



Brazil's Sole Stock Exchange Must Prepare for Competition

By Becca Lipman
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ATS Brasil is fighting the establishment to stimulate industry growth and global investment opportunities.

If everything goes according to plan Americas Trading System Brasil (ATS Brasil), a joint venture between ATG and NYSE Euronext will launch a new Brazilian exchange in 2014. It's difficult to capture just how much things will change if they are successful.

Brazil was once a multi-exchange market until the São Paulo exchange bought up the other regional exchanges and became a monopoly. As the sole stock-exchange operator BM&F Bovespa has reigned for years, setting the tone for trade in Brazil - to the decided detriment of various parties.

The issues with Bovespa are standard enough. The exchange does not have many companies listed, and it's not easy for retail investors to get in. In terms of technology, it is functional but far from state of the art, causing many high frequency traders to complain about speed and abandon the market. Bovespa's systems require every broker that uses their system to have an Oracle database that costs \$300-400 thousand per year to run.

A law from the CVM (Brazil's equivalent to the SEC) says exchanges must have some sort of risk measure. High frequency traders typically go through a global brokers, using some risk feature that will check and execute the order. Bovespa later required traders to go through their own risk system, which processes trades at the same speed. Those who invested in speed lost their edge, leaving HFT disenamored with Brazilian trading.

Brazil's growth economy is poorly represented by its exchange. Since the 1970's the Bovespa has listed only around 360 companies, putting Brazil in 23rd place world-wide in the range of Vietnam and Mongolia. About 52% of trading volume is on only ten stocks. Brazil has 195 million people, only 580,000 have ever owned a stock, and the number of people that trade at least once a month is around 200,000, or .31% of the total population. On that metric, compared to other countries, they are 41st in the world, behind Ghana, Zambia and Kenya. Bloomberg found Bovespa has one of the largest bid-ask spreads worldwide.

A couple years ago regulators started to take a look into opening the markets to other exchanges and a study was commission to assess the need. The study found the cost of trading some asset class is 27x more expensive than the US asset class, sparking a public hearing with members of the public markets, intermediaries, exchanges and banks. The decided opinion was that the market was going to open for competition.

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Bringing the Competition

Enter ATS Brasil, the first viable competitor to Bovespa. For a year they have been dealing with regulators and on June 18 the firm filed its formal request to CVM and expects approval by mid February. They are running testing and working with regulators to get the exchange right.

"We are fighting the establishment, which is not easy," says ATS Brasil CEO Alan Gandelman in an interview. "We're breaking a monopoly that has existed for a while. Bovespa is extremely profitable, it has margins around 70%, and we are pushing hard to be able to launch the new exchange by the 4th quarter of 2014."

Gandelman explains the biggest problem for other exchanges to get into Brazil is that Brazil's CBLC (Clearing and Depository Corporation) is owned by Bovespa. When asked at first to open up the clearing venue for competition, they declined, saying they have preparations and integrations to do prior to before working with third parties. Gandelman is skeptical that will get sorted out. "We don't think they're capable of delivering to another exchange. If it was only a time constraint, maybe, but knowing how their technology is we decided to create our own clearing."

That has led to more talks with the Central Bank of Brazil about what it takes to do their own clearing. They are about to file for a clearing license, at the end of the day ATS expects to have two companies, the ATS exchange and the ATS clearing company, with an independent structure providing clearing services for other exchanges in Brazil.

All of this change opens the door to new technologies, new markets, and investment opportunities. ATS is excited by these possibilities, and plans to leverage NYSE technologies. For example, they will also be the Universal Trading Platform (UTP) developed by NYSE, which Gandelman says is 4-5 times faster than the current system. "We will have connectivity with brokers. Brokers will connect with us, as will existing systems of Bovespa, and our systems can

read the Bovespa connections. Everything is interconnected." Brazilian law requires interconnectivity between trading houses and exchanges if there are more than one.

ATS Brasil is exploring having data in clouds and other database alternatives to compete with Bovespa's expensive Oracle system requirements. Gandelman also believes their technology will be able to take the full speed of high frequency traders needing risk measurements, and allow traders to go back to whatever risk system they have to be checked and approved.

"Cost are too high, liquidity is too low, and there are not enough retail players in the market. The technology could be better, and our offer plays into that," says Gandelman. "It's a commercial opportunity, yes, but it's also a need for the finance community. Also, we're sure that we're going to raise the bar by getting in with state of art technology... For Bovespa to compete with us they will have to be better and faster."

He adds that Bovespa will benefit from new customers, including HFT traders attracted by the exchange's abilities to handle higher speeds. In the first stage, ATS will just be handling cash equities and ETFs, customers will trade other assets on Bovespa. "The whole chain benefits from our competition." ATS Brasil seeks to secure approximately 10%-15% of Brazilian equities trading by the end of 2015.