Forex Brokers: ONE SIZE DOESN'T FIT ALL


Ella Fuller
GCI Trading

In the words of Henry Ford "any customer can have a car painted any colour that he wants so long as it is black." In the Forex industry the 'one size fits all' approach is, however, definitely not applicable. Ella Fuller, Head of Marketing at GCI Trading explores what questions you should be asking when selecting a Forex Broker.

As with all industries, (automotive, telecom, computer, pharmaceutical, etc.) the Forex industry began with a few pioneers offering online trading to the early-adopter market. But over the last 10 years, the demand for online trading has skyrocketed. Some came to online trading because of discontent with the bailout-ridden equity markets that no longer resemble the "free market" value a savvy investor can project. Others found online trading as a means of taking control back from "hedge funds" or "money managers" whose accountability and information sources are questionable. The result has been an influx of disparate investors who want to take trading and investing into their own hands.

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Eager to meet this demand have been a bevy of new Forex Broker entrants – most of them copycats, with little differentiation – hoping to gain a slice of this fast-growing market. However, the natural and healthy process of free-markets responding to evolving demands led to classic sub-segmentation with the successful brokers abandoning the "one size fits all" Forex model in favor of niche offerings aimed at meeting the needs of specific traders. As expected, the brokers that have not repositioned themselves have either closed their businesses (voluntarily or involuntarily) or merged with other institutions.

So now that the market is more fragmented, as a trader, how do you know which Broker to select?

Most important is recognizing what kind of trader you are. Though almost all firms focus on attracting "retail traders" – decidedly NOT a monolithic market – a select few make it their business to cater to AND never compete with their Introducing Brokers. Another major distinction among the highly differentiated "retail traders" is the type of instruments you trade. While Forex may seem ubiquitous, the range of currency pairs offered varies significantly. Many traders are interested in trading CFDs (contracts for difference) in Commodities like Gold and Indices like the S&P and Equity Shares and the cadre of firms offering these instruments is more selective. Options trading is becoming more popular for its unlimited upside potential and its limited downside loss, but still fewer firms offer these instruments. Of course, programmed trading is also a category of trading that not all firms offer.

Once you find a match in your trading needs at a basic level, the criteria you prioritize to select a firm becomes more personal. Among them is the trading environment – spreads, leverage, execution, etc. This is the criterion that assesses the opportunity you have to profit from your trades – all else equal.

Of course making money is important, but not if you are wasting your valuable trading time on unprofitable administrative issues. Therefore, another criterion for selecting a firm is support and back-office service. Is your broker responsive to your queries? Is the application process unduly onerous? Does the broker process your deposits and withdrawals expeditiously? Does the range of funding mechanisms meet your needs? These criteria are potentially the most impactful to a trader's satisfaction, but are difficult to assess without first-hand experience and often over-looked relative to other criteria.

The most important criterion for a long-term client of a broker is the security of your funds. This is the most difficult criterion to assess – even with trading experience with the firm. Many traders are mis-guided into believing that regulation is the surest way of protecting funds. But the largest regulatory body in the world, the US Commodities and Future Trading Commission (CFTC) gave regulatory approval to MF Global, Lehman Brothers and Refco – all of whom lost client funds with no recourse for clients. In fact, in all of Forex regulatory history, there have been far more client funds lost from regulated firms than from unregulated firms. This is not to undermine the value of regulation and the perception it brings. But perhaps the more important measure of funds security is a combination of broker longevity and evidence of segregated client funds. If the broker has been in existence for ten years or more, that broker must have a history of adapting to evolving market demands and is less likely to fizzle. The valid assumption being prosperous companies can function with operating capital and will not need to tamper with client funds. This is an easy statistic to research.

A broker that makes a point of segregating client funds from operating funds is also a better bet, but this is harder to verify. One way to beg the question is if withdrawals of the same currency come from an account number within the same institution that is different from the account number of a previous withdrawal. But again, you will have to question your point of contact and try to assess the quality of the response.

At the end of the day, when evaluating brokers, be wary of opinions appearing in forums claiming to be independent. NONE are completely independent because they must consider the benefit of their advertisers to some degree. And even the bloggers posting are often posting with a means to an end – that end not being to inform their competitive traders. The best way to assess a broker is to give it a try your-self. Once you identify a subset of brokers you believe will fit your needs, allot yourself a fixed amount of funds with which to trade to assess each.

In this environment of highly differentiated brokers, selecting the right one is not only complex, it is dynamic. Keep your eyes and mind open to your own evolving needs and the potential broker you believe will best meet them.

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