

What?

Recent History

Pre-1998 (1)

Pre-1998 (2)

Revolution in  
Trading

The current  
environment

Implications

# Market (Micro-)Structure for Asset Management

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### Recent History

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Pre-1998 (2)

### Revolution in Trading

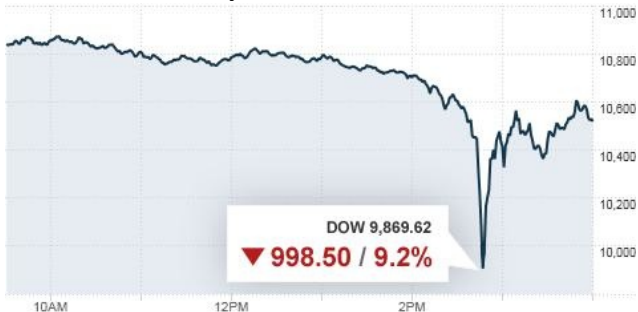
### The current environment

### Implications

- is the study of how transactions take place.
  - is closely related to the concept of liquidity.
- It has descriptive and prescriptive aspects.

In the news:

- ▶ *Flash Crash* of May 16, 2010



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- ▶ NYSE :: Specialist Market
  - ▶ Highly Centralized
  - ▶ Physical Place important
- ▶ NASDAQ :: Dealer Market
  - ▶ Most trades routed to a dealer
  - ▶ No physical place

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Dealers and specialists could make large profits from the bid-ask spread.

- ▶ Tick Size:  $1/8$  (anachronism).
  - ▶ Interesting side note: Bernard Madoff invented purchasing order flow
- ▶ NASDAQ Dealer Collusion (Odd-eighth avoidance).
- ▶ Traders could place limit orders, but questions of exposure.
- ▶ (And things were much worse in US options markets).

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Regulation:

- ▶ Decimalization (!)
- ▶ (Forced) Display of Limit Orders.
- ▶ Multiple Listing of Options

Technology :: High Frequency Trading (Really: High Frequency Quoting – fishing.)

- ▶ Program Trading (now 15%).

Fragmentation:

- ▶ Dark Pools.
- ▶ Electronic Trading Networks

Competition amongst Exchanges: Maker-Taker: rebate to liquidity providers / charge access fee to liquidity takers.

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Bid-ask spreads are much tighter.

Public quotes are much shallower.

Dealers no longer profit from the bid-ask spread. Emphasis is placed on the information in the order flow (*front running*).

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- ▶ Make trading costs *and execution* a point of distinction.
  - ▶ *Measure* both—and benchmark.
  - ▶ Don't give away order flow information.
  - ▶ Possible value in relationships.
- ▶ Recognize the effects of the new environment:
  - ▶ Heightened volatility :: **Reconsider** Limit / Stop Orders.
  - ▶ Black Pools *seem* an ideal venue—but are they subject to manipulation?