you'll receive volume weighted average price fills on your larger trades; either way you could end up paying more," she warns.

When trading on a retail ECN, your account and funds are held with a retail broker. Therefore, the firm's reputation, financial wherewithal, and regulatory oversight are still important considerations, continues Rody. "The broker's technology infrastructure should be firmly established to ensure connectivity, speed, and low latency. Make sure your broker is regulated by one of the primary regulators, such as the UK, Japan, Australia or the US, where you'll have added confidence knowing the broker must abide by a full set of rules and regulations, plus there is a framework for dispute resolution and, in most cases, safety of funds protection."

Rody adds that if you qualify as an eligible contract participant (ECP), your options are significantly better as you can trade on an institutional ECN. (ECP qualifications vary from region to region, but most have a net worth and investable asset requirement).

Support for strategies

An ECN platform, whether provided from a third party vendor or from in-house development, should always include an option to run a strategy, states Droguett. "Jforex, our inhouse platform, offers such functionality, and offers an API capable of handling even the most complex algorithms. Back testing and demo testing are parts of such functionalities, and are a very big part of our customer's attraction to our ECN."

Salem adds: "Trading on an ECN feed and execution model allows clients to implement more accurate strategies, with the abundance of resources clients are able to build, test and implement their own trading strategies. Theoretically these trading strategies are built to perfection to work on a fair trading basis. Previously, these clients had no access to the liquidity that would help them achieve those theoretical results." "Currently, with brokers providing ECN trading conditions to retail clients, these clients can now build better strategies and leverage opportunities from the market related to execution models and spread pricing," Salem concludes.



Mariusz Potaczala

Platform Launch

TMS Brokers has recently launched a new FX trading platform called TMS MT4 which uses STP and NDD execution and is integrated with the MetaTrader4 platform. It allows retail customers to perform online FX operations directly, immediately and automatically on the interbank market. The new platform compliments the existing GO4X platform which TMS operates as a Market Maker. Mariusz Potaczala, CEO at TMS Brokers comments: "The requirements of Polish consumers, as well as the emergence of ECN platforms, prompted us to launch this new service, dedicated to more advanced users than those on GO4X. The most important feature for this group is access to very tight spreads and extremely fast execution, without a dealing desk. Our new product meets these requirements" He continues: "TMS MT4 sets new standards in Poland. We are the first Polish broker to offer direct access to the interbank market, with variable, often zero spreads, low commissions and extreme speed of execution in conjunction with the most popular technology in our country; MT4. What is also very important for us is the transparency of this model, in which all customers' transactions are executed directly on the market. I would like to emphasise this because I notice a negative tendency to use a hidden partial or even complete Market Maker model by some brokers, who define themselves as STP dealers. It's very bad for our industry, because it causes a lack of confidence in institutions that define their services in a fair manner."