

All or Nothing: A New Paradigm in Money Market Trading for Corporates

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While electronic trading portals for corporate treasurers got off to a slow start in the FX market and have been largely ignored in the money markets beyond MMFs, this situation is rapidly beginning to change.

The use of money market trading platforms in the corporate sector has lagged behind the adoption of foreign exchange (FX) portals. This situation is now changing rapidly and many medium to large corporates are responding to increased pressures for more cost-effective treasury operations by introducing electronic platforms for their trading activities as part of a broader programme of automation.

But it is interesting to see that this change is not taking place in the kind of incremental fashion that has characterised the introduction of FX platforms over the past few years and was envisaged in the money markets until relatively recently. Corporate treasurers are increasingly approaching portal implementation in a 'big bang' manner, eager to move from having nothing automated to having comprehensive and fully integrated money market trading without going through incremental solutions along the way.

At the beginning of the century, corporate treasurers were obliged to manage their cash investments largely via a complex mix of different communication channels. Finding out what was available in the market normally involved ploughing through numerous daily notes of phone calls, faxes and emails from relationship banks, perhaps supported by the occasional visit to one of the few single bank web sites that were available at the time. The information collected was then reviewed either in a simple but unstructured way, or more likely through the time consuming process of inputting the information received into a spreadsheet followed by a more structured analysis. The resulting trading decisions were then implemented manually, again via various communication channels, typically by phone and fax.

However, things began to change shortly after this with the launch of two major FX portals, FXall and 360T, in 2000. While these portals were initially targeted at relatively large corporate organisations, they did begin the slow process of opening the eyes of the whole corporate treasury community to the opportunities available from a move to electronic trading and the benefits that this could bring. These early platforms faced two major and almost philosophical obstacles to acceptance and growth. First was the reluctance of the FX banks to participate on multi-bank platforms, which they were concerned would disintermediate them from their customers. And second was a mirrored concern on the part of the corporates that such platforms would create a degree of separation between them and their banks, and hence weaken closely guarded relationships.

This was a classic chicken-and-egg situation. The banks were unwilling to risk weakening their client relationships when they were not faced with a strong demand to do so from their existing customers. Meanwhile, corporates were not in a rush to push their banks to join and were certainly not in a hurry to sign up to a portal that did not have a good selection of the banks they wanted to use. But, as frequently happens at such times of major change, a number of 'leaders' emerged from the corporate community and championed the use of these portals. Not only were they prepared to implement a portal and, if necessary, consider using other banks that were already participating, but they were also prepared to put pressure on their own relationship banks to join or suffer the consequences. As a result, after a relatively slow and sometimes difficult start, these portals began to establish themselves and have continued to grow. And, of course, neither the banks nor the corporates can now envisage a world without a substantial proportion of FX trading being undertaken through these trading platforms.

Money Market Trading

While progress was being made on the FX side - albeit slowly - developments to cover the money market trading activities of the corporate treasury community were virtually non-existent. From the outset, the FX portals always said that they would also offer money market instruments to meet the corporate treasurers' Holy Grail of a single platform covering all their requirements. But the reality has been that they have had to be so focused on getting the FX side of their offering established that they have to all intents and purposes ignored money market instruments in any serious way.

The earliest providers of third-party portals for specific money market instruments have made little if any effort to break into the broader money markets and the reality is that, beyond money market fund (MMF) trading, there is currently nothing remotely close to meeting the full set of money market trading needs of the corporate community. The range of available offerings across the other main money market instruments, such as terms deposits, certificates of deposit, repos and commercial paper, remain very limited and highly fragmented.

To date there has been a close similarity in the progress of FX and MMF platforms in terms of their relatively slow acceptance and adoption by both the bank and corporate sides of the market. However, all the evidence suggests that there is going to be a radical departure between the two experiences going forward. What has become increasingly clear recently is that attitudes towards electronic trading portals in the corporate space have changed fundamentally. Far from being seen as something that might make life a bit easier and could perhaps deliver marginal benefits, electronic trading platforms are increasingly being seen as a front line tool in the corporate treasurer's battle to monitor and manage all kinds of risk while being expected to deliver significant efficiency gains and associated cost reductions.

With this increasing realisation that electronic trading platforms can help corporate treasurers to reach apparently contradictory objectives has also come a clear understanding that the benefits of using such platforms increase very rapidly and in a non-linear way as the scope of the portal increases. There may be some benefit to a corporate treasurer from trading one of their MMFs on a platform but there will be proportionately a lot more if the platform can be used to trade all their MMFs through a single gateway. The same considerations apply across instruments and portal benefits increase rapidly as more instruments are added to facilitate comprehensive and integrated access to all relevant money markets.

As this understanding of the power of portals has grown, there has been a further realisation that in an ideal world there would not be separate money market and FX portals but rather a single portal covering the full range of a corporate treasurer's money market and FX needs. Some MMF and FX portals have tried to address this issue by forming alliances but these have not been a major success to date as treasurers have tended to use a platform for a particular purpose and ignore any additional offerings that have been 'bolted on' via strategic alliances. They would clearly prefer to use an integrated system with single access, the same look and feel throughout and comprehensive position reporting across all markets and instruments. As a result, there is a rapidly growing expectation within the corporate treasury community that portals will be moving to deliver this capability in the relatively near future.

Conclusion

In a world of reducing numbers of counterparties and frequently changing credit ratings, corporate treasurers are being obliged to search more widely for eligible counterparties and instruments. Market discovery has become more difficult than ever and once appropriate investment opportunities have been identified efficient trading across a more distributed investment base becomes an essential requirement. Perhaps the major driver for a truly comprehensive money market and FX platform is the ability to provide a complete credit module on the platform allowing treasurers to automatically capture all their trades and then monitor and manage the resulting credit exposure across all counterparties, instruments, currencies and regions if required, as well as by credit rating and maturity. It is only in this way that they will be able to make fully informed investment decisions that they are confident are within defined counterparty limits and respect any other relevant treasury policies and permissions.

While electronic trading portals for corporate treasurers got off to a slow start in the FX market and have been largely ignored in the money markets beyond MMFs, this situation is beginning to rapidly change. Corporate treasurers are putting increased pressure on money market portal providers to offer the full range of money market instruments they typically use, including term deposits, certificates of deposit, repos and commercial paper. Plus, they increasingly expect to see a broad range of liquidity providers, and particularly all their relationship banks.

It is only in these circumstances that they will be able to complete most if not all of their trading via the platform and thereby realise all the benefits that can flow from electronic trading. And, in the relatively near future, further pressure will be exerted to provide comprehensive, combined money market and FX portals with an underlying credit module to allow corporate treasurers to effectively monitor and manage their trading activities within the treasury policy framework they have been given.