

Hosting services whitepaper

In this whitepaper Elise M. Fleischaker of Trading Technologies examines the growing use of hosting services among trading organizations and explores some of the primary benefits provided by these solutions.

Any organization operating its own trading network knows that tremendous effort goes into building, maintaining, monitoring and troubleshooting such an extensive mission-critical operation. With traders' livelihoods, customer relationships and significant amounts of capital riding on the network's performance and reliability, constant pressure is exerted on IT staffers to keep everything running smoothly, at optimal speed, all the time – with no exceptions.

The current economic environment only adds to that pressure. Given recent bank failures and market uncertainty regarding those that remain, customers need reassurance that their technology providers are secure.

Nobody can deny that trading volumes in recent years have exploded, generating massive increases in quoting and market data traffic that have put trading networks under stress never seen before. Part of that volume and quoting surge can be attributed to the growing use of algorithmic trading, which further taxes these networks.

Growth is coming from all corners of the world, not just via traditional financial centers like Chicago, New York and London. Market volatility is attracting new participants from emerging and frontier markets. Now a firm's trading infrastructure

must serve the needs of traders situated in extremely remote locations, as well as those who trade from gleaming office towers within major metropolitan areas.

The current economic environment throws new challenges into the mix. The subprime fallout is putting urgent pressure on banks and others to deliver steadfast quality while reducing costs. Amidst recent bank failures and falling trust in the banks that remain, hedge funds, commercial firms and other trading institutions need reassurance that their technology providers are secure. A bank's decision to decouple technology from clearing can significantly reduce both operational risks and costs. A firm's choice to outsource trading infrastructure to a well-capitalized, economically viable third-party hosting provider can have a significant positive impact on customer confidence.

The Hosting Services Landscape

From a big picture perspective, third-party hosting services are a well-established model. Companies have used them for years to outsource management of their websites, email, CRM systems and other functions.

Within the trading industry, hosting services have been around for many years. Independent software vendors (ISVs) like GLTRADE, TradeWeb and Trading Technologies (TT) offer full-service trading-network hosting operations that can provide 24/7 monitoring, failover and co-location services. The rising need for outsourced services has also brought on the emergence of boutique firms that specialize in some aspect of hosting or IT service outsourcing, among them 7 Ticks, Firmus Group and YJT Solutions.

While some hosting solutions for the trading industry have existed since the beginning of this decade or longer, firms were not immediately eager to embrace hosting when it first arrived. Many wanted to retain control of their networks, which they deemed proprietary, while others felt their internal IT teams were better qualified than a vendor to manage this critical business function.

But as benefits of hosting became apparent and trading volumes grew at an ever-increasing rate, the industry recognized a need and began to undergo a sea change, which is still underway. Now many of the world's leading players – including several of the largest global banks, clearing houses and trading firms – utilize third-party

hosting services to manage their trading networks.

Why Opt for Hosting?

Many organizations choose to utilize the services of a hosting provider because these experts can achieve optimal trading network performance and stability. Hosting networks with fast, highly resilient, fully redundant connections to the exchanges can deliver maximum uptime through shared facilities in multiple continents. A fully redundant cross-connect architecture that leverages high capacity circuits can yield higher availability and performance. Services built on a multi-gigabit fiber-optic backbone can supply datacenter failover and intra-site redundancy. Hosting providers make sizable investments in location and connectivity diversity to offer the most stable, available and disaster-resistant exchange connections possible. All of this is enhanced with leading-edge monitoring techniques, which ensure early detection and prevention of outages.

Hosting services also offer co-location services for clients who demand minimal system latency. Placing trading gateways as close as possible to the exchanges provides orders with exceptionally fast access to the exchanges' electronic matching

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engines. With more firms adopting algorithmic and black-box trading, and with latency demands being measured in microseconds rather than milliseconds, the benefits of co-location placement can have a measurable impact and drive further adoption of hosting.

Companies that distribute trading screens to external customers as well as internal trading desks have a great deal at stake. These firms often find the benefits of performance and stability to be the primary drivers behind the decision to go with a hosted solution.

As Salvatore Ventura, head of the services organization for Credit Suisse Prime Services, explained when Credit Suisse announced it had moved to TT’s TTNET solution, “Our major energy and commodity hedge fund clients in prime services demand high performance trading solutions and our partnership with TT enables us to provide an additional solution to meet their demands. TTNET provides a high performance solution that our customers require.”

BNP Paribas Commodity Futures’ Managing Director, Louis Caiafa, echoed this sentiment. When BNP Paribas revealed in the summer of 2007 that it has chosen TT’s hosting solution, Caiafa was quoted as saying, “In response to increasing demand from our major energy and institutional clients for a high performance trading solution, we are pleased to partner with TT to access electronic derivative markets across the globe. We chose to deploy via TTNET because it provides the scalable and full-failover solution that our customers require.”

Choosing an ISV’s hosting service can benefit a firm by taking a great deal of pressure off its IT department. This is especially true if an organization trades numerous asset classes, and uses multiple systems for each asset class. In this scenario, it would be very costly for an IT group to maintain enough staff and expertise to effectively manage each of those platforms. Hosting can relieve this burden by placing all aspects of network administration, hardware configuration, infrastructure maintenance, data line management, upgrades, backups, security and user support into the hands of the experts who know the software better than anyone else. The ISV’s specially trained and highly qualified technicians perform all required system maintenance and upgrades, freeing up the customer’s IT organization to focus on its core areas of expertise.

This savings of time and the ability to focus on core business processes are common benefits reported by those that utilize hosting services of all types. A recent customer survey published by hosting provider Rackspace Hosting reported that more than 40% of the respondents said outsourcing their IT functions to a hosting service saved 30–50% of their time. As a result, 44% of those respondents said they estimated they could spend at least 25% more time on new projects because

of the time saved due to outsourcing. Clearly if trading firms realize a similar cost savings, the impact of hosting is significant.

Hosting also permits firms to easily distribute trading screens to customers around the world from the hosting provider’s hubs using Internet and private lines. A large dedicated hosting solution might employ a seamless architecture that is fully redundant and highly scalable up to hundreds of servers, allowing firms to roll out installations in customer-driven phases and quickly connect new traders in various locations as needs dictate. When the distribution of software is handled through the hosting service’s existing high-bandwidth lines and servers, firms can add new screens without lengthy, disruptive and expensive implementations. A hosting solution lets customers take advantage of shared exchange circuits, saving the considerable cost of ordering private exchange lines. The lines are already in place, so there’s no waiting for exchange line installation. The process is extremely rapid and very cost-effective.

Outlook

So will more firms outsource their trading infrastructure to hosting providers, or will this trend reverse? Industry pundits foresee no reduction in the utilization of hosted trading networks. Conversely, demand is forecast to rise. Some experts even see hosting as a necessary offering among ISVs. According to Paul Zubulake, a senior analyst in futures and options with Boston-based research firm Aite Group, “Firms who do not provide a co-location solution for their customers will be at a competitive disadvantage as the high-volume, low-latency proprietary trading shops now require nearby server proximity to the exchange’s matching engine. The vendors who provide a hosted solution for their clients will be the probable choice of the brokerage and trading community.”



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