Treasuries: What lessons might carry over from other markets?

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<th><strong>S&amp;P index basket securities</strong></th>
<th>E-mini futures contract</th>
<th>SPY (Exchange Traded Fund)</th>
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<td>Iceberg orders</td>
<td>Many venues, mechanisms</td>
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Last sale reporting of on-the-run treasuries: why not?

- Dealers would be reluctant to accommodate customers knowing that the trades would be made public before they had a chance to work off their position.
- Partial exceptions
  - TRACE doesn’t publish sizes larger than $5 Million.
  - The London Stock Exchange has a publication delay to large trades.
  - “It wouldn’t really help investors get better prices.”

finra-markets.morningstar.com/BondCenter, Nov. 6, 2013
An open limit order book. Why not?

- US equity markets did not always have this.
  - SEC’s Order Handling Rules, 1996
  - Reg NMS Access Rule, 2008
- Brokers must disseminate customers’ bids and offers.
- Markets must allow non-member customers to execute against their advertised quotes.
- Futures markets did not always have this.
  - The CME’s Globex system was originally an “off-hours” market.

Small investor participation. Why not?

- The treasury encourages participation in the primary market (TreasuryDirect auctions)
- But trading costs are high in the secondary market.
  - A recent quote on the OTR 10-yr T-note from a retail broker’s web site was 99.671 bid, offered at 99.719
  - Bid-ask spread of 4.8 bps
- A typical spread on the SPY is $0.01/$200=0.5 bps.
Trading halts/pauses. Why not?

- On Friday, October 16, 2015, trading in about thirty NASDAQ NMS stocks was paused due to “limit-up, limit-down” halts.
  - They have become routine.

Opening and re-opening auctions

- Equity markets use a single-price double-auction conducted by the primary listing exchange.
- Isn’t this just like the primary market auction?
- NO. It must be tightly integrated with the secondary market.
Off-the-run bonds: what is to be done?

- Low activity stocks: the Euronext solutions
  - Designated market makers paid by the issuer
  - Periodic call auctions.
What’s left?

- Should the market be consolidated or fragmented?
  - How do we get the benefits of market-center competition and order competition?
- Should we allow dark markets?
  - Dark markets might be preferred by certain trading clienteles.
  - But they might weaken the lit markets.

What will stock markets look like in the future? (a slide from the 1990 deck)

- At the moment floor markets appear surprisingly robust.
  - The NYSE has the lion’s share of trading in their listed stocks.
  - NASDAQ is a dealer market.
  - The CME, CBT and NYMEX dominate futures trading.
- But many non-US exchanges use electronic trading.
- How might the US floor markets “go electronic”?
- The CBT’s Aurora system might just be lighting the way.
  - Next slide: an Aurora screen shot