

BONDWAVE DATA DIGEST - VOLUME 1

ATS Volume –Through the Looking Glass - Stepping Toward Transparency

BondWave introduces a new series titled Data Digest. As we explore and mine our extensive data library of the fixed income marketplace, we frequently come across interesting patterns, observations, and new data. In the Data Digest series, we will begin to share what we discover with the fixed income investing community.

Volume 1 explores the new ATS Indicator field that the Financial Industry Regulatory Authority (FINRA) and the Municipal Securities Rulemaking Board (MSRB) recently added to their respective trade data feeds, Bond Trade Dissemination Service (BTDS) and Real-Time Transaction Reporting System (RTRS).

ATS Volume Indicator

On July 18, 2016 FINRA and MSRB began to publish, through their respective trade reporting facilities (TRACE and EMMA), limited details about where fixed income trades are executed.

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By adding an Alternative Trading System (ATS) Indicator to their data feeds they now make it possible for market participants to determine whether a trade was executed electronically via an automated trading system.

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FINRA instituted similar reporting requirements in the equity market in the second quarter of 2014 and subsequently increased the granularity of the data available over time. Beginning in the second quarter of 2016 FINRA added an additional requirement for non-ATS's to also report their volume statistics. Thus, making it possible to gain a complete understanding (albeit on a delayed basis) of where equity trading occurs.

It would not be unreasonable to assume that FINRA and MSRB might follow a similar pattern for fixed income trade reporting over time.

ATS Universe

Table one contains a list of TRACE ATS's registered with FINRA¹. While there are 22 TRACE ATS's listed several do not appear to actively trade (internet searches revealed no information) and at least one is solely focused on the inter-dealer market.

¹ <http://www.finra.org/industry/ats/trace-ats-identifiers-list>

TRACE ATS Identifiers List	
BGCX	BGC FINANCIAL L.P.
BRLQ	BRILLIQUID.COM
IEBC	ICAP ELECTRONIC BROKING LLC
CSCA	CREDITEX SECURITIES CORPORATION
DLWB	DEALERWEB
ELET	ELECTRONIFIE SECURITIES LLC
FTBR	FOLIOFN INVESTMENTS, INC.
GFIG	GFI SECURITIES LLC
LATG	LATIUM DIVISION OF GFI SECURITIES LLC
GARE	ICAP TRADING SYSTEM
IATS	IBKR ATS
ITGP	POSIT
VABD	KCG BONDPOINT
LQNF	LIQUIDNET FIXED INCOME ATS
BNDS	MTS BONDSPRO
OPBX	OPENBONDX LLC
OTCR	OTC LINK ATS
SZRO	SPREAD ZERO ATS
TMCC	TMC BONDS L.L.C.
TWDA	TRADEWEB DIRECT LLC
TMID	TruMid ATS
TPCD	TPCREDITDEAL

It is also important to note that not all electronic fixed income trading platforms are registered as ATS's. In a recent report² on electronic fixed income trading, SIFMA profiled 19 platforms (15 operational and 4 not yet operational) with a variety of business models including limit order books (LOB), matching sessions, request for quotes (RFQ), dark pools and click to trade (CTT). Of the 19 platforms reviewed in the SIFMA report, 11 are listed as registered ATS's on the FINRA website. Notable among the electronic trading platforms that are not listed as ATS's are Bloomberg and MarketAxess.

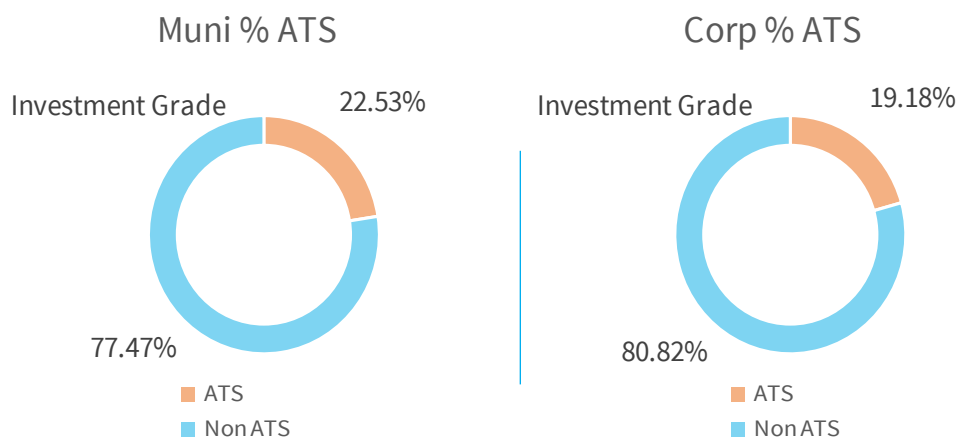
Bloomberg employs multiple formats (dark pool, RFQ, and CTT), but does not publish volume information. MarketAxess employs both an LOB and an RFQ platform. According to data published on their website³, MarketAxess accounted for 13.8% of corporate bond volume in June, 2016.

² SIFMA Electronic Bond Trading Report: US Corporate & Municipal Securities – February, 2016

³ <http://investor.marketaxess.com/volume.cfm>

ATS Volume⁴

With several weeks of data now available for both corporate and municipal bonds some trends have begun to emerge. Municipal bonds trade slightly more frequently on ATS's than do corporate bonds.

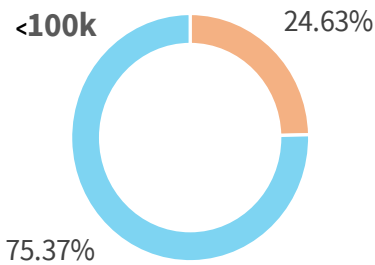


⁴ Graphical data is based on trade reporting data published by TRACE and EMMA data from 07/18/16 to 08/11/16

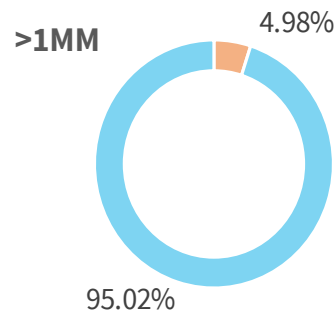
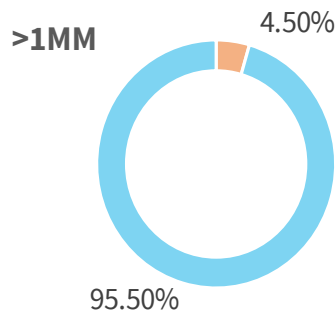
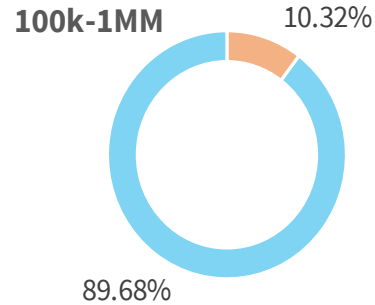
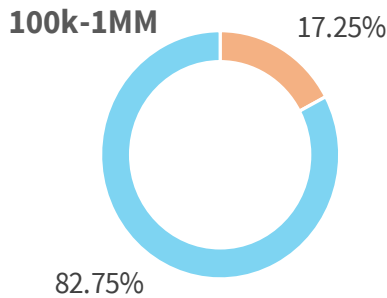
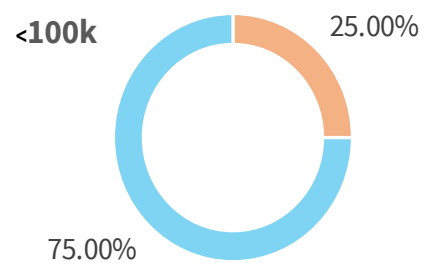
Though there is some difference by size, traders looking to execute either small or large trades (less than \$100,000 par or greater than \$1,000,000 par) of either municipals or corporates face the same fill percentages on ATS's. However, for the in between trades ATS's have a bigger slice of the pie for municipals (17.25%) than they do for corporates (10.32%).

Whether a municipal trader is executing investment grade or high yield bonds they are likely to have a similar experience on an ATS. Whereas the corporate trader is more likely to find a fill in investment grade bonds on an ATS than high yield bonds.

Muni by Size



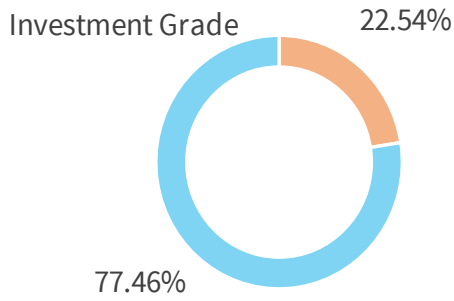
Corp by Size



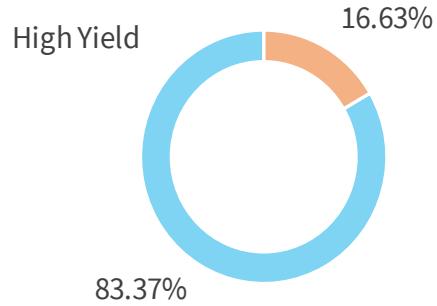
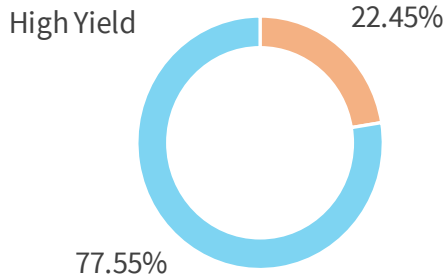
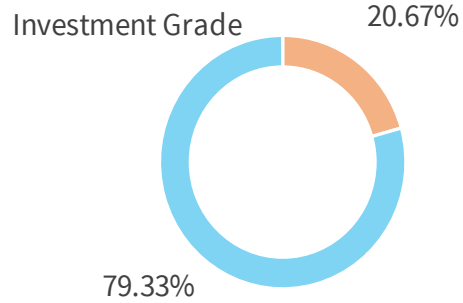
■ ATS
■ Non-ATS

■ ATS
■ Non-ATS

Muni IG vs HY



Corp IG vs HY

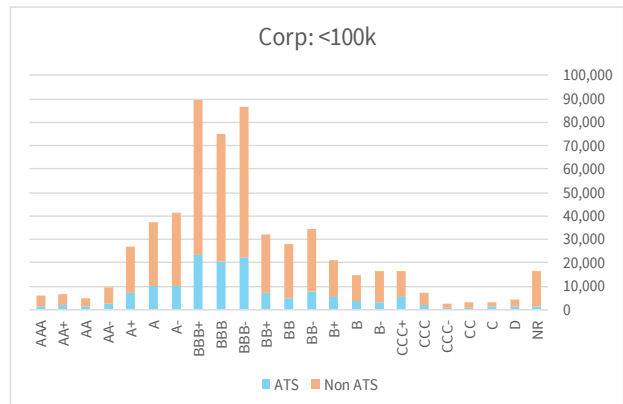
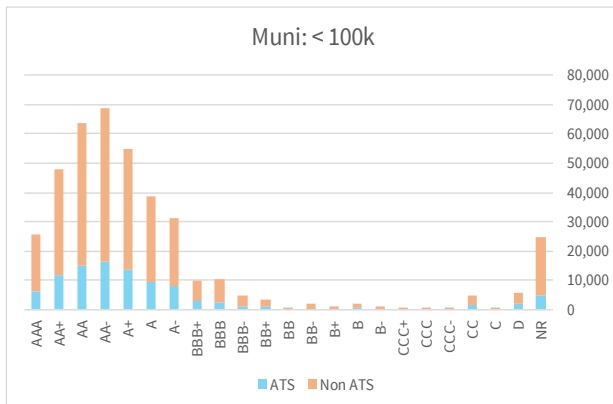


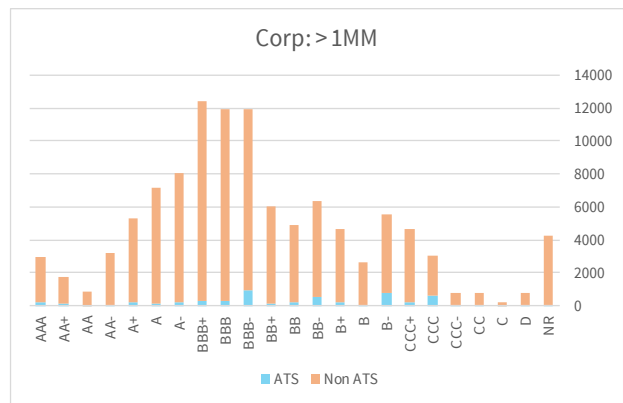
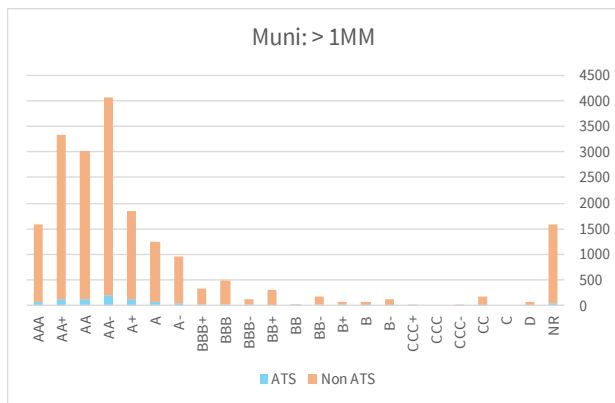
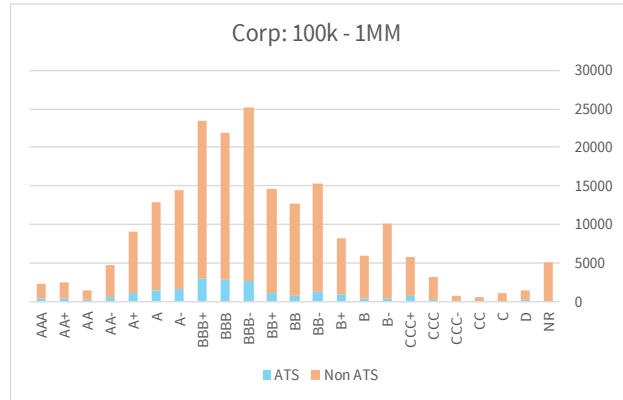
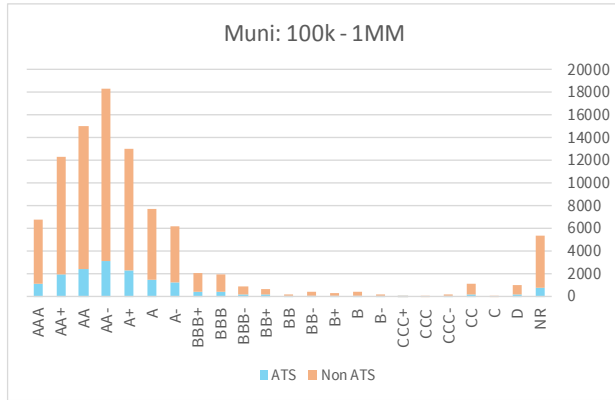
■ ATS
■ Non-ATS

■ ATS
■ Non-ATS

Part of this difference is driven by the different rating distributions of municipal and corporate bonds. Municipal bonds have a much higher concentration of higher investment grade securities.

While corporates are highly concentrated in lower investment grade and upper high yield categories.





Cancelled or Corrected Trades

Electronic trading generally decreases the number of cancelled or corrected trades by removing some of the sources of error in communications. The FIX Protocol messaging language was developed to replace telephone communications and facilitate electronic trading while helping to minimize trade costs and maximize efficiency⁵.

Even though most fixed income ATS's rely on electronic RFQ's rather than the posting of executable bids and offers, even that amount of automation can lead to process efficiencies that decrease the miscommunications that can lead to trade cancellations and corrections.

The corporate bond data available allows us to examine this phenomenon. TRACE includes a designation of whether a trade has been cancelled or corrected. ATS trades have a significantly lower incidence of both cancellations and corrections.

	Non ATS	ATS
Corrected	1.88%	0.47%
Cancelled	1.71%	0.48%

Source: TRACE data from 07/18/16 to 08/11/16

5 <http://www.fixtradingcommunity.org/pg/main/what-is-fix>

Conclusion

As FINRA and MSRB illuminate electronic trading on ATS's, it would not be surprising to see this activity grow. A similar pattern unfolded in the equity markets over the course of a decade where the NYSE saw its market share in its own listings dwindle from 80% to 20% as dark pool trading (ATS's and OTC venues combined) grew to almost 40% of the market⁶. While the factors driving growth of dark pool trading in equities are different, the growth of ATS trading in fixed income securities could potentially come from some combination of the following factors:

- Data as Marketing – Published statistics will increase awareness of ATS trading leading to greater usage
- Lower cancellation and correction rates – If ATS trading remains less error prone traders are more likely to shift trades to the platforms
- Regulatory impetus – With increased regulatory focus on fixed income trading there is a greater need for pre-trade data to demonstrate best execution. Automated platforms are in the best position to capture and provide pre-trade data.
- DOL Fiduciary Rule – while outcomes are still uncertain, the rule could drive growth in 'As Agent' trading which could provide additional growth in ATS trading.

A Note on the Data

Throughout this article, the focus has been on numbers of trades rather than par values or market values. One reason for this is that TRACE does not report actual par values for large trades until 18 months after the trade occurs. In investment grade corporate bonds, any trade larger than \$5,000,000 is reported as 5MM+ rather than the actual trade size. In high yield corporate bonds any trade larger than \$1,000,000 is reported as 1MM+ rather than the actual trade size. Because TRACE publishes a daily total of par values for all trades executed, it is possible to measure the impact of the individual bond reporting method.

To do that, we totaled all trades using the capped amounts and compared that to the total daily TRACE reports using the uncapped amounts. For the time period covered by this article (from 7/18/2016 to 8/11/2016), the uncapped average daily volume of corporate bond trading was \$24.0 billion. Using capped trades the average volume was \$15.7 billion. Because the uncapped volume is 53% larger than the capped volume, using capped volume statistics leads to inaccurate analysis.

Municipal bond reporting follows the same capping convention as corporate bonds, but the lag between reporting capped and uncapped trades is only 5 days. The difference between uncapped and capped volume calculations is 61% (\$9.8 billion vs. \$6.1 billion).

⁶ <http://www.wsj.com/articles/intercontinental-exchange-proposing-major-stock-market-overhaul-1418844900>

About BondWave

BondWave LLC (BondWave®) is a financial technology company and registered investment advisor specializing in fixed income solutions. We serve a wide range of customers, from small independent RIAs to some of the largest broker-dealers and custody providers in the financial services industry. Traders and advisors use our tools to provide a superior fixed income experience to their clients.

We believe in the value of investing in individual bonds and the importance of this asset class in any investor's overall strategy. In the past, because of the size and complexity of the bond market, simple tools did not exist to make investing easy for traders and advisors to more effectively service their clients. As a result, the vast majority of retail investors access bonds via funds where they are unable to achieve the same benefits that individual bonds offer.

BondWave has developed the tools to meet this challenge.



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