

Competition among Trading Venues: Information and Trading on Electronic Communications Networks

Michael J. Barclay, Terrence Hendershott, D. Timothy McCormick

First published: 07 November 2003

<https://doi.org/10.1046/j.1540-6261.2003.00618.x>

Citations: 227

Abstract

This paper explores the competition between two trading venues, Electronic Communication Networks (ECNs) and Nasdaq market makers. ECNs offer the advantages of anonymity and speed of execution, which attract informed traders. Thus, trades are more likely to occur on ECNs when information asymmetry is greater and when trading volume and stock-return volatility are high. ECN trades have greater permanent price impacts and more private information is revealed through ECN trades than through market-maker trades. However, ECN trades have higher ex ante trading costs because market makers can preference or internalize the less informed trades and offer them better executions.

REFERENCES

Barclay, Michael, William Christie, Jeffrey Harris, Eugene Kandel, and Paul Schultz, 1999, The effects of market reform on the trading costs and depths of Nasdaq stocks, *Journal of Finance* 54, 1–34.

[Web of Science®](#) | [Google Scholar](#)

Barclay, Michael, and Terrence Hendershott, 2003, Price discovery and trading after hours, *Review of Financial Studies*, forthcoming.

[Google Scholar](#)

Barclay, Michael, and Jerold Warner, 1993, Stealth trading and volatility: Which trades move prices? *Journal of Financial Economics* 34, 281–305.

[Web of Science®](#) | [Google Scholar](#)

Bessembinder, Hendrik, and Herbert Kaufman, 1997, A cross-exchange comparison of execution costs and information flow for NYSE-listed stocks, *Journal of Financial Economics* 46, 293–319.

[Web of Science®](#) | [Google Scholar](#)

Biais, Bruno, Christophe Bisiere, and Chester Spatt, 2002, *Imperfect competition in financial markets: Island vs. Nasdaq*, Working paper, Carnegie Mellon University.

[Google Scholar](#)

Conrad, Jennifer, Kevin Johnson, and Sunil Wahal, 2002, Institutional trading and alternative trading systems, *Journal of Financial Economics*, forthcoming.

[Google Scholar](#)

Coppejans, Mark, Ian Domowitz, and Ananth Madhavan, 2001, *Liquidity in an automated auction*, Working paper, Penn State University.

[Google Scholar](#)

Domowitz, Ian, and Jianxin Wang, 1994, Auctions as algorithms, *Journal of Economic Dynamics and Control* **18**, 29–60.

[Web of Science®](#) | [Google Scholar](#)

Easley, David, Nicholas Kiefer, and Maureen O'Hara, 1996, Cream-skimming or profit-sharing? The curious role of purchased order flow, *Journal of Finance* **51**, 811–833.

[Web of Science®](#) | [Google Scholar](#)

Glosten, Lawrence, 1994, Is the electronic open limit order book inevitable?, *Journal of Finance* **49**, 1127–1161.

[Web of Science®](#) | [Google Scholar](#)

Grossman, Sanford, 1992, The information role of upstairs and downstairs markets, *Journal of Business* **65**, 509–529.

[Web of Science®](#) | [Google Scholar](#)

Hasbrouck, Joel, 1991a, The summary informativeness of stock trades: An econometric analysis, *Review of Financial Studies* **4**, 571–595.

[Web of Science®](#) | [Google Scholar](#)

Hasbrouck, Joel, 1991b, Measuring the information content of stock trades, *Journal of Finance* **46**, 179–207.

[Web of Science®](#) | [Google Scholar](#)

Hasbrouck, Joel, 1995, One security, many markets: Determining the contributions to price discovery, *Journal of Finance* **50**, 1175–1199.

[Web of Science®](#) | [Google Scholar](#)

Hasbrouck, Joel, and Gideon Saar, 2001, *Limit orders and volatility in a hybrid market: The Island ECN*, Working paper, New York University.

[Google Scholar](#)

Heckman, James, 1979, Sample selection bias as a specification error, *Econometrica* **47**, 153–162.

[Web of Science®](#) | [Google Scholar](#)

Hendershott, Terrence, and Haim Mendelson, 2000, Crossing networks and dealer markets: Competition and performance, *Journal of Finance* **55**, 2071–2115.

[Web of Science®](#) | [Google Scholar](#)

Hollifield, Burton, Robert Miller, and Patrik Sandås, 2001, *Empirical analysis of limit order markets*, Working paper, University of Pennsylvania.

[Google Scholar](#)

Huang, Roger, 2002, The quality of ECN and Nasdaq market-maker quotes, *Journal of Finance* **57**, 1285–1319.

[Web of Science®](#) | [Google Scholar](#)

Lee, Charles, and Mark Ready, 1991, Inferring trade direction from intraday data, *Journal of Finance* **46**, 733–747.

[Web of Science®](#) | [Google Scholar](#)

Macey, Jonathan, and Maureen O'Hara, 1997, The law and economics of best execution, *Journal of Financial Intermediation* **6**, 188–223.

[Web of Science®](#) | [Google Scholar](#)

Madhavan, Ananth, 1995, Consolidation, fragmentation, and the disclosure of trading information, *Review of Financial Studies* **8**, 579–603.

[Web of Science®](#) | [Google Scholar](#)

Mendelson, Haim, 1982, Market behavior in a clearing house, *Econometrica* **50**, 1505–1524.

[Web of Science®](#) | [Google Scholar](#)

Mendelson, Haim, 1987, Consolidation, fragmentation, and market performance, *Journal of Financial and Quantitative Analysis* **22**, 187–207.

[Web of Science®](#) | [Google Scholar](#)

Parlour, Christine, and Duane Seppi, 2003, Liquidity-based competition for order flow, *Review of Financial Studies* 16, 301–343.

[Web of Science®](#) | [Google Scholar](#)

Simaan, Yusif, Daniel Weaver, and David Whitcomb, 2003, Market-maker quotation behavior and pre-trade transparency, *Journal of Finance*, 58, 1247–1267.

[Web of Science®](#) | [Google Scholar](#)

U.S. Securities and Exchange Commission, 2000, Electronic communications networks and after-hours trading.

[Google Scholar](#)

Weston, James, 2001, *Competition on the Nasdaq and the growth of electronic communication networks*, Working paper, Rice University.

[Google Scholar](#)

Citing Literature



[Download PDF](#)

ABOUT WILEY ONLINE LIBRARY

[Privacy Policy](#)

[Terms of Use](#)

[About Cookies](#)

[Manage Cookies](#)

[Accessibility](#)

[Wiley Research DE&I Statement and Publishing Policies](#)

[Developing World Access](#)

HELP & SUPPORT

[Contact Us](#)

[Training and Support](#)

[DMCA & Reporting Piracy](#)

OPPORTUNITIES

Subscription Agents
Advertisers & Corporate Partners

CONNECT WITH WILEY

The Wiley Network
Wiley Press Room

Copyright © 1999-2024 John Wiley & Sons, Inc or related companies. All rights reserved, including rights for text and data mining and training of artificial intelligence technologies or similar technologies.

WILEY