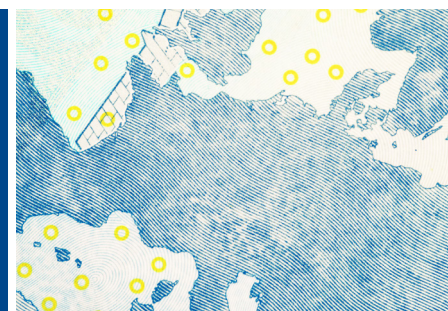


# Currency solutions Q&A: Fiduciary FX



## 1. What is fiduciary foreign exchange?

Fiduciary foreign exchange is an enhancement of the agency foreign exchange approach for trading foreign exchange to settle international trades, to convert foreign income such as dividends, and to hedge currency risk.<sup>1</sup> An agent trades on behalf of its client (typically an institutional investor such as an asset owner or asset manager), seeking the best terms at the time of the transaction. The agent is compensated with an agreed-upon fee for its service. An agent who is also a fiduciary has an ethical and legal responsibility to act in the investor's best interests. Agency and fiduciary roles contrast with principal dealing, the traditional means for trading foreign exchange.

## 2. What is principal trading?

A principal, or market maker, uses its own capital to trade with its customers. Because the principal is dealing from its own account, it has an incentive to get the best deal for itself. Unfortunately, a good deal for the market maker is a bad deal for the customer.

## 3. What is the fee for Fiduciary FX and how does that compare to fees for principal trading?

A fiduciary will trade for a fully disclosed nominal fee. The fiduciary will provide trading reports so that customers can verify the fiduciary's pricing. Principal trading can vary broadly from just a few basis points to double-digit basis points, depending on certain factors such as the type of trading (e.g., converting dividends is more expensive than trading to settle a security transaction) and whether the investor negotiates the transaction or allows the principal to trade without oversight.

## 4. Given the wide range in costs, why trade with a principal and not the fiduciary?

An investor might trade with a principal because of convenience and simplicity. Given the profits in trading, principals make it easy for investors to trade with them. It's much like shopping at a convenience store: efficient, but expensive.

## 5. How does Fiduciary FX work?

At its simplest, an investor sends an order to the fiduciary. The fiduciary manages the trading and settlement of the order. At the end, the fiduciary sends the trade results back to the investor so that the investor can update its systems and accounts.

More specifically, agents will net the order with other investor activity, minimizing the amount that has to be traded in the market and keeping costs low. The fiduciary will seek the best price possible given constraints with the order. When the deal is done, the fiduciary sends an electronic message to the investor's custodian so that the custodian is prepared to exchange currencies on settlement day. The fiduciary manages the settlement process, addressing issues that might arise. Periodically, the fiduciary provides a third-party transaction cost analysis report, giving the investor an objective assessment of the fiduciary's effectiveness.

The investor doesn't participate in the process except to deliver orders and receive the execution results.

## 6. Sounds straightforward. But what if something goes wrong?

Assuming the order was accurate, the fiduciary is responsible for issues that arise from its trading and settlement efforts. That responsibility extends from order receipt to settlement to delivery of the execution results to the originator of the order.

## 7. Getting back to the differences between principal and fiduciary; maybe a principal's convenience and simplicity makes trading with it worthwhile. What trading complexities do Fiduciary FX participants face?

Fiduciary FX trading can be more complex because the fiduciary trades with many banks on behalf of several customers. However, fiduciaries can appropriately manage that complexity (and thus decrease operational risk) by investing in technology, systems and staff and designing its trading processes to minimize the risk of error. The fiduciary has an incentive to manage complexity and risk because customers will typically hold the fiduciary responsible if an error occurs.

## 8. So a fiduciary can offer low costs and keep risk under control. What are some other benefits?

One benefit is reporting. Reporting is a key component of a well-managed trading program. Quality reporting describes how much has been traded, with whom the fiduciary traded, and at what cost. More detailed information shows each transaction and the associated cost. Comprehensive information helps investors manage an important component – foreign exchange trading – of its overall trading program. Some agents may provide their own transaction reports, but clients should require a report from a third-party for an unbiased and objective view of the fiduciary's trading expertise.

## 9. What else is important in currency trading?

We believe agency trading is superior to principal trading, and many other investors do too.<sup>2</sup> Principal traders have responded to the loss of business to agency trading by developing an agency offering.<sup>3</sup> That may be a legitimate service, but investors have to be careful because banks that offer agency and principal trading services may have conflicts of interest. That is because the bank is managing its own risk as well as the risk of its clients. Make sure to read the fine print in the agreement. Ask questions to ensure that the agent is a 'pure' one (meaning the agent doesn't trade with an affiliated desk) and that clear barriers exist between the principal and agency trading units to avoid information leakage and or market manipulation.

## 10. The potential conflict between agent and principal sounds a bit worrisome. What can I do about it besides reading the fine print?

We think agency trading is popular because it improves the trading experience. Investors might gain additional confidence that their investment requirements are being handled with the investor's interest foremost in the service provider's mind by hiring an agent who is also a fiduciary. By choosing a fiduciary to manage assets, asset owners can be more confident that the service provider has an ethical as well as legal responsibility to put the asset owners' interests before the interests of the service provider.

Investors should also require foreign exchange service providers to be signatories to the FX Global Code, [globalfx.org/docs/fx\\_global.pdf](http://globalfx.org/docs/fx_global.pdf), a set of global principles of good practice in the foreign exchange market.

---

### About Mesirow

Mesirow is an independent, employee-owned financial services firm founded in 1937. Headquartered in Chicago, with locations around the world, we serve clients through a personal, custom approach to reaching financial goals and acting as a force for social good. With capabilities spanning Global Investment Management, Capital Markets & Investment Banking, and Advisory Services, we invest in what matters: our clients, our communities and our culture.

To learn more, visit [mesirow.com](http://mesirow.com) or contact Joseph Hoffman at 312.595.7019 or [joseph.hoffman@mesirow.com](mailto:joseph.hoffman@mesirow.com).

1. As an example, suppose a foreign investor buys a Japanese security on a Japanese exchange. The investor would need to pay yen for the security and so would sell its home currency (say euros) and buy yen. The fiduciary manages this trade (sell EUR and buy JPY) on behalf of the investor. When the investor sells the security, the fiduciary would do the reverse trade: sell JPY and buy EUR for the investor's account.
2. Bakie, John. "Benchmark Change Drives FX towards Agency Model." *The Trade*, 16 July 2015, [www.thetradenews.com/Asset-Classes/Foreign-exchange/Benchmark-change-drives-FX-towards-agency-model/](http://www.thetradenews.com/Asset-Classes/Foreign-exchange/Benchmark-change-drives-FX-towards-agency-model/).
3. Baert, Rick. "Shadow of MiFID II is Falling on FX Trading Transparency." *Pensions & Investments*, 11 December 2017, <http://www.pionline.com/article/20171211/PRINT/171219956/shadow-of-mifid-ii-is-falling-on-fx-trading-transparency>.

Past performance is not an indication of future results. Actual results may be materially different from the results achieved historically. Nothing herein is meant to be taken as a recommendation to buy or sell a particular asset or invest in a particular strategy. Mesirow Currency Management ("MCM") is a division of Mesirow Financial Investment Management, Inc. ("MFIM") a SEC registered investment advisor, a CFTC registered commodity trading advisor and a member of the NFA and Mesirow Financial International UK, Ltd. ("MFIUK"), authorized and regulated by the FCA. The information contained herein is intended for institutional clients, Qualified Eligible Persons and Eligible Contract Participants or the equivalent classification in the recipient's jurisdiction and is for informational purposes only. This information has been obtained from sources believed to be reliable, but is not necessarily complete and its accuracy cannot be guaranteed. Any opinions expressed are subject to change without notice. It should not be assumed that any recommendations incorporated herein will be profitable or will equal past performance. Mesirow does not render tax or legal advice. Nothing contained herein constitutes an offer to sell or a solicitation of an offer to buy an interest in any Mesirow investment vehicle(s). Any offer can only be made through the appropriate Offering Memorandum. The Memorandum contains important information concerning risk factors and other material aspects of the investment and should be read carefully before an investment decision is made.

**Australian Investors:** The information contained herein is intended for Wholesale Clients only and is for informational purposes only. This document is not a prospectus or product disclosure statement under the Corporations Act 2001 (Cth) (Corporations Act) and does not constitute a recommendation to acquire, an invitation to apply for, an offer to apply for or buy, an offer to arrange the issue or sale of, or an offer for issue or sale of, any securities or investment service in Australia, except as set out below. The strategy has not authorised nor taken any action to prepare or lodge with the Australian Securities & Investments Commission an Australian law compliant prospectus or product disclosure statement. Accordingly, this strategy and document may not be issued or distributed in Australia other than by way of or pursuant to an offer or invitation that does not need disclosure to investors under Part 6D.2 or Part 7.9 of the Corporations Act, whether by reason of the investor being a 'wholesale client' (as defined in section 761G of the Corporations Act and applicable regulations) or otherwise. This document does not constitute or involve a recommendation to acquire, an offer or invitation for issue or sale, an offer or invitation to arrange the issue or sale, or an issue or sale, of any strategy or investment service to a 'retail client' (as defined in section 761G of the Corporations Act and applicable regulations) in Australia.

**Canadian Investors:** The information contained herein is intended for Permitted Clients only and is for informational purposes only. This confidential material pertains to the offering of the currency strategies described herein only in those jurisdictions and to those persons where and to whom they may be lawfully offered for sale, and only by persons permitted to sell such strategies. This material is not, and under no circumstances is to be construed as, an advertisement or a public offering of the strategies described herein in Canada. No securities commission or similar authority in Canada has reviewed or in any way passed upon this document or the merits of the strategies described herein, and any representation to the contrary is an offence.

**Netherlands and Luxembourg Investors:** The information contained herein is intended for Professional Clients as the term is defined by MiFID II and is for informational purposes only. Recipients that are classified under MiFID II as retail clients must opt up to Professional Clients before receiving any services from Mesirow Financial Currency Management.

**Japanese Investors:** Mesirow Financial Currency Management provides discretionary investment management services to managed accounts held on behalf of qualified investors only. MCM will not act as agent or intermediary in respect of the execution of a discretionary investment management agreement. Please note that this presentation is intended for educational purposes and solely for the addressee and may not be distributed.

**Hong Kong Investors:** The contents of this document have not been reviewed by any regulatory authority in Hong Kong. You are advised to exercise caution in relation to the contents of this document. You should obtain independent professional advice prior to considering or making any investment. The investment is not authorized under Section 104 of the Securities and Futures Ordinance of Hong Kong by the Securities and Futures Commission of Hong Kong. Accordingly, the distribution of this Presentation Material and discretionary management services in Hong Kong are restricted. This Presentation Material is only for the use of the addressee and may not be distributed, circulated or issued to any other person or entity.

**South Korean Investors:** Upon attaining a client, Mesirow Financial Investment Management, Inc. ("MFIM") will apply for the appropriate licenses and retain the services of a local licensed intermediary (a Korean financial investment company). In the interim, MFIM will rely on and sub-delegate to Mesirow Advanced Strategies, Inc. ("MAS").

**Singapore Investors:** Mesirow Financial Currency Management provides discretionary investment management services to managed accounts held on behalf of qualified investors only. MCM will not act as agent or intermediary in respect of the execution of a discretionary investment management agreement. Please note that this presentation is intended for educational purposes and solely for the addressee and may not be distributed.

**Swiss Investors:** Services are only offered to Regulated Qualified Investors, as defined in Article 10 of the Swiss Collective Investment Scheme Act. There can be no guarantee investment advice will be profitable or meet its investment objectives.

**UAE Investors:** This information does not constitute or form part of any offer to recommend, issue or sell, or any solicitation of any offer to subscribe for or purchase, any securities or investment products or strategies in the UAE (including the Dubai International Financial Centre and the Abu Dhabi Global Market) and accordingly should not be construed as such. Furthermore, this information is being made available on the basis that the recipient acknowledges and understands that the entities and securities to which it may relate have not been approved, licensed by or registered with the UAE Central Bank, the Dubai Financial Services Authority, the UAE Securities and Commodities Authority, the Financial Services Regulatory Authority or any other relevant licensing authority or governmental agency in the UAE. The content of this report has not been approved by or filed with the UAE Central Bank, the Dubai Financial Services Authority, the UAE Securities and Commodities Authority or the Financial Services Regulatory Authority.

**United Kingdom Investors:** In the United Kingdom, this communication is directed only at persons who fall within the definition of: (i) "investment professionals" as defined in COBS 4.12 and Article 14 of the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (the "PCISE Order"); or (ii) "high net worth companies, unincorporated associations etc" as defined in COBS 4.12 and Article 22(2)(a) to (d) of the PCISE Order (all such persons together being referred to as "Relevant Persons"). This communication must not be acted on or relied on by persons who are not Relevant Persons. Any investment or investment activity to which this communication relates is available only to Relevant Persons and will be engaged in only with Relevant Persons.

Mesirow refers to Mesirow Financial Holdings, Inc. and its divisions, subsidiaries and affiliates. The Mesirow name and logo are registered service marks of Mesirow Financial Holdings, Inc., © 2022, Mesirow Financial Holdings, Inc. All rights reserved. Investment management services provided through Mesirow Financial Investment Management, Inc., a SEC registered investment advisor, a CFTC registered commodity trading advisor and member of the NFA, or Mesirow Financial International UK, Ltd. ("MFIUK"), authorized and regulated by the FCA, depending on the jurisdiction.