Electronic Trading Growth in Convertible Bonds

November 14, 2024

Executive Summary:



Convertible bonds combine elements of bonds, stocks and derivatives, making them a unique asset class. Electronic trading has transformed the convertible bond market, driving improved execution quality, efficiency, and competition.

Coalition Greenwich research in 2020 examining the convertible bond market found that electronic trading had “wrought meaningful change, creating significant value for market participants.” In the years since, electronic trading adoption has accelerated, driving improved execution quality and additional efficiency for market participants.

An emphasis on best execution has led to increased interest in and use of multidealer platforms (MDPs). These electronic platforms provide a centralized hub for investors to compare prices across multiple dealers, increasing competition and driving down their trading costs.

Nearly one-third of convertible bond investors now trade convertible bonds electronically. Additionally, 13% who aren’t currently utilizing electronic trading expect to do so in the next two years.

As traders become more comfortable with electronic trading, they’re starting to place larger orders. Trades over $5 million are growing over 45% year over year on Tradeweb, one of the largest MDPs for U.S. convertible bonds.

Electronic trading offers benefits beyond improved execution quality, including pre-trade transparency, real-time executable prices and automation of manual processes. Dealers are integrating their internal systems with MDPs, leveraging the “buy, build, and integrate” approach. Convertible bond traders are now demanding the same tools and automation as their colleagues in other asset classes. With the right incentives and tools, even less-liquid products like convertible bonds can be traded electronically.

Methodology:

Between January and June 2024, Coalition Greenwich interviewed 141 investors at funds domiciled in North America and Europe that trade U.S. convertible bonds. Respondents were asked a series of questions about their activity in the U.S. convertibles market, including the proportion of convertibles volume executed via multidealer platforms, as well as key factors that are most important to the trader when deciding which broker to engage.

Data from Tradeweb, a multidealer platform operating an RFQ market for convertible bonds, was also analyzed to better understand market liquidity and participation.



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