CHAPTER 7: INTEGRATING CALL AND CONTINUOUS TRADING

Junius Peake, University of Northern Colorado
Paul Davis, TIAA-CREF
Gerald Putnam, Archipelago, Inc.
Cameron Smith, Island ECN
Daniel Weaver, Zicklin School of Business, Baruch College
Steven Wunsch, AZX, Inc.

JUNIUS PEAKE: I started on Wall Street in 1950 at $60 a week. My first job was changing the TransLux ticker ink. I got it all over my shirt and tie, and discovered it was absolutely indelible. Wall Street, 50 years ago, was very different than it is today. We used to say that if we got paid for the quotes, we would do the executions for free, because it took you 15 minutes to find out what a quote was. We also had customers who entered orders as good until close, and that was normal for them, and then they would cancel the order and move it further away from the market price.

Now to today. We have a very distinguished panel here. To introduce them, let me turn to one of my favorite books, the dictionary. We have an academician, Dan Weaver, and an academician is a member of an institution of learning. We have Gerald Putnam from Archipelago, and an Archipelago is an expanse of water with many scattered islands. Next we have Cameron Smith from Island. Is that one of the islands in the Archipelago? An island is a body of land, surrounded by water, and smaller than a continent. We have a stock exchange represented by Steven Wunsch, a stock exchange

This chapter is based on the transcript of the conference, The Electronic Call Auction: New Answers to Old Questions, held at Baruch College/CUNY on May 16, 2000.

Junius Peake was speaking facetiously. He was saying that when the price of a stock approached the execution price ("close" meant "near", not "at the end of the trading day"), the order would be cancelled. Peake was jokingly suggesting that when customers entered orders, they didn't really want them executed.
being a place where security trading is conducted on an organized system. And finally we have Paul Davis from TIAA-CREF.

In 1976, Morris Mendelson from the Wharton School, T. Williams and I wrote a paper. In it, we talked about the fact that people were very frightened about moving to electronic trading. It was like people back in the 14th century who would draw maps of the world with pictures of sea monsters and areas labeled “terra incognito.” We proposed an electronic trading system, and the proposal was turned down by everybody. The New York Stock Exchange claimed that nobody could afford an electronic trading system. It might cost as much as $20 million, they said, and where would that kind of money come from? Here we are, 25 years later. We still do not have an electronic system on the New York Stock Exchange, and they have spent $2 billion in the last few years.

What we have today is dual competition for orders. We have the order that the brokerage firm wants to get from the customer. When the customer gives the order to the broker, that order, in effect, is then sold to some market center. However, what the customer wants is that the order be able to interact with every potential counter-party order.

Island ECN, in some of its recent testimony, said that it absolutely believes in price-time priority. That has been one of my mantras, as well. Island does not believe in price-time priority of cross markets, however. Only within their own market can we have price-time priority. In other words, it is great in our market but no good in others.

Maybe the solution is for the SEC to do something I think they should have done 25 years ago. The Commission should issue a rule that says it wants the National Market System to operate under price-time priority. And on and after some specific date in the future, no security will trade (and be a National Market System security) unless it trades under price-time priority. We will build it. And we would build it. We would have a National Market System in a year and a half. I do not know whether Island, Archipelago, the New York Stock Exchange or Nasdaq would be the winner. But the big winners would be the customers.

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69 The NYSE reportedly spends $400 million annually on technology, up 25% since the late 1990s. See FORTUNE magazine, April 15, 2002.