



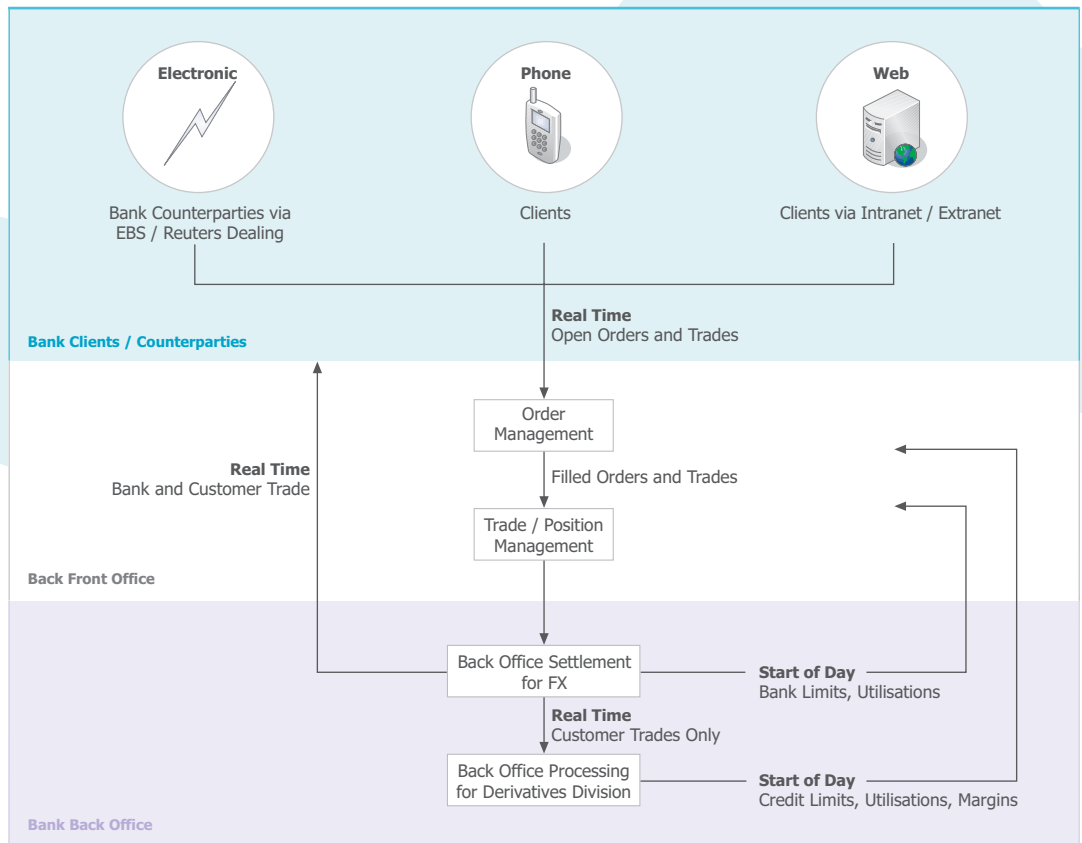
Creating a Real-Time STP Environment For eFX

If you are anything like me, you receive e-mails, read articles and attend project meetings that refer to STP (Straight Through Processing) as the Utopia of workflow solutions. These e-mails and articles seem to suggest that STP is the "only" thing keeping your organization from being the picture of efficiency. At the project meetings you attend the main topic is why haven't you completed that STP project for your financial institution? The obvious question, if STP is so great, why after all this time is (almost) everyone still talking about it, with few if any having implemented it?

The answer may lay in a book by Carlota Perez, a researcher at Britain's University of Sussex, called "Technological Revolutions and Financial Capital: The Dynamics of Bubbles and Golden Ages" published late last year. (Edward Elgar, 2002). The author suggests that technological revolutions have two consecutive lives. The first, which she calls the "installation period", is characterized by difficult adaptation. It is typically led by what Perez

calls "financial capital", and features adaptation resistance from established firms and institutions.

The second period, Perez calls "the deployment period". This period is characterized by hyper-adaptation, is led by production capital, and focuses on how this new technology can be effectively implemented in a mature industry to make things more efficient and therefore profitable. Based on

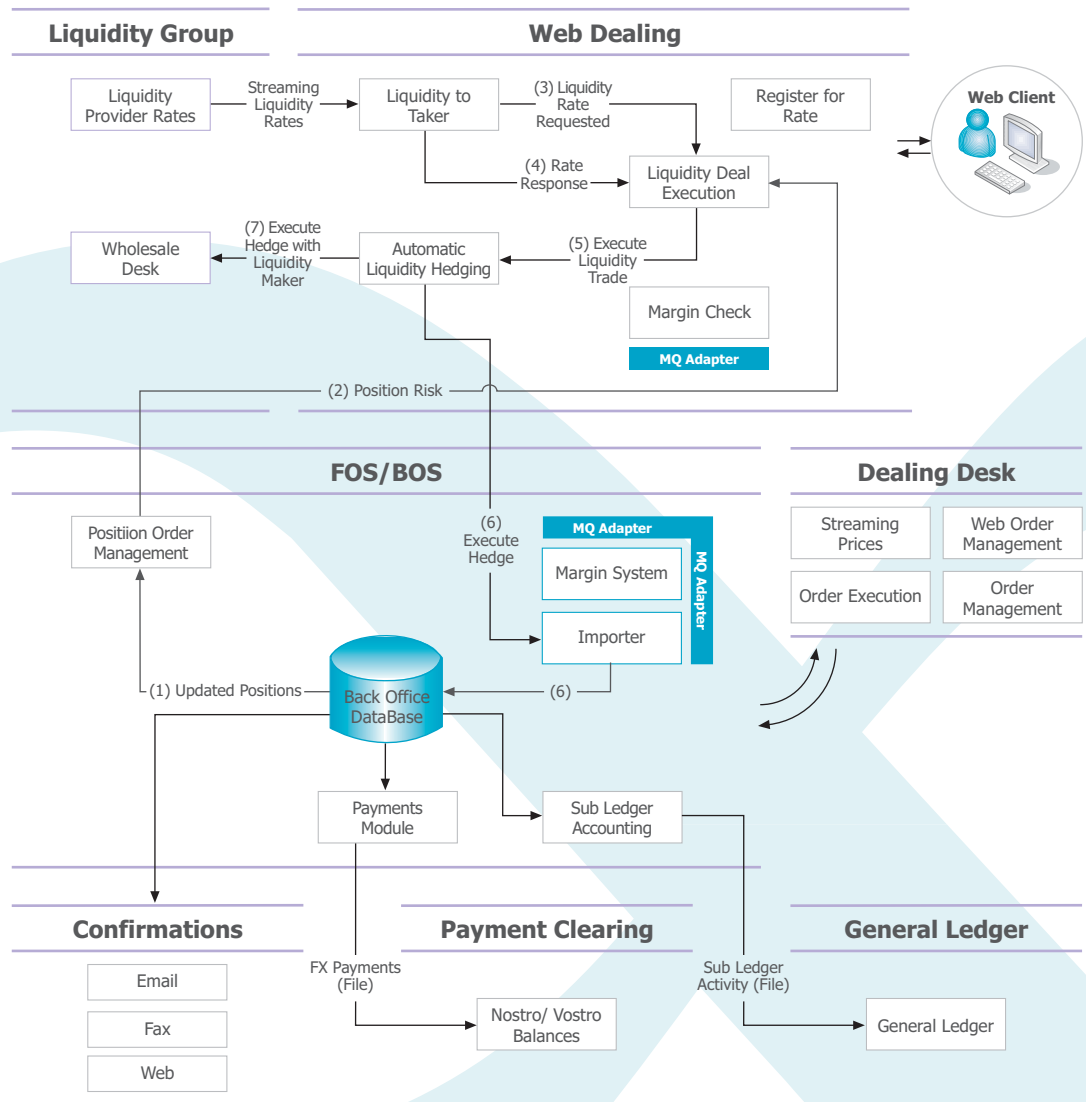


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our many meetings with financial institutions, I believe we are arriving at this second, critical stage.

A dictionary might define STP as the ability to electronically create a trade, and keep it electronic through the processes of execution, confirmation and settlement with no manual intervention. As profits from trading become more and more difficult to accomplish, many financial firms are looking for electronic STP, as a means to increase these margins. This can be achieved by increasing the number of executions a desk or firm can handle, while lowering the cost per execution. Reduction of errors is also a major factor.

During the last technology boom, many companies were born, offering advanced innovations in e-trading. The approach many took was to try and sell their entire system or solution as a replacement for whatever systems or processes were currently

in production. Adopting this strategy required an institution to make a significant investment in hardware and software, as well as to change the entire work process. This generally included replacing efficient production technology, because it was legacy and couldn't be integrated with the newer e-enabled applications. For many STP adaptors this process proved to be too costly and time consuming to undertake. An alternate strategy had to be created to solve the problems of integration while remaining cost effective.

To see how a major financial institution with trading desks in multiple geographical centers solved this problem, we will first describe their existing, highly manual, processes and then outline their solution for creating a true STP environment without removing their efficient legacy back office platform.

EBS and Reuters Dealing 3000 trades are manually ticketed and key punched into the back office

system. Pricing for branch office executions manually entered twice a day by dealing desk. All transactions less than \$75,000 USD executed at branch level, key punched into branch system, sent to dealing desk, key punched into risk system to generate ticket then key punched into back office for processing.

Deals in excess of \$75,000 executed via phone with dealing desk, tickets written, deals key punched into risk system then back office system. Manual end of day reconciliation of all trades.

When an analysis was performed on the processing of a foreign exchange transaction this institution discovered their cost averaged nearly \$85 dollars per execution. Without the economic ability to replace their legacy back office system this institution determined that they must do something creative to lower their processing expense while creating the basis for an e-forex system.

What approach did this institution take that allow it to create an ROI, enter the e-forex marketplace, and reduce the cost per transaction?

The following is an outline of the approach used to accomplish true STP and establish the basis for a long-term e-forex strategy.

- ∞ Create a new front-end database, thereby enabling a single point of entry for all types of FX transactions.
- ∞ Populate the database electronically utilizing standard API connections, with all deals from Reuters Dealing and EBS, and any other portal connection in use.
- ∞ Add to that database all open and executed orders from the proprietary and customer order books.
- ∞ Allow sales, branch, corporate, users access to streaming executable prices via a new lightweight Internet dealing module.
- ∞ Integrate this database with a new front office, risk management system to allow for pre-execution margin and credit checking.

- ∞ Book all executed transactions to the front-end database.
- ∞ Integrate the database utilizing a MQ product to exchange information across different platforms, sending and receiving data as messages.
- ∞ Publish a consolidated electronic blotter to the legacy back office system for end-of-day processing.

By creating a single database for front office risk management, risk managers will now be able to manage risk more effectively and in real-time. Importing deals to the database from Reuters and EBS eliminates keypunch entry, reducing chances for errors as well as keeping the overall position accurate.

Managing your order book electronically into that same database accomplishes both of the above-mentioned goals, reducing opportunity for error and providing the trading manager with a real position from which to minimize or eliminate risk.

These new processes coupled with the delivery of electronically streaming rates to sales, branch, and corporate users reduce the manpower required to handle low margin, high volume business. Keeping the rates real-time, with positions automatically updating the overall book, ensure a dramatically lower average processing cost converting what once was a money losing service into a profit center. Most importantly cost per transaction utilizing the same metrics fell dramatically to below \$20 per transaction.

By utilizing existing technology for real-time data transfer, standard published API's and creative integration of inexpensive front and middle office processing modules; this institution was able to maintain their legacy back office system, saving them millions of dollars and many months of difficult systems replacement and integration while creating a truly electronic Straight-Through-Process that is the basis for their long term e-forex strategy.