

Best Execution - Policy and Procedures

1 Background

- 1.1 Under MiFID (the Markets in Financial Instruments Directive, implemented in the UK in November 2007), all firms have a duty to ensure they achieve best execution for retail and professional clients.
- 1.2 MiFID defines best execution not only in terms of price but also in relation to other factors including:
 - costs
 - speed
 - size
 - likelihood of execution and settlement
 - nature
 - “any other relevant consideration.”
- 1.3 Regulators had the equity markets primarily in mind when promulgating the rules on best execution but it is recognised that there are significant differences between equity and fixed income markets. In particular:
 - All ECM bond, loan and swap trades are traded OTC, not on exchange. It is noted however that in the future, trades may be exchange traded.
 - Liquidity in fixed income markets varies depending on a security’s asset class or credit rating and the prevailing market conditions in that particular asset class.
 - Portfolio Managers (PMs) need to exercise caution when seeking competitive quotes in the market because they may alert the market that the firm is potential buyer/seller of a particular security and this can turn the price against the firm i.e. if it become known that ECM is a seller, the price could fall; if it becomes known that ECM is a buyer, the price could rise.
 - For swap trades, competing quotes are not always obtained. This may be because there is only one counterparty available, or because the size of the trade makes it impractical to do so. Live prices are always compared to quoted prices to ensure reasonableness.
 - Timing is crucial – in a fast moving market, prices may not remain stable long enough to give the PM time to conduct a full price survey of the market before deciding with whom to execute. In this situation, it is more efficient for the PM to make a judgement as when to accept a quoted price, without necessarily having had the opportunity to approach all potential counterparties.
- 1.4 Primary issues – a fixed price is set by the lead bank organising the issue so there is no scope for seeking competitive quotes.
- 1.5 Secondary market
 - The range of counterparties available will vary greatly according the specific sub asset class to which a security belongs.
 - Deals may either be “on-the-run” (most recent issue of a security)) or “off-the-run” (earlier issues of a security). On-the-run issues are generally quoted by a wider range of market participants and therefore tend to be more liquid and have a narrower bid/offer spread than off-the-run issues.

Dated 17/07/2013

- Banks and brokers distribute runs of indicative prices throughout the day via Bloomberg.
- The firm can also approach counterparties directly to gauge any interest in making a market in a security. This will particularly be the case if we believe the trade is likely to have specific interest with a particular counterparty eg it has previously indicated that it is interested in buying or selling a particular security.

1.6 ECM may only use counterparties that are on the firm's list of Approved Counterparties. ECM performs its own due diligence procedures over potential counterparties; these are then proposed to CACEIS who has the final approval authority for adding counterparties onto the list in relation to ECM's SPV clients, such as the Luxembourg and Dublin vehicles. For swap counterparties, ECM is limited by the rating limit requirement for counterparties as specified in each prospectus.

2 How ECM achieves Best Execution

2.1 The performance fee structure of the funds incentivises the firm to achieve best execution, i.e. fees are based on performance net of all fees and charges. There is also the desire to achieve performance targets in order to attract new clients and retain existing ones.

2.2 ECM deals on a nil commission basis and does not participate in soft commission arrangements, so there is no incentive for the firm to direct business to counterparties offering commission based incentives to the detriment of the net price payable to/by the client.

2.3 Lead PMs have accountability for their own portfolios, including achieving best execution in relation to all transactions performed on behalf of the portfolio. However, the majority of trades are executed by the specialist PMs as they have detailed knowledge of the appropriate markets but these prices are reviewed by Lead PMs to ensure best execution has been obtained on a reasonableness basis. Similarly, the PMs trading swaps have responsibility for the returns of the funds, so are incentivised to ensure best execution at all times.

2.4 Traded prices are reviewed relative to the most recent prices used to value the portfolio. The ECM Deal Ticket system highlights trade prices which are more than a pre-determined margin away from that valuation level.

2.5 When placing an order for a bond or a loan, the PMs have the option of nominating whether the trade should be done on a "Best Execution" or at a "Target Level" basis. Best Execution basis means that a trade will be executed at the best price quoted; Target Level basis will specify the price or spread at which the trade must be executed and once a counterparty offers the target price/spread, the deal is executed. Swap hedges are always traded based on Best Execution.

2.6 The traditional method of achieving best execution, i.e. contacting a number of counterparties for a quote, can sometimes be problematical in credit markets as this could potentially alert the marketplace as to the firm's intentions and therefore jeopardise the portfolio manager's ability to obtain the best price possible. ECM utilises the expertise, experience and market knowledge of its PMs when deciding with which counterparties to do business and the extent to which it is advisable to search for competing quotes.

Dated 17/07/2013

- 2.7 On a periodic basis, the Head of Compliance, the Co-Chief Investment Officer, and the Head of Rates and Treasury Management will review the Approved Counterparties list and volumes of business executed with counterparties for appropriateness. They are also reviewed periodically by credit research for credit worthiness.
- 2.8 For more liquid credit asset classes, it is possible to compare against indicative prices available from electronic trading platforms to demonstrate the reasonableness of the price obtained. Similarly, live swap prices are available from multiple sources.
- 2.9 For bond trades, ECM can use client driven electronic trading platforms such as TradeWeb, although these are currently only typically available for small trade sizes (typically up to €1 million). These systems generally invite quotes from a range of different counterparties, giving the PM the option to select the most appropriate quote. The PM may also choose to obtain quotes from known counterparties in addition to the electronic quotes. For swap and FX trades, electronic trading platforms are used extensively. The number of counterparties on the platform dictates whether best execution can be evidenced.