

LIQUIDITY MAKING

Central to NYSE Arca’s market structure, Lead Market Makers provide liquidity and trading efficiency to foster issuer growth

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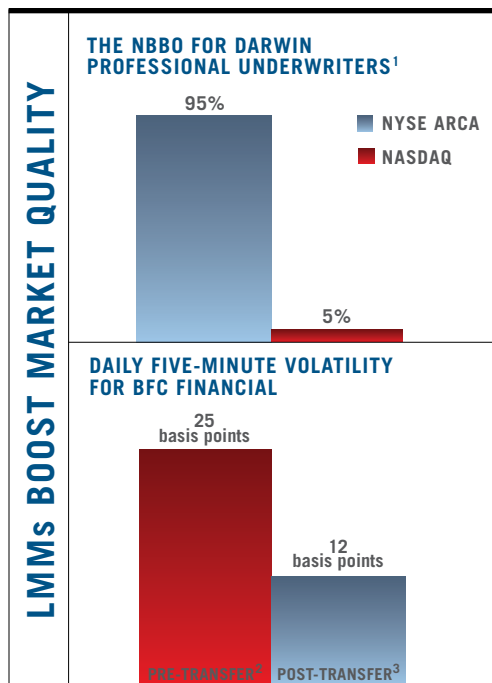
ONE OF THE FIRST SIGNS OF THE SYNERGIES between the NYSE auction market and the fully electronic NYSE ArcaSM platform is the newly created Lead Market Maker, or LMM, role. Exclusive to the NYSE Arca market model yet akin to specialists in the NYSE floor-based system, LMMs are selected by issuers and are responsible for maintaining depth, tight spreads and the opportunity for price improvement. They also serve as a single point of contact for each NYSE Arca issuer, providing accountability and crucial market insight into the trading of the listed security.

“By redefining the role of the market maker, NYSE Arca has created a marketplace that blends the speed benefits of a fully electronic platform with the price and liquidity benefits of the auction market,” says **NYSE GROUP INC.** (NYSE) CEO John Thain. “This provides superior trading quality and, ultimately, the liquidity to allow our issuers to grow. This platform also leverages the vision of the merger creating the NYSE Group by helping to support smaller, emerging businesses joining our family of listed companies.”

Issuers are not required to have an LMM, but doing so — which comes at no additional cost — can give their shareholders more opportunities for better pricing and more liquidity since an LMM is obligated to make narrow, two-sided markets every second of every trading day. A supplement to NYSE Arca’s natural liquidity, LMMs dampen volatility and lower all-in trading costs for investors.

So far, NYSE specialist firms have taken on the LMM role. This allows issuers planning to list on or transfer to the NYSE to develop a relationship and grow with a specialist firm.

In addition to maintaining continuous, two-sided quotes, LMMs must meet minimum performance requirements that include, for each stock, a percentage of the time that his or her quotes are the national best bid and offer (NBBO), an average dis-



DATA RANGES: ¹May 19 - June 19. ²May 30 - June 21. ³June 22 - July 21.

played size and an average quoted spread. NYSE Arca sets the appropriate performance requirements for each individual security (based on its price and other trading characteristics). LMMs fulfill these quote and execution obligations by electronically interacting with the market and algorithmically price improving incoming system orders. Only one LMM firm may make a market in a given security. The LMMs, and the

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issuers, regularly receive from NYSE Arca reports that monitor market quality and the LMM’s contribution.

CREATING COMPETITION

Having an LMM fosters price competition, explains Carmen Barone, a partner at **VAN DER MOOLEN HOLDING NV** (VDM) subsidiary VDM Specialists and senior managing director, listed-company relations. “We actually set the standard,” he says. “We raise the competitive bar because as the LMM, we are required to constantly publish a bid and offer. In other words, anyone who wants to bid has to bid with me or outbid me, and anyone who wants to sell has to offer with me or better my offer.”

To become an LMM, firms must meet certain selection criteria, including adequate capital, operational capacity and experience with making markets in equities. NYSE Arca is structuring its pricing to make sure trading in its listed companies is liquid by establishing business incentives for the LMM firms. Every time they add liquidity to the book, NYSE

Arca pays them a “liquidity” rebate. Only when a firm removes liquidity from the book is it charged a transaction fee.

CUSTOMER SERVICE

NYSE Arca’s first new listing since the NYSE Group was formed was the May IPO of **DARWIN PROFESSIONAL UNDERWRITERS INC.** (DR), a subsidiary of **ALLEGHANY CORP.** (Y). CFO Jack Sennott points to the tremendous visibility the company received on its listing day and to the service of both NYSE Arca and Susquehanna Specialists. “You get the service team of the full NYSE Group, and everyone I’ve met seems singularly focused on providing excellent customer service,” he says.

He adds that Susquehanna is attentive, communicating with Darwin three or four times a day, and that the firm has improved its performance each month since the listing. For example, the average quoted spread decreased to 7¢ in July from 8¢ in June, and the percentage of time Susquehanna provides the NBBO improved to 50.9 percent in July from 48.6 percent in June.

Meanwhile, investors are recognizing the market’s exceptional market quality, choosing to execute 74 percent of Darwin’s trading volume through NYSE Arca. NYSE Arca reports that it offers the best price in Darwin 95 percent of the time (see chart), that Darwin’s quoted size is more than twice as large as its Nasdaq industry peers and that Darwin is 21 percent more liquid than its Nasdaq industry peers. “We feel we’ve gotten the best of both worlds,” says Sennott. “It’s been a great transaction for us, and we were thrilled with the process.”

“You’re getting electronic trading with virtually instantaneous order executions,” agrees Leo Hinkley, senior vice president, investor relations

for **BFC FINANCIAL CORP.** (BFF), the first transfer to NYSE Arca from Nasdaq. “You also get the support of your LMM, which is a tangible benefit. The market can be a jungle, and having a friendly voice on the other end of the phone

paring the stock’s market data one month before and one month after the transfer shows that as the quoted spread decreased several percentage points, the quoted size increased 42 percent and volatility decreased by more than half (see chart).



who knows your name and company is a true advantage. It’s like having an extra set of eyes and ears on the market.”

BFC Financial chose as its LMM firm VDM, which already was the NYSE specialist for BFC’s primary holdings **BANKATLANTIC BANCORP INC.** (BBX) and homebuilder **LEVITT CORP.** (LEV). “We have a great track record with VDM and the NYSE, and our objective is to move BFC up to the NYSE,” says Hinkley.

Beyond increased visibility and superior service, Hinkley notes, NYSE Arca has provided significant market-quality improvements. Com-

Moreover, NYSE Arca says it offered the best price 63 percent of the time (compared to 3 percent of the time on other markets).

Hinkley says that the move has “turned out to be magnificent. The increased visibility and liquidity, the volume and depth of trading activity and the seamless transition to NYSE Arca is a testament to both the people at VDM and NYSE Group. Our phone volume rose appreciably,” he adds, “and a great number of investors, both institutional and retail, expressed their delight that we made the move.” □

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