

Best execution across stock exchanges is in best interests of South African investors

Kevin Brady, CEO of A2X, shares his views on stock-market developments

For much of the past 130 years, the JSE has been the only exchange in South Africa, so brokers have only ever needed to look at and trade on one market. But now they need to ensure that they look across all markets where the share is traded to ensure they get the best price. This process is referred to as achieving best execution.

The process is much like booking a flight. While historically you may have purchased a ticket on the only available airline, with the introduction of competition and technology, you now can use a flight comparison site to ensure you get the lowest fare offered for your preferred route.

Best execution has been common practice in most developed markets for years and now South Africa can apply these technologies and realise the benefits that competition creates.

Capital markets regulators internationally support the concept. In 2007, Europe introduced The Markets in Financial Instruments Directive (MiFID). This directive meant that European trading firms were obliged to take all reasonable steps to pursue best execution for their clients.

Similarly, in 2011 when the first competitor to the Australian Stock Exchange (ASX), Chi-X Australia, entered the market, the Australian Securities and Investments Commission (ASIC) also introduced a rule that required all market participants to take 'reasonable steps' to obtain the best outcome for their clients.

In contrast, South Africa's regulatory environment is not quite yet in line with international best practice. At this stage, each of the exchanges has defined its own best execution rule. A2X has followed Europe's MiFID II best execution rule which requires a broker to obtain the best possible result for the client considering: price, costs, speed, likelihood of execution and settlement, size, nature and any other relevant order execution considerations.

Encouragingly, the finalisation of a cross-market best execution requirement by the Financial Services Conduct Authority (FSCA) is imminent and its implementation is set to be an important milestone in protecting investors' interests.



Kevin Brady

Technology

Since A2X opened its doors for trade in October 2017, it has been challenging for most South African brokers to trade on the new market because their infrastructure was designed for a single exchange. Transitioning to a dual-trading venue environment takes both time and resources.

However, on the back of an increasing number of companies listing on A2X and growing investor appetite for best execution, some of the country's leading brokers are making the required investment.

As most exchanges operate in microseconds, the use of modern technology is not only the most efficient way for brokers to achieve best execution, it is vital they use it to do so. A smart order router (SOR) automates the process. It scans the available exchanges in real-time to find the best available deal.

A couple of leading brokers who are

members of A2X have recently implemented SORs and are now able to transact seamlessly at the best quoted price across the two markets. Not only does this ensure they get the best deal for their clients but they also save on fees when transacting on A2X.

Impact of lower costs

Although A2X has only been operational for some 20 months, the positive impact that lower costs have on increasing liquidity and narrowing spreads is starkly evident. In all the liquid stocks listed on A2X, the national best bid and offer price is most frequently found on the A2X platform and often with better liquidity.

As has happened elsewhere, competition will help grow the overall level of trade activity in South Africa's equity market, save investors and brokers money, and in time lower the cost for companies looking to raise capital.

When best execution regulation is implemented in South Africa by the FSCA, the brokers likely to benefit most will be the ones that have proactively taken steps to ensure they executed in their client's best interests, even before regulation forced them to do so. Competition is here. It is time for brokers to act now if they are to stay ahead of the curve.

A2X Markets (A2X) is a new stock exchange playing an integral part in the progression of the South African marketplace. It began trading on October 6, 2017, offering an efficient and cost-effective trading venue to secondary list and trade shares, exchange traded funds (ETFs) and exchange traded notes (ETNs).

A2X has appointed Strate as its central securities depository and operates within the proven and reliable South African settlement structure and uses technology developed by the UK's Aquis Technologies, which includes proven exchange matching and surveillance systems and a clearing platform custom-built for A2X. The end-to-end costs of transacting on A2X are 50% lower than current levels charged in South Africa.