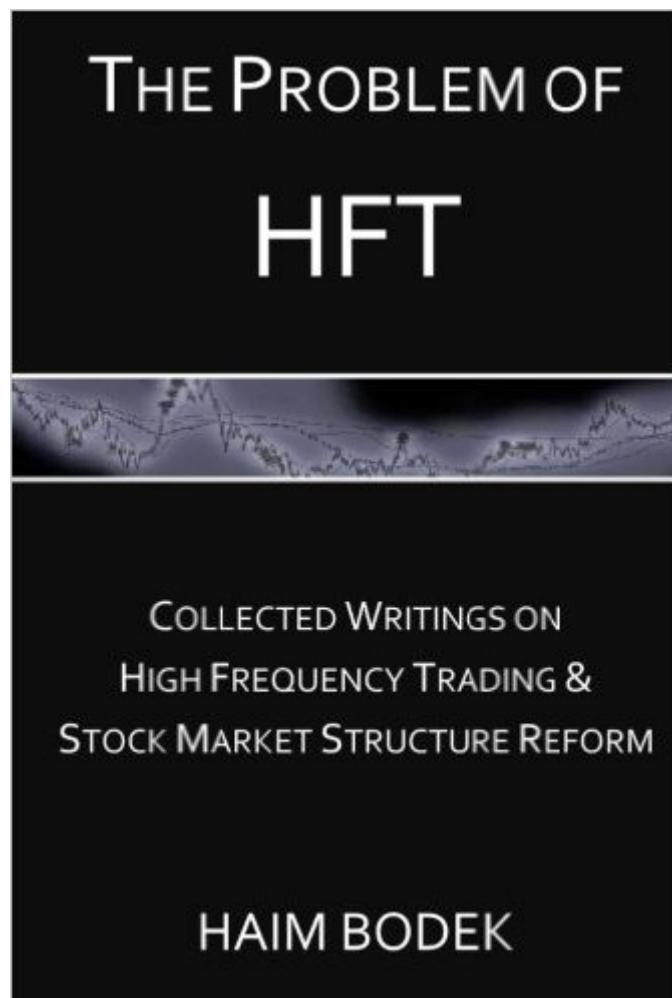


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# The Problem Of HFT - Collected Writings On High Frequency Trading & Stock Market Structure Reform



## **Synopsis**

This book explores the problem of high frequency trading (HFT) as well as the need for US stock market reform. This collection of previously published and unpublished materials includes the following articles and white papers: 1. The Problem of HFT - explains how HFTs came to dominate US equity markets by exploiting artificial advantages introduced by electronic exchanges that catered to HFT strategies2. HFT Scalping Strategies - describes the primary features of modern HFT strategies currently active in US equities as well as the benefits these strategies extract from the maker-taker market model and the regulatory framework of the national market system3. Why HFTs Have an Advantage - explains the critical importance of HFT-oriented special order types and exchange order matching engine practices in the operation of modern HFT strategies4. HFT - A Systemic Issue - a discussion of the latest industry and regulatory developments with regard to exchange order matching practices that serve to advantage HFTs over the public customer5. Electronic Liquidity Strategy - proposes a conceptual framework for institutional traders to achieve superior execution performance in HFT-oriented electronic market venues6. Reforming the National Market System - proposes a 10-step plan for strengthening the operation of the US equities marketplace in order to serve the needs of long-term investors7. NZZ Interview with Haim Bodek - addresses current topics and proposals for US equities market structure reforms8. TradeTech Interview with Haim Bodek - addresses the current status of the HFT special order type debate

## **Book Information**

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## **Customer Reviews**

Haim did a great job highlighting the more complex issues around the micro-structure of American financial markets. Avoiding the typical complaints that are heard, Haim dives into the deep

connections around exchanges, certain High Frequency Traders, and the order types created for those specific traders. What I found to be the most shocking was under the section The Alpha in an Order Type. Haim addresses the knock-on effects created by Reg-NMS in which certain order types were created to help HFT during specific market conditions so as not to hinder the traders strategies. The most shocking part is found at the number three slot in a list of innovations which served to preference HFT over the public. Traders who were entering orders and expecting to be "makers" wound up having their orders flipped into those that would be identified as "takers", resulting in a fee being paid. This is not a public order type and subjects non-HFT investors and non expert-network connected traders to manipulation through order types that are not part of the public record. This type of catering to HFT creates an issue around disclosure as some traders have no way of knowing about this type of back-door manipulation. These order types are not the generic Limit, Market, AON, etc. They were specifically created for specific market conditions for specific traders and the only way to know them is to have cocktails with an exchange head. Think of it like this: in chess there are specific move sequences all players understand and accept. Players can only use the standard pieces and move them only in accordance with the rule book. However, lets say that with one move away from checkmate, the other player introduces a new movement ability to win the game, you'd call him a cheat.

I've been following Haim Bodek's white papers and articles, which are cited in my own work on regulatory aspects of the securities market structure, and it was really exciting to see a book that brings his work together, while expanding it and providing several unifying themes. The overarching comment is that the book is a terrific reading, and Bodek's work helped connect many dots together in my own head. This book occupies a different niche compared to popular books / journalistic accounts, such as "Dark Pools" by Scott Patterson or "Crashshoot Investing" by Jim McTague, and a certain level of sophistication is assumed. Another good thing is that Bodek's book issues a grave warning but does not overdramatize / over-sensationalize. There is no overall doom-and-gloom scenario, and the author in fact documents several positive developments taking place in securities markets (I must add that some of them are attributed to his own advocacy efforts). Furthermore, as opposed to many recent empirical studies that focus on various correlations and questionable hypotheses, this book digs deep into the underlying trading processes from the perspective of a securities industry insider. The book evaluates the overall state of the securities market structure and offers several reform proposals. One piece of the puzzle is a largely redistributive effect of many rules adopted by trading venues as self-regulatory organizations. Although no rule has a truly

neutral effect on \*all\* market participants, Bodek goes into great detail to demonstrate that certain order types are created by trading venues in order to market them to high-frequency traders, who, in turn, are able to win the zero-sum trading game.

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