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The switch from continuous to call auction trading in response to a large intraday price movement

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Abstract

Some European exchanges (e.g. Euronext, Frankfurt and Madrid) make use of a mechanism to moderate price volatility that was proposed by Madhavan (1992) as preferable to a trading halt in times of market stress. It consists of a temporary switch from continuous to call auction trading in an individual security whenever its price moves beyond predetermined limits. This article studies whether this mechanism sharpens the information content of prices, dampens volatility and normalizes trading volume and intensity. Taking intraday data for the Madrid order driven continuous market, I find post switch improvements in the information content of prices and reductions in volatility, especially for thinly traded stocks. Trading volume and intensity peaked around auctions, but soon returned to preevent levels.

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Notes

¹ See Galper ([1999](#)).

² For reviews of the trading halt literature, see Kyle ([1988](#)), France et al. ([1994](#)), Harris ([1998](#)) and Kim and Yang ([2004](#)).

³ For a more detailed account of the SSE trading system and trading rules, visit <http://www.sbolsas.es>.

⁴ The official rules provide for resolution of possible ties between different prices.

⁵ The static and dynamic price collars are also used to control opening and closing auctions. When the final virtual resolution price of the auction lies outside one of the collars (the static collar in the case of opening auctions, and either the static or the dynamic collar in that of closing auctions), the auction is extended for 2 min. However, no such extension of volatility auctions is possible.

⁶ Parallel analyses were also carried out for subsamples defined by whether the auction-resolving price was higher or lower than the price in the last transaction before the auction. No asymmetry was found between these two subsamples as regards the behaviour of price discovery, price volatility, bid-ask spread or trading volume and intensity (results available on request).

⁷ Unfortunately, it has not been possible to gain access to data allowing analysis of the progress of learning during volatility auctions.

Related Research Data

[A closing call's impact on market quality at Euronext Paris](#)

Source: Journal of Financial Economics

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