
Swaps Liquidity Aggregation: Best Execution to Product Selection

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Executive Summary

Swaps liquidity is going to fragment. History tells us that a combination of available technology and catalyzing regulation, both of which now exist in the swaps market, creates an environment in which liquidity fragmentation across multiple electronic trading platforms is nearly inevitable. Regulatory reform will impact how this fragmentation takes place, but they will not prevent its coming.

This fragmentation presents an opportunity for dealers at risk of being disintermediated by Dodd-Frank-inspired regulations, and technology companies that have had little opportunity in the overly manual swaps market. Aggregating liquidity via smart technology is common in other markets such as equities and FX; providers of such tools hope to make a splash with SEF aggregators using lessons **they've** learned from the past. Their enthusiasm is warranted, but creating SEF aggregators and advanced smart order routers for the swaps market is considerably more complex than it is for those other markets.

Aggregating request for quote (RFQ) and order book markets into a single view is no easy feat. Automating the inherent complexity of an experienced swaps **trader's decision-making process will require technology that's akin to artificial intelligence. And we can't ignore regulatory uncertainty. Even if the final rules are passed early in 2012, industry lobbying and/or a change in the White House in 2013 could see the rules changed yet again.**

How and when swaps market liquidity will fragment can be debated forever; but it **will fragment. The problem is, using today's liquidity profiles and execution models to design the swaps trading tools of tomorrow is denying the inevitability of change.**

The TABB Group Vision Note **Swaps Liquidity Aggregation: Best Execution to Product Selection** is based upon conversations with swaps dealers, proprietary trading firms, hedge funds, swap-execution facilities and technology providers. The report examines historic precedent for market

automation and liquidity fragmentation, the impact of proposed regulation and liquidity fragmentation and approaches being utilized to reaggregate swaps liquidity via SEF aggregation technology.

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