

Global Forex: The Rise of Retail

April 2010

FX trading volumes increased last year among only one type of financial institution: retail aggregators. The 16% growth in trading volumes among this segment in a year marked by stagnant levels of trading volumes among other users has made retail aggregators a much more important part of global FX markets. In 2008, retail aggregators accounted for 11% of worldwide FX trading volume; in 2009 that share increased to 12%.

Retail aggregators actually generate 28% of all spot transaction volume in global FX markets, up from 24% in 2008. What makes that proportion all the more impressive is the fact that the \$12 trillion in annual spot transactions generated by retail aggregators originate with just 32 corporations. “Those numbers indicate that retail aggregators generate some \$375 billion in spot transactions per capita every year — a figure that ranks them among the most active and important accounts in global foreign exchange markets,” says Greenwich Associates consultant Andrew Awad. “By way of comparison, the typical bank generates about \$75 billion in spot transactions each year.”

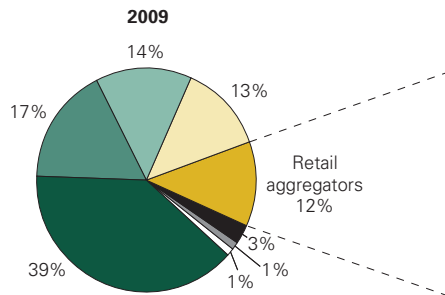
With the downturn in equity markets and high levels of volatility among global currencies, FX trading has gained popularity among retail investors around the world since the start of the global financial crisis. Benefitting from this trend have been the firms that provide execution services to retail traders, several of which have grown into some of the world’s biggest producers of FX trading volume.

The Return of Mrs. Watanabe

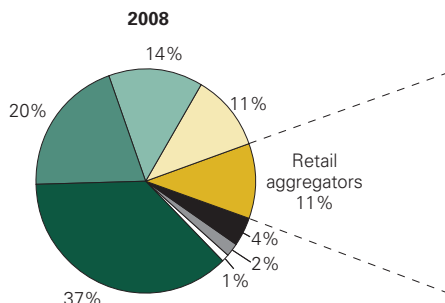
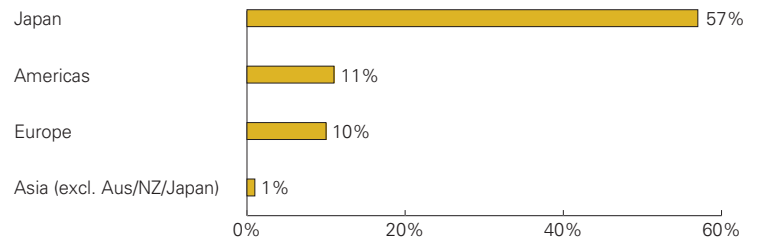
In terms of the popularity of foreign exchange among retail investors, few countries can match Japan, where the huge numbers of individual investors that originally entered the market to take advantage of the carry trade in the early 2000s became epitomized as “Mrs. Watanabe,” the metaphoric Japanese housewife/speculator.

The boom in retail FX trading in Japan has given rise to a host of retail aggregators. As a group, retail aggregators generated over half of the \$6.4 trillion in FX customer trading volumes in Japan in 2009, up from 27% in

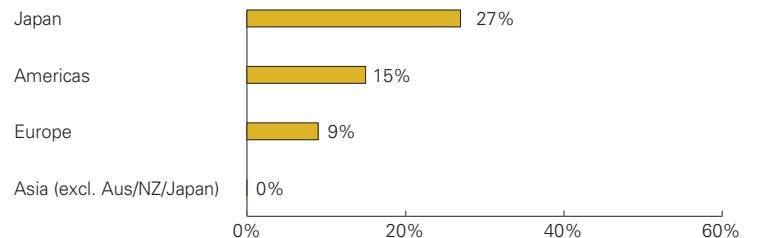
Significance of Retail Aggregators in Global FX Markets



Retail Aggregators Percent of Trading Volume by Region



Retail Aggregators Percent of Trading Volume by Region



Banks
 Fund managers
 Hedge funds
 Corporates
 Retail aggregators
 Other financials*
 Government agencies
 Insurance companies

Note: Based on responses from 1,497 respondents in 2009, and 1,437 in 2008. *Other financials includes broker/dealers and credit companies. Source: 2010 Global Foreign Exchange Study

2008. “Although retail trading volumes in Japan fell off considerably with the onset of the global financial crisis, they have since rebounded,” says Greenwich Associates consultant Tim Sangston. “The aggregators that service this retail business have become by far the biggest source of FX trading volume in Japan, easily outpacing banks, which produced 9% of total volume in 2009, and corporates, which generated 17%.”

The dominant role of retail aggregators sets Japan apart from other regional foreign exchange markets. Outside of Japan, retail aggregators represent only 9% of worldwide FX trading volumes.

Changes Ahead? Retail Forex Attracts Regulators’ Scrutiny

Retail foreign exchange trading is coming under increased scrutiny from regulators around the world. In the United States, the U.S. Commodity Futures Trading Commission has issued a proposal that would impose new requirements on retail brokers covering registration, disclosure, record keeping, financial reporting and operational standards. The provision that has generated the most controversy, however, is a proposal to cap the amount of leverage available to retail traders at a standard 10:1 ratio. Currently, the self-regulatory National Futures Association caps leverage ratios at 100:1 for major currencies and 25:1 for exotic currencies. Japan’s Financial Services Agency is moving in the same direction. New rules will reduce the amount of permissible leverage in that market to 50:1 this summer and then to 25:1 in 2011.

Critics of these moves contend that the imposition of such strict leverage limits would curtail retail trading activity within the U.S., but would do so mainly by driving retail investors offshore to countries like the United Kingdom, which currently has no limits on leverage and where at least one retail FX broker advertises leverage as high as 500:1. “In an era in which switching to an offshore broker requires little more than clicking to a new Web site and opening an account, this is a legitimate concern,” says Greenwich Associates consultant Peter Kane.

Greenwich Associates consultants Tim Sangston, Frank Feenstra, Peter D’Amario, Riccardo Cumerlato, Woody Canaday, and Peter Kane specialize in derivatives and foreign exchange.

Methodology

Greenwich Associates conducted in-person interviews with 1,497 top tier users of foreign exchange and 630 interest rate derivatives users at large corporations and financial institutions on market trends and their relationships with their dealers. Interviews were conducted in North America, Latin America, Europe, Asia, and Japan between September and November 2009.

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