

MTS Mid Price: Speed, Security, Simplicity

One of the biggest challenges for market makers in sovereign debt is covering risk quickly, efficiently and without information leakage. Silvia Di Giovanni, Head of Cash Interdealer Markets, MTS Markets, explains how the new automated version of MTS Mid Price delivers on all these points.

Challenging times, limited solutions

For many banks, various factors have radically changed the way in which they conduct their market making activities in European sovereign debt. This has left them with conflicting objectives:

- ▶ They are required to make prices to support the secondary market liquidity provision needs of debt management offices (DMOs)...
- ▶ ...but they do not wish to consume balance sheet unnecessarily, nor be hit or lifted on somebody else's terms.

Conventional means of covering positions resulting from market making activity are inefficient:

- ▶ Using cash bonds: both trading on the regular order book and using more traditional trading methods risk information leakage and negative slippage. (The alternative of laying off to clients is not a practical option unless the bank does very large volumes of client business.)
- ▶ Futures: potentially imprecise hedge for actual exposure.

This problem applies across the board, but at present particularly affects two groups:

- ▶ Banks that have limited balance sheet capacity available for sovereign debt market making and so must have fast inventory turnover.
- ▶ Traders covering inflation and other markets where bid/offer spreads are wide.

A practical alternative...

The latest version of MTS Mid Price gives traders a practical alternative by providing a highly automated market with firm pricing, with the key distinction that participants' intent is hidden. Mid-Price is a separate order book where traders can send executable orders to buy or sell at their own mid-level.

On Mid-Price, hidden matching occurs at the Mid Level of the MTS standard order book only when a robust (i.e. tight spread, sufficient depth) mid-price can be calculated, the book is 'open for trading', and an opposite order exists from another counterparty.

Only the MTS Mid Price is visible in the order book and this is highlighted (*see orange highlight in Figure 1*) whenever there is an order to buy or sell at this level. No individual order details are visible in the order book, so it is impossible for other participants to see the size or side of any orders placed.

MTS Mid Price is already supported by the latest software versions of leading MTS ISVs. Configuring mid-price streaming is therefore simple to set up and price updates are completely automated.

...with multiple benefits

DMO obligations: quoting and trading activity on MTS Mid Price may contribute to DMO rankings.

Discretion: a critical difference between MTS Mid Price and the regular order book is that on Mid Price a trader's pre-trade activity is completely invisible to other participants, so there is no risk of information leakage. All that is visible is the MTS Mid Price for each issue, which becomes highlighted whenever there is an order to buy or sell (see orange highlight in Figure 1) at that mid-price.

Control: Any trades executed on the MTS Mid Price order book will be on the trader's terms, as opposed to an aggressor's and banks can now contribute their own mid-price automatically. While matching will always occur at the MTS Mid Price, the bank will execute at that level or better.

Flexibility: the trader's desired mid-price can still be posted anonymously in the Mid Price book and will immediately become tradable (highlighted as in Figure 1) should the MTS Mid Price hit the same level.

MTS Mid Price - Figure 1

MTS Mid Price

38	Ticker	Cpn	Maturity	PX	Strategy	Bench.	Prc	Yld	MTS Mid Price	Status	Price MP	Price Spread MP	Yield Spread MP	VQty	Side
2	DBR	4.250	04-Jul-18	●	TED-Spread	71.66	102.330	0.402		on	102.337	0.6	1.0	10	Sell
3	DBR	3.750	04-Jan-19	●	TED-Spread	80.20	103.580	0.513		on	103.592	1.1	1.0	10	Sell
4	DBR	3.500	04-Jul-19	●	Curve Spread	85.78	104.588	0.622	104.5825	on	104.570	1.7	1.0	10	Buy
5	DBR	3.250	04-Jan-20	●	Curve Spread	-3.6	105.336	0.696		on	105.315	2.2	1.0	10	Buy
6	DBR	3.000	04-Jul-20	●	Curve Spread	-13.9	105.890	0.712		on	105.895	0.5	0.2	10	Sell
7	DBR	2.250	04-Sep-20	●	Curve Spread	-15.8	104.155	0.733		on	104.185	2.8	1.0	10	Sell
8	DBR	2.500	04-Jan-21	●	Curve Spread	-12.9	105.069	0.843	105.0650	on	105.065	0.3	0.1	10	Buy
9	DBR	3.250	04-Jul-21	●	Curve Spread	-17.0	108.230	0.920		on	108.27	3.7	1.0	10	Sell

● When the MTS standard order book is liquid a Mid Price is published by MTS

● The Mid Price is highlighted when there is an order to buy or sell at mid and can be aggressed to attempt matching

● You can manage the Mid Price as per standard quoting features including:

- Status (On/Off)
- Level Contributed
- Spread from your Mid (cts/bps)
- Quantity
- Side (Buy/Sell)

...with multiple benefits

Hedges for any trades executed on the regular book can be set up to post automatically to the MTS Mid Price book and be managed automatically once there. There is also good chance of obtaining a perfect hedging match on MTS Mid Price, without any of the information leakage risk and additional spread cost of using the regular book. Even if that isn't possible, a far more accurate hedge than just using futures should still be achievable.

Positive slippage: by posting blind on the MTS Mid Price book close to the current MTS Mid Price (on the appropriate side), traders have the opportunity of picking up positive slippage on their trades.

Immediacy: for urgent trades, traders can simply post in the MTS Mid Price book at the current displayed MTS Mid Price for immediate execution. This is a far better option than the alternative of aggressing on the regular book, which results in information leakage plus having to incur the cost of crossing the spread.

Conclusion

The latest version of MTS Mid Price is another example of MTS's 30 year commitment to technological innovation. It enables traders making markets in European sovereign debt to perform as efficiently as possible in the current highly demanding environment. It's fully automated capabilities make it possible for dealers to manage very large trade volumes, with minimal effort, and without moving the market.



Silvia Di Giovanni

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Silvia Di Giovanni has been with MTS for over 10 years and, as Head of Cash Markets, she is currently responsible for managing and growing the interdealer network.

Before joining MTS, Silvia covered multiple roles within the fixed income space ranging from short term interest rates broking at Icap and Dawney Day at the beginning of her career to the position of fixed Income Sales to help growth of the Italian market in Europe for Spear Leeds and Kellogg and Van Der Moolen to managing Asset Under Management (AUM) for Cassa Lombarda in Rome.

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