

Reply to BLOG

This is DEGIRO's reply to an anonymous blogger on AmsterdamTrader regarding DeGiro as posted on September 17th. The blog is clearly written with only one purpose, which is writing a sensational story in an attempt to receive attention.

It is about the inhouse matching functionality of DeGiro. We go step-by-step through the blog in order to explain the actual situation beyond what he writes.

First introductory paragraph – no title

Main point of the first paragraph, and in fact repeated throughout the whole story, is that due to inhouse matching clients run counterparty risk instead of being cleared by a clearing like Clearnet. Here he mixes things up. Every broker has a net position at the clearing in the omnibus account in which the broker keeps the positions of the client. That means that for the safety offered by the clearing, the long and the short positions of various clients cancel out. This has really nothing to do with the way the trade is executed. Moreover, for many brokers the omnibus account storing the derivative positions of the client is in the name of the broker and therefore at risk if the brokerage firms defaults. This is not the case at DeGiro: it is in the name of Stichting DeGiro, the separate, custodial entity solely used to keep positions for clients. It is even better: non-leveraged buy and hold positions in securities are kept in a separate entity and separated at clearing level.

So the inhouse matching as is, nor the counterparty of the inhouse matched trade is in any way affecting the safety of the positions of the client. So the main point of the story is completely off.

This inhouse matching is also not as sensational as it seems, because – according to the order policy of IB as in the attachment – the same might happen at Lynx / Today's and Tradersonly. Moreover, the order policy of Binck speaks of "samenvoegen van orders".

So, DeGiro matches and enables clients to trade **within the bid-ask spread** of the market. So, in fact the execution is **enhanced** instead of becoming worse!

Indeed, this is efficiency, as for these trades DeGiro has not to pay external trade fees and it might not come as a surprise that all the **efficiencies together** explain why DeGiro is on average 80% cheaper than its competitor. To put things into perspective, currently around 90% of all transactions are executed on the primary exchanges.

Solid Evidence

This is a clear proof of one of the **perils of inhouse matching**. Due to the fact there is somebody else willing to sell the options, the client got a better (in this case : more liquidity) execution than he would have gotten in Euronext. On top of that this execution is efficient, so he only pays 85cts per contract. So, the execution is both better and transaction costs are lowest in the market available, clearly perfectly in line with the objective of the MiFiD regulation regarding best execution duties for brokers.

The position overview shows on what exchange the product is listed. In fact positions are not held at any exchange and the blogger, as a self appointed market maker, should know that.. In the PDF confirmations of the transaction, it is clearly visible for client that a trade is not executed at the exchange. In that respect, the trading venue is very transparent towards the client.

Clients tricked...

This is again the same argument, there is no central counterparty protection by a clearing for individual clients of a broker, that is entirely besides the point of the clearing system that clears the net positions of a broker against other clearing parties.

HedgeFund HiQ is on...

It is no secret that DeGiro is part of a group that also contains fund manager HiQ Invest. Moreover, DeGiro platform originates from brokerage for professional clients and as such it is not a surprise that, just like other professional clients, over 50 funds managed by HiQ are clients of DeGiro, including HiQ Market Neutral Fund. As DeGiro matches clients with clients, there will evidently be matches against HiQ Funds.

Client is counterparty instead of....

The comment about the margin call would mean that DeGiro communicates expected order flow of one client to another client. This is illegal and could lead to criminal prosecution, so not quite to be expected of a financial institution that is AFM licensed for almost 10 years.

Don't set the fox

Again, the same. This would be illegal. Orders are matched, no quotes are send around or arising from order activity of clients, so there is no way of other clients to know what orders or whose orders are coming in. Another wild accusation of a sensation seeking blogger.

Devastating for the market

Maybe the blogger means that he, as a market maker, wants to profit from the spread that our clients want to pay instead of letting DeGiro give this advantage to its own clients? It is really the case that due to our efficiencies we remove part of the easy money for the HFT and market making community. Instead of keeping this to our selves, we give it back in low fees. Our clients seem to love it.

DEGIRO acting as central counter party

Again the same misunderstanding of the blogger about the actual role of the clearing organization. DeGiro is not at all a CCP in the EMIR perspective, so this remark is really clueless.

Is it legal?

YES it is. DeGiro has been in talks with AFM from the beginning of offering its services to retail clients. Also the fact the inhouse matching is part of the offering has been extensively discussed. Clients are explicitly informed, please read the order execution policy, which is about executing orders and check out our PDF trade confirmations!

The blogger mentioned MiFiD 2017. As far as we understand it now, there is no rule in this new regulation that will change our current order execution policy.

Popcorn time

The tables are not turned at all. In case of the Binck/TOM case, there was a worse execution for the client, in this case the execution is better. This was the whole clue of the Binck/TOM disagreement.

Conclusion

DeGiro is in favor of transparency regarding its services, which is the main motivation for commenting to this BLOG. We really think that this reply contributes to the knowledge of the general public regarding inhouse matching, clearing and settlement. However, we are quite disappointed in the sensation-seeking nature of this blog. The fact that the blogger wants to be anonymous does not contribute to the transparency that is so clearly needed in the financial sector.

Appendix - IB Order Execution Policy (Lynx / Todays / TraderOnly)

IB UK ORDER EXECUTION POLICY Approach: IB UK's order execution policy is premised upon the principle that, for the combination of clients served and products offered, a client order is most likely to be executed at the optimal price, at the greatest speed and with the highest levels of accuracy and certainty of completion (i.e. "best execution") if that order is submitted via direct access to a fully automated market venue. Moreover, to the extent that an order is associated with a product listed on multiple market venues, "best execution" is achieved by reviewing the bids and offers at each of those venues in an automated manner and directly routing the order to the venue having either the most favorable price or the most favorable price net of execution costs. While automatically executed orders may not have an opportunity to be executed at a price better than the execution venue's posted bid or offer, they are not subject to being held by a market maker or specialist and executed at an inferior price or declined execution if the market moves in the client's favor while the order is pending. Given this background, IB offers clients two primary methods of routing orders to the market for execution. First, IB UK clients may provide specific instructions to directly route their orders through the IB trading platform to the order book of a particular venue of their choice. When this method has been selected, IB UK will be deemed as having satisfied its best execution obligation. Second, for products that are multiply listed, IB UK offers SmartRoutingSM a proprietary computerized routing algorithm that is designed to optimize both speed and price of execution by continuously scanning competing execution venues and automatically seeking to route the order to the best venue. Clients may select SmartRoutingSM based upon two criteria, the first being the most favorable price, and the second the most favorable price after taking into consideration execution costs. A general description of SmartRoutingSM including details as to how this execution method considers factors such as quote prices, speed and likelihood of execution, quote size, and nature of order along with the execution venues covered may be found at: www.interactivebrokers.co.uk Execution Venues: IB UK provides clients with direct access to a number of execution venues that have been selected based upon the level of relevance they maintain within their particular region in addition to factors such as product breadth, liquidity, electronic access, costs and speed and likelihood of settlement. These considerations, in the aggregate, are intended to provide a range of execution venues most likely to provide clients with best executions. While these venues will typically fall into the classification of Regulated Markets, they may also include other exchanges, Multilateral Trading Facilities, Systemic Internalisers, and third-party investment firms, brokers and/or affiliates acting as market makers or liquidity providers.