

## FINalternatives Survey: High-Frequency Trading Has a Bright Future



By Irene Aldridge -- High-frequency trading has grown exponentially in the past several years, and, according to the *FINalternatives* 2009 Technology and High-Frequency Trading Survey, that growth is here to stay.

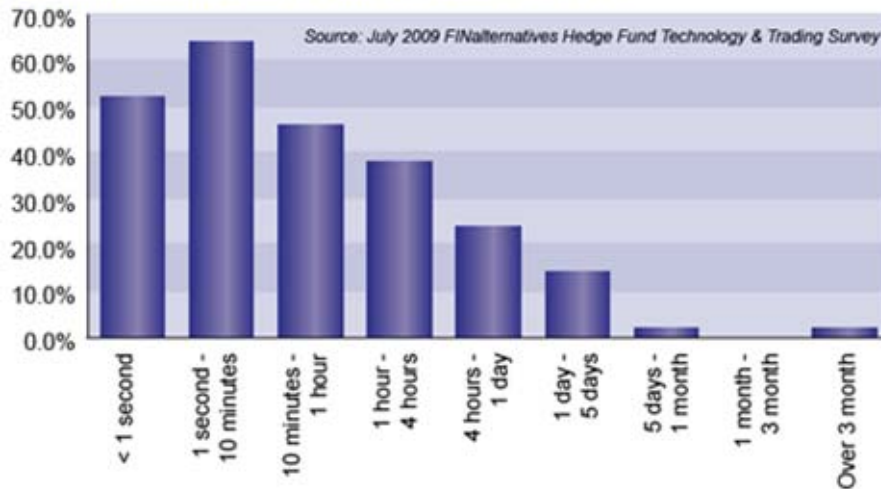
A whopping 90% of respondents think that HFT has a bright future. In comparison, only half believe that the investment management industry has favorable prospects, and only 42% have a positive outlook when it comes to the U.S. economy. Given that dose of pessimism, it should be noted that HFT tends to work particularly well in volatile range-bound markets like the current economic environment.



**[0]Hedge Fund Technology & Trading**The optimism for HFT—which research firm Tabb Group estimates accounts for 73% of equities trading volume on U.S. exchanges—is bound to bring additional skill and capital to the high-frequency arena. At present, many financial industry participants understand the business of HFT, yet few understand the details and implementation involved. Some 39% of hedge fund managers, investment advisers, executing brokers and proprietary traders have just “a little” understanding of the high-frequency business, according to the *FINalternatives* survey, with 52% reporting a solid understanding. By contrast, only 40% of the respondents report that they had a solid grip on the implementation of HFT, with 19% reporting no understanding of implementation tactics whatsoever.

The outlook for HFT is largely driven by the high profitability potential of well implemented HFT systems. While traditional buy-side trading strategies hold positions for weeks or even months, HFT is characterized by fast turnover of capital. Instead of capturing large price changes over extended periods of time, HFT aims to book multiple small gains over short periods of time. An overwhelming 86% believe that the term “high-frequency trading” referred strictly to holding periods of only one day or less.

### Distribution of responses to the question "What position holding time qualifies as HFT?"



Intra-day position management is important for two reasons: savings from the overnight position carry costs and elimination of the overnight risk. The carry is the cost of holding a margined position through the night; it is usually computed on the margin portion of account holdings after the close of the North American trading sessions. Overnight carry charges can substantially cut into the trading bottom line in periods of tight lending or high interest rates.

Second, closing down positions at the end of each trading day also reduces the risk exposure from the passive overnight positions. Smaller risk exposure again results in considerable risk-adjusted savings.

In addition to high capital turnover and intraday entry and exit of positions, the FINalternatives survey respondents further identified the following key distinctions of HFT:

- Trading decisions made upon tick-by-tick data analyses; and
- Algorithmic trading.

Tick-by-tick data processing and high capital turnover do indeed define much of HFT. Identifying small changes in the quote stream sends rapid fire signals to open and close positions. The term "high-frequency" itself refers to fast entry and exit of trading positions, the process best executed by algorithms and dedicated computer programs employing artificial intelligence.

Only 51% of the respondents report using HFT at present, but 60% of the respondents indicate that they intend to use HFT in the future.

The FINalternatives survey garnered 202 responses, of which half worked for a hedge fund, 26% for an investment advisory or consulting firm, 12% for a fund of hedge funds, and smaller numbers for executing brokers, proprietary traders, mutual funds, research providers, technology firms and family offices. Some 59% said that portfolio management is their primary responsibility.

*Irene Aldridge is an expert in algorithmic and high-frequency trading. Her new book High-Frequency Trading: A Practical Guide to Algorithmic Strategies and Trading Systems (Wiley Trading, ISBN: 978-0470563762) is available for [pre-order on Amazon.com](http://www.amazon.com) [1]. She can be reached at [ialdridge@ablealpha.com](mailto:ialdridge@ablealpha.com) [2].*

---

#### Source URL:

<http://www.finalternatives.com/node/8583>

**Links:**

[1] [http://www.amazon.com/High-Frequency-Trading-Practical-Algorithmic-Strategies/dp/0470563761/ref=sr\\_1\\_1?ie=UTF8&s=books&qid=1248267633&sr=8-1](http://www.amazon.com/High-Frequency-Trading-Practical-Algorithmic-Strategies/dp/0470563761/ref=sr_1_1?ie=UTF8&s=books&qid=1248267633&sr=8-1)

[2] <mailto:ialdridge@ablealpha.com>