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ASIC mistaken on CFD disclosure: IG

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Local contracts-for-difference (CFD) heavyweight IGMarkets Australia Ltd says the corporate watchdog's concern with investors' understanding of the high-risk trading products is misplaced.

Chief executive Tamas Szabo welcomes steps by the Australian Securities and Investments Commission (ASIC) toward tighter industry regulation, but says ample disclosure of risks is already being made.

"All CFD providers highlight the risks of CFDs on both advertising when the account is open and on our website," he said.

"We ourselves vet all our clients that open accounts."

Mr Szabo was responding to concerns voiced by ASIC's acting chairperson Belinda Gibson last Wednesday that investors do not properly understand the risks of trading in CFDs.

"We do have a concern whether a lot of people in the CFD market really understand that this is a leveraged play in equities and (that) they really understand things like counterparty risk with CFD providers," she said.

ASIC's market surveillance operation will increase its focus on derivatives such as CFDs, and will issue a discussion paper on the derivatives market within two months.

A CFD is an agreement to exchange the difference in value of a particular asset between the time at which a contract is opened and the time at which it is closed.

The high-risk derivative instruments are typically used by sophisticated traders taking geared, short-term positions in volatile markets.

IGMarkets' vetting process means it currently rejects about 10 per cent of applications by prospective clients, Mr Szabo says.

"We make sure they have the right amount in savings and earnings that we believe is sufficient for someone to trade CFDs," he said.

But ASIC's wish to improve the transparency surrounding counterparty risk was well founded, he said.

Unlike many other players, IG Markets does not pass its clients funds' to brokers to cover its hedging positions.

Doing so can expose clients to the risk of losses if the CFD provider or broker falls into financial difficulty, Mr Szabo says.

CFDs can be used to trade equities, indices, foreign exchange and commodities.

CFD traders made up just four per cent of all direct share traders by June 2009, according to research firm Investment Trends.

Equity market volatility means the CFD market has been booming, giving IGMarkets a 43 per cent revenue boost to STG46 million (\$ A79.1 million), excluding the impact of currency movements, during the 12 months to May 31, director David Skilton said.

By June 2009, IGMarkets had a 25 per cent market share to rival CMC Markets' 22 per cent, but the latter was the most widely used provider with a 41 per cent share of unique clients and the highest trading volume.

City Index, MF Global, First Prudential Markets, Macquarie Prime and Commonwealth Securities also offer CFD trading products.

Executives from CMC Markets and City Index were not available for comment.

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