# Clustering and Competition in Asset Markets[1]

Sanford J. Grossman, Merton H. Miller, Kenneth R. Cone, Daniel R. Fischel, and David J. Ross

University of PennsylvaniaUniversity of ChicagoLexecon, Inc.University of Chicago and Lexecon, Inc.Lexecon, Inc.



## Abstract

Economists, financial commentators, regulatory agencies, and the legal community have recently criticized the Nasdaq Stock Market, Inc., because there is greater clustering of stock quotations on even-eighths on Nasdaq than on the New York Stock Exchange or the American Stock Exchange, a phenomenon which critics attribute to collusion or some other defect in Nasdaq market structure. However, as this article demonstrates, clustering occurs in varying degrees in many other incontestably competitive financial markets, including the NYSE, the AMEX, the London Stock Exchange, the London gold market, and the international foreign exchange market. This article provides a competitive theory of clustering that emphasizes the effect of uncertainty, the size of transactions, volatility, and the informational and transactional roles of quotations on the degree of clustering. In addition, the article examines how market structure can affect the degree of clustering and considers the relation between clustering, spreads, and investors' transactions costs.