CEPR-Imperial-Plato Inaugural Market Innovator (MI3) Conference

Evolving Market Structure in Europe and Beyond

29 June 2017

Overview

This document provides an overview of the key points covered during the research paper presentations and panel discussion the recent Plato Partnership Market Innovator (MI3) Conference, '*Evolving Market Structure in Europe and Beyond*'. Once approved, this document will be fully designed and distributed as a follow-up to attendees. This is in addition to following-up on our promise to post information and links to all the research papers to the Plato website.

Regulating Dark Trading: Order Flow Segmentation and Market Quality, Katya Malinova

Keypoints:

- The paper looked at whether the introduction of meaningful minimum price improvement regulation and the restriction of dark pool trading had a significant effect on dark pool trading levels in Canada.
- The paper found that the regulations made it less attractive to provide liquidity in the dark.
- The paper looked at the 7 weeks prior and 7 weeks after the regulation was introduced.
- 8% of trading happened in the dark before the rule changed. The three hypotheses that were looked at were that there would be a fall in the level of liquidity provided, a fall in dark trading volume and a reduction in the probability of trade execution.
- Trading halved overnight from 9% to 4%, but different dark pools were affected differently: one venue was almost unaffected, but the other saw a significant impact almost immediately.
- In the first venue, market flow came from all trader types.
- In the second, most of the market flow came from retail investors, where speed was less of a priority, and there was a high level of intermediation expected.
- The higher the level of intermediation, the more it predicted a larger level of decline and execution.
- Retail investors most likely did not realise they were affected, and most of the activity swapped to the lit venue.
- There was almost no aggregate market impact, but there were clear winners and losers.
- Retail trades saw less price improvement, and were more likely to face higher trading fees; HFTs earned higher fees by switching to the lit market, but smaller traders were unable to compete effectively in the lit market and so disappeared.
- The market re-segmented through an inverted make/take fee model
- The segmentation of retail order flow may reduce depth in lit markets.
- The impact of price improvements rules depends on the nature of liquidity provision in the market: intermediated markets lose, but un-intermediated markets are largely unaffected.
- Institutional investors on lit markets where retail flow migrated benefitted, which in turn benefitted all market participants.

Key questions:

"Was there a corresponding rise in intermediation after the switch to lit markets?"

Yes, there was a higher level of intermediation on lit markets, but the long term picture is still emerging.

"Was there an additional price impact from investors now knowing there were offering to retail investors?"

No, the price benefits were available to everyone in the lit market.