

MYTH BUSTERS: WHY OUTSOURCED TRADING DESERVES CLOSER INSPECTION

By Chris Elliott and Massimo Labella, TD Cowen

Despite rapid growth in the use of outsourced trading desk solutions, there are still misconceptions about what is involved when bringing a third party in to help handle your firm's trading needs. To discuss this, **Chris Elliott**, Head of TD Cowen European Business Development, **Massimo Labella**, Head of Europe Prime and Outsourced Trading at TD Cowen, and **David Berney**, a founding partner of Ergo Consultancy, recently held a round table discussion at [Trade Tech Europe 2023](#) in Paris, moderated by **Jon Watkins**, Managing Editor of Global Custodian & Publisher of The Trade. Together, they considered the way outsourced trading is evolving and cleared up a few of the most common misunderstandings.

There has undoubtedly been a surge in interest in outsourced trading desk solutions. How do we know? For a start, practically all of the main providers, including TD Cowen, have been on a hiring spree in the past couple of years to meet increased demand, even as new service providers have entered the market. Asset management firms around the world have realised that outsourced trading can offer a wide range of benefits, making their funds more efficient, flexible and ultimately profitable.

The main obstacle for many firms has, in fact, already been overcome. In the wake of the pandemic, hundreds of buy-side firms have learned that it's possible to have a fund's traders sit in an entirely different location from a portfolio manager without any significant downsides. Once that idea has been accepted, the upsides to outsourced trading become that much more compelling.

Nonetheless, even as many firms have embraced the benefits of outsourced trading, there are still misconceptions about what is involved and what it means to enter into such an arrangement. Our round table discussion at Trade Tech explored some of these areas. On the following pages are some of the biggest myths that we tackled in that session.

Myth Number 1: Outsourced trading is an ‘all or nothing’ proposition

The word “outsourced” tends to suggest a firm is swapping out an entire department or area of activity. But that is often not the case when it comes to the way TD Cowen, or other providers, will be used. In some cases, we may handle all of a fund’s trading activity. But a large number of our clients are mid-sized or large funds who use outsourced trading to supplement their own trading team. Smaller funds also will sometimes want to have a team of in-house traders.

We call this the hybrid model, where an outsourced trading desk adds to a firm’s capabilities and/or addresses any gaps in skills or coverage that a fund’s in-house team may have. The hybrid model can widen a fund’s options by expanding market access to trade an unfamiliar asset class or geography, adding liquidity sources, handling unusually large order flow, increasing skillsets or covering a gap in staffing.

READ RECENT INSIGHT: [The evolving buy-side trading desk](#) for the most common reasons why asset managers are joining the outsourced trading wave.

Myth Number 2: Outsourced trading is aimed at cutting costs and headcount

As buy-side traders have watched the outsourced trading desk phenomenon grow, many have understandably worried about what this means for their jobs.

There are two things people need to consider in this regard. One is that outsourced trading is not just a cost-saving exercise. There may be some cases where it does become significantly more cost-efficient to outsource your trading, but that is often not the main driver. The emphasis is generally more on what can be gained in terms of trading acumen, new sources of liquidity and operational agility. An outsourced trading solution is primarily about strengthening the trading desk

and ancillary activities such as compliance, reporting and TCA. Our view is that an outsourced trading solution should be about adding, not subtracting, so that a fund can focus on its core strengths and strategic objectives.

A second issue is that buy-side traders are still very much needed, regardless of the growth of outsourced trading. The employers may change but the need for skilled traders has not. Whereas before, traders might have worked directly for a fund, now an increasing number of them work for an outsourced trading desk provider across multiple funds. But the role hasn’t fundamentally changed.

Myth Number 3: The benefits are mainly focused on the trading desk

One of the unexpected benefits from an outsourced trading desk solution is not linked to the front office. The back office benefits as well.

TD Cowen prides itself on the skills of its trading team, with many experienced traders in offices around the world ready to handle even the most complex of trades. But a major benefit for our clients is based on

the way we can help them simplify their operations. An outsourced trading solution can result in a stronger, streamlined compliance process. It can also provide business continuity. Such advantages are not the first things people think about when they think about outsourced trading.

Myth Number 4: Outsourcing solutions are one-size-fits-all

This is one of the biggest myths around. Many people assume that outsourced trading effectively commoditises the role of the trader and that it thus results in the same service for each client. But the reality is that every solution we offer is unique to the firm we work with. That starts with the infrastructure and it extends to every aspect of the relationship.

At TD Cowen we are constantly updating our technology to ensure it can accommodate a diverse range of clients. In the vast majority of cases, we can integrate a fund's technology with ours easily and seamlessly. But there may be cases, such as when a fund has proprietary technology, when this simply will not work. Even in these rare cases, TD Cowen is able to find solutions that are painless for the client. For instance, if need be, we can

adopt their own infrastructure within our environment.

This ability to cater to a client's unique set of needs extends to the people we provide to work their account. Because TD Cowen has such a large team of traders, we can make them available to different accounts to make sure the right people are in place to address the client's requirements. It's also the case that even the largest of funds that have big in-house trading teams can benefit from an outsourced trading relationship. There may be times when a fund wants the anonymity that an outsourced trading desk can provide, such as when a large, complex or sensitive trade needs to be executed.

The net result is that an outsourced trading solution can be whatever the client wants. It can be light-touch or much more involved, depending on what is needed.

FINAL THOUGHTS

The marketplace for outsourced trading is not only growing rapidly but also changing. At the end of the round table, David Berney of Ergo Consultancy highlighted six trends that are underway:

- 1) Continued growth in the hybrid model
- 2) Further expansion of multi-asset class coverage and execution to help clients capture more alpha
- 3) Demand for greater support across the entire trade lifecycle
- 4) More providers entering the space
- 5) More solutions involving the "one-to-many" agency model of outsourcing, as well as RTO (reception and transmission of orders)
- 6) Growing demand from clients wanting to anonymize or decide on a trade-by-trade basis whether to disclose their identity

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