

Latest report from Forefactor discusses future of Smart Order Routing In response to Order Protection Rule Amendments

Examines SOR solutions that address market fragmentation and best execution requirements

Toronto, May 3, 2011— The future of Smart Order Routing (SOR) is currently being shaped by amendments to the Order Protection Rule (OPR) NI 23-101. In its latest report published today, Forefactor, the independent market research and strategic consulting firm, examines the expanding definition categories for orders that would be subject to the OPR requirement, and the split in Smart Order Routers (SORs), between marketplace and participant, to meet different end-user needs in this expanding market.

Forefactor's founder and CEO Renée Colyer comments: "Unfortunately, the OPR is about 5 years too late. Given that its main purpose is to provide brokers with the option to avoid the cost of connecting to multiple market places and subsequently necessitating the purchase or build of an SOR, The benefit of this rule is that even though it may be a few years off the mark, Forefactor believes it will aid smaller brokers in lowering their fixed technology costs, perhaps giving those brokers a fighting chance."

Colyer continues: "With regulatory changes making SORs increasingly relevant in the order execution process, the main question will not be whether to use an SOR, it will be which kind of SOR to use - a marketplace or a participant. A major consideration in the selection process involves the SOR's access to hidden liquidity. In the same manner that marketplaces have proprietary information about their dark/grey orders, participants who operate their own dark pools have a similar information advantage.

Value-added features such as the ability of an SOR that executes Canadian equities to route to US markets can create complications such as having to deal with the exchange rate. Different trading scenarios will naturally lead end-users to one SOR over another. The report details some of the differences as well as the potential advantages and disadvantages of each.

Colyer explains: “Marketplace SORs need to sweep all other markets of protected orders before executing the order on the home exchange. For participant SORs the main concern is more about routing infrastructure such as hardware, algorithms, communication lines, etc.”

Routing algorithms may differ depending on key factors aligned with each of their respective SOR providers. Through a compelling case scenario, the report demonstrates a situation in which the specific algorithm used by an SOR might create a locked market in which a buy order could remain unfilled despite being tradable.

As a result of today’s regulatory regime, SORs will be necessary for all order flow terminating at a lit Canadian market. While there are some exceptions to OPR obligations, the need for SORs in response to amendment to NI 23-101 is clear. Furthermore, choosing the right SOR can provide opportunities for the investment community to obtain an edge in best execution in their access to dark pools and foreign markets.

The report, “Smart Order Routing in Canada – A Cog in the Best Execution Wheel” is the latest in a growing library of syndicated research reports. Forefactor’s reports cover a variety of topics and are designed to provide clients with the intelligence needed to better understand their operating environments and the events that directly impact their business performance, competitive positioning and ongoing strategic development.

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About Forefactor

Forefactor is an independent, fact-based market research and consulting firm. Focused solely on global capital markets, Forefactor leverages its research and consulting expertise to provide critical insights that ensure clients are successful throughout the lifecycle of every strategic initiative. Forefactor combines experience in the design and execution of research with in-depth knowledge of the entire investment cycle to arm its clients with actionable recommendations and implementation roadmaps for reducing risk, anticipating change and maintaining a clear competitive advantage.

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