

Measuring Execution Quality in U.S. Treasury Markets

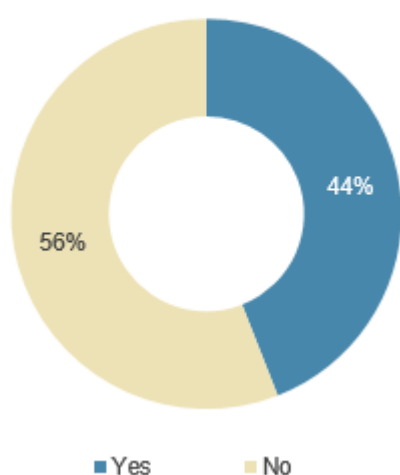
July 21, 2021

The buy side sees the U.S. Treasury market as largely transparent. That's a good thing. However, less than half of that same group told us they regularly perform transaction cost analysis (TCA). That suggests one of two things: Either the buy side does not have as much visibility into the market as they think, or they're not utilizing the transparency they do have as much as they should. Either way, it leaves me struggling to not restate one of the biggest clichés in business: "If you can't measure it, you can't improve it."

Do you feel the U.S. Treasury market is generally transparent (i.e., you have the data you need to make trading and investing decisions)?²



Does your trading desk perform Transaction Cost Analysis (TCA)?



Source: Coalition Greenwich 2021 Market Structure & Trading Technology Study.

To further that point, the existence of transparent markets does not guarantee execution quality. Executing at the price on the screen when the order was initiated could be good enough for some. Achieving the price

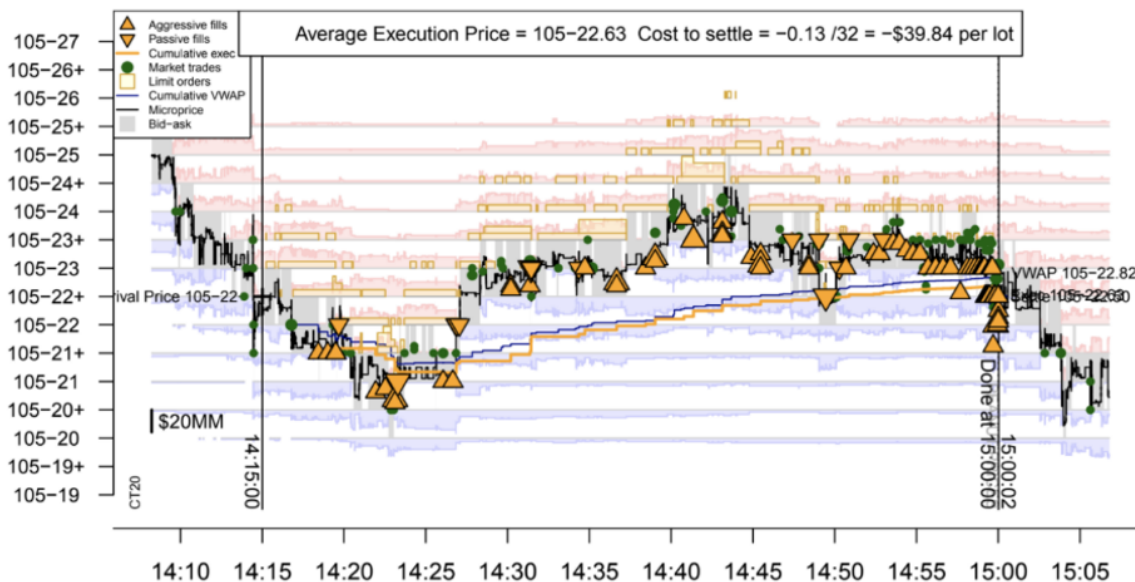
target set by the portfolio manager or pricing models might be good enough for others. But truly achieving the best execution possible requires not simply measuring the resulting price against a sometimes arbitrary benchmark, but digging into the details trade after trade to ensure all of the right factors—time, size, price, objectives, market conditions, et al—are taken into account.

Virtuous Cycle

Reliable pre-trade market data acts as the fuel for execution algorithms, whether fully automated order-book-focused algorithms or those used to interact automatically in the request-for-quote (RFQ) market. In an ideal world, this includes full depth of book, which is readily available for U.S. Treasuries and U.S. Treasury futures, and historical market data going back minutes, months or years.

When the trading algorithms are done doing their thing, the pre-trade data can be combined with the resulting execution data to analyze what actually happened, whether the trade objectives were achieved and, mostly importantly, what could be done better next time. This could include information on better timing of that particular trade, an algorithm that might have been more effective or suggestions about which dealers might have been better suited to that trade. [Quantitative Brokers](#) provided us with this great example of TCA output they created for a 20-year U.S. Treasury trade, which notes a savings of \$39.84 per lot traded:

Quantitative Brokers - Closer Algorithm Order: Sell \$100mm CT20



Source: Quantitative Brokers, Closer Algorithm - Transaction Cost Analytics for Cash Treasuries

These actionable results should then feed back into the pre-trade process, which starts the whole cycle again. The longer this goes on, the smarter the entire process should become, and hopefully, the better the execution quality received.

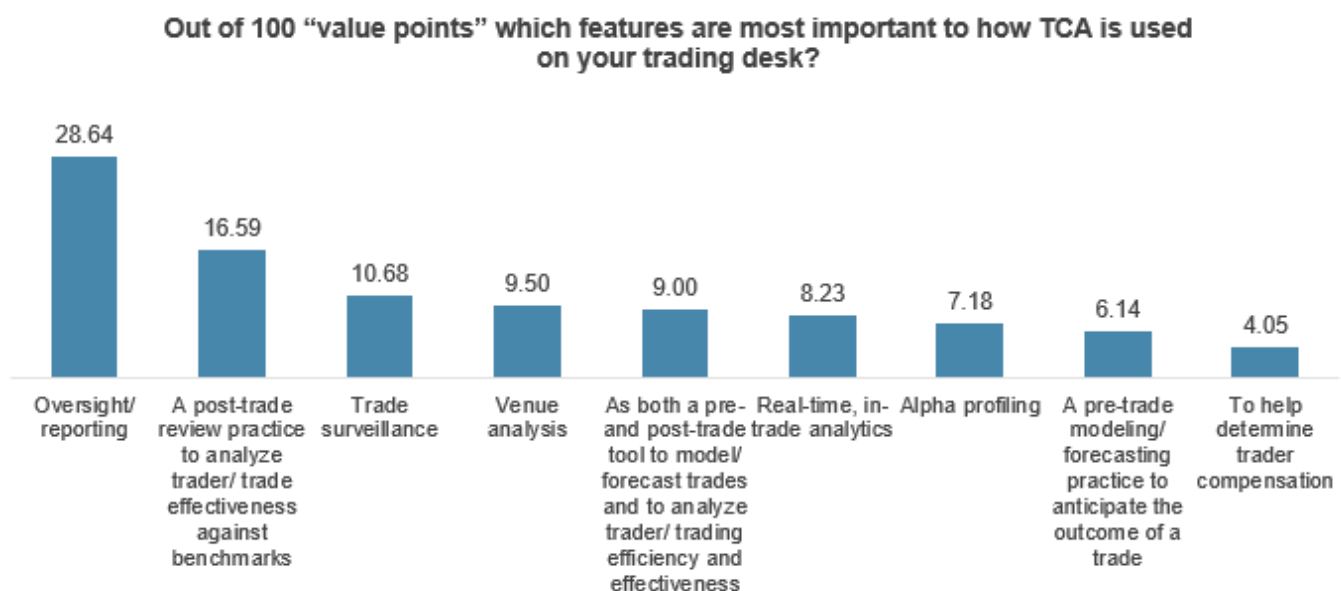
Bonds are Not Equities

This process is not unlike the feedback loop seen in TCA products focused on U.S. equities, where TCA is effectively ubiquitous on the buy side. But it is important to reiterate that the U.S. Treasury market is not the U.S. equity market. Sure, the market is liquid and seen by investors as transparent, but bond-trading venues are much more lightly regulated, there is no trading tape (U.S. Treasury reporting is weekly, and in aggregate), and there is no retail presence to speak of. So while the high-level TCA process feels the same, the underlying mechanics of that process are vastly different.

First, trading in U.S. Treasuries happens across six major platforms, not including the third of the market that is handled via phone and instant message. Each platform has its own approach to normalizing and disseminating data, which means that outside of the largest banks and buy-side firms, few have access to the data offered by every platform, leading to an incomplete picture of the market. Even with the data in hand, the data licenses can often limit how that data is used.

Second, about 70% of trading activity in this market is done on a name-disclosed basis, with nearly half happening via RFQ. That means that a visible price is not necessarily the best price a trader can receive. Relationships matter with regards to pricing, and market makers often do not show their best prices in the anonymous market, saving those for direct-client interactions.

Lastly, the process is still largely a post-trade one at this point. Few investors told us they value TCA for its ability to help them pre-trade, which leaves us believing there remains a huge opportunity to move the market forward with enhanced pre-trade analytics.



Source: Coalition Greenwich 2021 Market Structure & Trading Technology Study.

Technology is not a Roadblock

In the late 1990s before fintech was cool, the technology available could not solve all of the business

problems being put forth. Thirty years later, the tables have turned, with technology now able to handle tasks and challenges that some in the business aren't interested in automating yet. One of the longest running roadblocks to TCA adoption is the perfect case in point—traders do not always want their performance to be measured!

Looking forward, TCA isn't just for the buy side. Liquidity providers can and increasingly are measuring their performance in the market more precisely than ever. Dealer-to-client e-trading has grown over the past year, and with it, the amount of data available to market participants to measure their success. And if the SEC and FINRA move forward with proposed plans to enhance oversight and require more detailed reporting, the information available to all in the market should only increase.

Methodology

The Coalition Greenwich 2021 Market Structure and Trading Technology Study is based on responses from 157 fixed-income investors in the U.S. and Europe. Asset managers made up 44% of responses, with the remainder a mix of hedge funds, insurance companies, regional banks, and others.

www.greenwich.com | ContactUs@greenwich.com

Coalition Greenwich, a division of CRISIL, an S&P Global Company, is a leading global provider of strategic benchmarking, analytics and insights to the financial services industry.

We specialize in providing unique, high-value and actionable information to help our clients improve their business performance.

Our suite of analytics and insights encompass all key performance metrics and drivers: market share, revenue performance, client relationship share and quality, operational excellence, return on equity, behavioral drivers, and industry evolution.

About CRISIL

CRISIL is a leading, agile and innovative global analytics company driven by its mission of making markets function better. It is majority owned by S&P Global Inc., a leading provider of transparent and independent ratings, benchmarks, analytics, and data to the capital and commodity markets worldwide.

CRISIL is India's foremost provider of ratings, data, research, analytics, and solutions with a strong record of growth, culture of innovation, and global footprint.

It has delivered independent opinions, actionable insights and efficient solutions to over 100,000 customers through businesses that operate from India, the U.S., the U.K., Argentina, Poland, China, Hong Kong, and Singapore.

For more information, visit www.crisil.com

Disclaimer and Copyright

This Document is prepared by Coalition Greenwich, which is a part of CRISIL Ltd, an S&P Global company. All rights reserved. This Document may contain analysis of commercial data relating to revenues, productivity and headcount of financial services organisations (together with any other commercial information set out in the Document). The Document may also include statements, estimates and projections with respect to the anticipated future performance of certain companies and as to the market for those companies' products and services.

The Document does not constitute (or purport to constitute) an accurate or complete representation of past or future activities of the businesses or companies considered in it but rather is designed to only highlight the trends. This Document is not (and does not purport to be) a comprehensive Document on the financial state of any business or company. The Document represents the views of Coalition Greenwich as on the date of the Document and Coalition Greenwich has no obligation to update or change it in the light of new or additional information or changed circumstances after submission of the Document.

This Document is not (and does not purport to be) a credit assessment or investment advice and should not form basis of any lending, investment or credit decision. This Document does not constitute nor form part of an offer or invitation to subscribe for, underwrite or purchase securities in any company. Nor should this Document, or any part of it, form the basis to be relied upon in any way in connection with any contract relating to any securities. The Document is not an investment analysis or research and is not subject to regulatory or legal obligations on the production of, or content of, investment analysis or research.

The data in this Document may reflect the views reported to Coalition Greenwich by the research participants. Interviewees may be asked about their use of and demand for financial products and services and about investment practices in relevant financial markets. Coalition Greenwich compiles the data received, conducts statistical analysis and reviews for presentation purposes to produce the final results.

THE DOCUMENT IS COMPILED FROM SOURCES COALITION GREENWICH BELIEVES TO BE RELIABLE. COALITION GREENWICH DISCLAIMS ALL REPRESENTATIONS OR WARRANTIES, EXPRESSED OR IMPLIED, WITH RESPECT TO THIS DOCUMENT, INCLUDING AS TO THE VALIDITY, ACCURACY, REASONABLENESS OR COMPLETENESS OF THE INFORMATION, STATEMENTS, ASSESSMENTS, ESTIMATES AND PROJECTIONS, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE ARISING OUT OF THE USE OF ALL OR ANY OF THIS DOCUMENT. COALITION GREENWICH ACCEPTS NO LIABILITY WHATSOEVER FOR ANY DIRECT, INDIRECT OR CONSEQUENTIAL LOSS OR DAMAGE OF ANY KIND ARISING OUT OF THE USE OF ALL OR ANY OF THIS DOCUMENT.

Coalition Greenwich is a part of CRISIL Ltd, an S&P Global company. ©2024 CRISIL Ltd. All rights reserved.