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Equity Trading and the Allocation of Market Data Revenue

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Abstract


Revenues generated from the sales of consolidated data represent a substantial source of income for U.S. stock exchanges. Until 2007, consolidated data revenue was allocated in proportion to the number of reported trades. This allocation rule encouraged market participants to break up large trades and execute them in multiple pieces. Exchanges devised revenue-sharing and rebate programs that rewarded order-flow providers, and encouraged algorithmic traders to execute strategies involving large numbers of small trades. We provide evidence that data revenue allocation influenced the trading process, by examining trading activity surrounding various events that changed the marginal data revenue per trade.

Keywords: Equity market, Exchange revenue, Trade size

JEL Classification: G10, G14

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