

Quote Disclosure and Price Discovery in Multiple-Dealer Financial Markets

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Abstract

We examine the effects of price disclosure on market performance in a continuous experimental multiple-dealer market in which seven professional market makers trade a single security. The dealers trade with one another and with computerized informed and liquidity traders. Our key comparison is between fully public price queues (pretrade transparent market) and bilateral quoting (pretrade opaque). We find that opening spreads are wider and trading volume is lower in the opaque markets due to higher search costs there. More importantly, however, higher search costs also induce more aggressive pricing strategies, so that price discovery is much faster in the opaque markets.

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