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Charles Jones, Columbia Business School

Title: Potential pilot problems

Abstract: Institutional trading costs have fallen, and other measures of developed stock market liquidity have improved over the past 15 years or so. This is probably due to increased competition among liquidity providers and technological efficiencies. Still, the optimal regulatory stance is far from clear. Randomized controlled trials of regulatory changes provide the best opportunity to accurately assess regulatory treatment effects. Such pilot programs were recently used in the US to evaluate the effects of repealing the uptick rule limiting short sales, and another pilot has been proposed by the US Securities and Exchange Commission to evaluate possible changes to Regulation NMS, which governs competition among trading venues there. However, pilots must be carefully designed. If there are spillover effects, regulatory changes to treatment stocks can also affect control stocks, and standard empirical methods can lead researchers astray unless they are adjusted to take these spillovers into account.