

# Peer Comparisons

## Upgrading Transaction Cost Analysis to Transaction Quality Analysis

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There is a fundamental problem with transaction cost analysis that limits its utility and hinders its adoption: Does anyone really know what TCA data means? If I told you the cost of your bond trade was four basis points, would you even know what that means? Or would you ask me if four was good, or bad?

Transaction cost analysis without context often looks like a big pile of numbers. Too often the size of the pile is used to imply that there are meaningful insights buried inside, if only we are perceptive enough to find them. And the implied message is the bigger the pile the greater the insights. I once received an equity TCA report from a broker that contained over 45,000 numbers. Nowhere in the report was there any guide to how to interpret these numbers or place them into context. Was the four basis points of post-trade reversion good? Was it bad? How was it even calculated?

With so many numbers and so little context they may as well have used a random number generator to create that report. And now that I think about it, perhaps they did. When I contacted my coverage salesperson (who had sent the report) the answers to my questions seemed as random as the numbers that led to the questions in the first place. It became clear this was an exercise in quantity over quality.

At BondWave we are seeking to provide quality over quantity by developing ways to assign meaning to TCA data. Placing TCA data in the proper context allows us to know if a TCA figure was good, bad, or indifferent.

### DEFINING MY PEERS

One unique element of fixed income trading is that nearly every disseminated trade report represents the whole of the order. There is very little slicing and dicing of parent orders into child orders resulting in multiple executions on a single parent order. This feature comes in handy when defining peers. A peer can be defined as every trade that resembles my trade, rather than every trader that resembles me. If I am buying a BBB corporate bond with 10.5 years to maturity in institutional size, then I want to compare my execution to other institutionally sized purchases of BBB corporate bonds with 10.5 years to maturity. These are my peers. Once I have a jury of my peers, I can render a verdict on the quality of my execution rather than just calculating the cost.



Imagine that

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### TRANSACTION QUALITY

Going back to one of our original questions, if I told you the cost of your trade was four basis points, would you even know what that means? Well, if I also told you that the average cost for all trades that are like your trade is five basis points then it would mean that you have done an above average job. But if I told you the average cost for your peers is only three basis points that would mean there is room for improvement.

This leads to other areas of improvement in using trade costs, we can now make more valid statements across trades of all types. If all costs are defined as performance relative to my peers, I can finally compare trades I have done at different sizes across different maturities and ratings in a meaningful way. I can also compare across brokers even when the nature of the trades going to them differs.

### MANAGING TRANSACTION QUALITY

At BondWave we often say, "If you do not measure it, you cannot manage it." Measuring transaction costs is a minimum requirement for every trader. But measuring transaction quality can prove much more fruitful. Recognizing that there are many ways to transact fixed income trades, it becomes important to measure and compare these alternatives. And by expanding from transaction cost measurement to transaction quality measurement we also expand the comparison to all alternatives executed by all peers.

To learn more, please visit [bondwave.com](https://bondwave.com),  
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#### ABOUT BONDWAVE LLC

Founded in 2001, BondWave, an affiliate of First Trust Portfolios L.P., is a financial technology firm specializing in fixed income solutions. We serve a wide range of users including traders, compliance professionals, and RIAs from the smallest to the largest firms in the industry who use our tools to provide a superior fixed income experience to their clients while supporting critical regulatory mandates.

Effi<sup>®</sup>, our Engine for Fixed Income, is the single platform through which we deliver all our solutions providing intuitive dashboards and insights into every fixed income position and transaction. Capabilities include portfolio analytics and reporting, custom alerts, and proposal generation, as well as tools that support best execution, fair pricing, and mark-up monitoring and disclosure on both a pre- and post-trade basis. BondWave leverages advanced technologies and data science to develop proprietary data sets that fuel our innovative solutions.