NEW YORK STOCK EXCHANGE

STUDY OF FLOOR TRADING

February 1964

This report is confidential and intended solely for the information and benefit of the immediate recipient hereof.

CRESAP, McCORMICK and PAGET

Management Consultants

342 MADISON AVENUE, NEW YORK 17, N.Y.
MURRAY HILL 7-5450
CABLE ADDRESS: CONSULTANT-NEWYORK

NEW YORK-CHICAGO-SAN FRANCISCO-LOS AN
DÜSSELDORF-MUNICH

February 14, 1964

Mr. G. Keith Funston
President
New York Stock Exchange
Eleven Wall Street
New York, New York 10005

Dear Mr. Funston:

We are pleased to submit the accompanying report on our study of floor trading, made pursuant to your letter dated October 3, 1963. Essentially this report covers the findings and presents the conclusions derived from our study and, in addition, expresses our opinion regarding the section on floor traders of the Report Of Special Study Of Securities Markets Of The Securities Exchange Commission.

The recommendations submitted in the report recognize that the basic characteristics of the auction market for securities, conducted by the New York Stock Exchange, should be preserved by retaining and improving all activities which contribute to a fair and orderly market for buyers and sellers. They also recognize that effective functioning of an auction market in securities requires the presence of speculative risk-taking at various times and to varying extents, depending upon conditions, and, further, that it should originate primarily on the Floor of the Exchange where it can be intimately related to the needs of the moment by quick decisions and where the activity can be fully controlled in the interest of protecting the investing public.

In approaching this study, we were cognizant particularly of the complexities in conducting an auction market in securities and of the necessity of examining the qualitative aspects of performance on the Floor, as well as the quantitative results of trading. To this end, our study group spent an aggregate of approximately 50 hours on the Floor, observing its operations on "normal" days and under conditions of stress such as occurred on November 26, 1963.

We wish to take this opportunity to express appreciation to the members of the Exchange and to members of the executive organization who devoted much valuable time in assisting us to gain the necessary comprehension of the operations..

Yours very truly,

Cresap, McCormick and Paget

CRESAP, McCORMICK and PAGET

NEW YORK STOCK EXCHANGE

STUDY OF FLOOR TRADING

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I - INTRODUCTION

This chapter summarizes the background of this study, states the objectives and scope, describes briefly the approach used, and explains the arrangement of the report.

BACKGROUND

This study was undertaken at the request of the New York Stock Exchange for "an independent comprehensive study of floor trading as currently conducted on the Floor of the New York Stock Exchange. . . . " The activities of the floor trader - the Exchange member who buys and sells for his own account as he sees fit - have been subject to controversy for many years. For a small minority of floor members, it is their primary or sole activity. For a majority of floor members, it is an occasional or frequent adjunct to their principal activity as brokers or dealers.

The request for the present study stemmed from the findings and conclusions contained in the Report Of The Special Study Of Securities Markets prepared by the staff of the Securities and Exchange Commission and dated July 16, 1963 (Part 2), and referred to here as the "Special Study." Section 11 of the Securities Exchange Act of 1934 authorized the Securities and Exchange Commission (SEC) ". . . to regulate or prevent floor trading by members of national securities exchanges, directly or indirectly for their own account or for discretionary accounts. . . . " Accordingly, the SEC has from time to time made studies on floor trading activity, and the New York Stock Exchange (NYSE, or the Exchange) has made its own independent studies. As a result of these studies, the Exchange adopted rules governing floor trading, and the Exchange and the SEC established procedures for surveillance of trading. The evolution of the rules has been well described by the Special Study (pages 226 to 237). Through these rules, practices and other factors, trading activities on the Floor of the Exchange have been substantially improved over the conditions prevailing in the years preceding the 1934 Act.

Traditionally, the regulatory powers of the SEC have been exercised in restricting floor trading on the Exchange; there appears to have been no endeavor, by either the SEC or the Exchange, to sponsor rules which would provide a framework within which the floor trading function could be constructively used to improve the auction market. On the contrary, floor traders and floor trading have been a focal point of continuing criticism by the staff of the SEC - criticism which has reached the pronounced form of recommendations* that the Commission exercise the authority, granted by Section 11 of the 1934 Act, to abolish floor trading.

OBJECTIVES AND SCOPE OF THE STUDY

The objectives established by the Exchange in its letter of authorization of the present study were twofold:

"1. A statement of your firm's opinion regarding the Securities and Exchange Commission Study Report's criticism of floor trading (Ref: Chapter VI), including appropriate comments on the various statistical studies referred to by the SEC, and their concluding recommendations re complete abolition of floor trading; and

"2. If, after studying all the facts and pertinent opinions available, you conclude that floor trading should be continued unchanged as to rules and present practices you will so state. If, however, you believe it should be continued with some modification in the present rules, you will express your judgment as to what changes should be made."

The letter of authorization indicated that the study should be addressed to, "but not necessarily restricted to," the study objectives stated above.

These objectives were interpreted as constituting authority to reach whatever conclusions and to formulate whatever recommendations the study's findings appeared to warrant. The franchise of the assignment was regarded as permitting recommendations which might range from complete agreement with the Special Study, on the one hand, to complete agreement with the position of the NYSE, on the other.

*Report to the Commission by the Trading and Exchange Division dated January 15, 1945, p. 44; and page 241 of the Special Study, referred to above.

Furthermore, the complicated mechanism of the NYSE, and its unusually close interrelationship of functions, prevent the isolation and examination of one specific area. While cognizant of the scope of the assignment, the study team felt compelled to take a broad look at member trading, for any change of the NYSE mechanism inevitably affects more than the one area in which the change is made.

APPROACH TO THE STUDY

The survey team of Cresap, McCormick and Paget included personnel with previous experience in the securities business, who thus had a background for understanding the operations of the auction market which would not otherwise have been attainable within the time specified for completion of the study. Regarding the approach to the study, the letter of authorization specified:

> " To conduct this study, the New York Stock Exchange will make available to you all pertinent reports, studies, floor trading data used for surveillance purposes, and other appropriate material you may wish to examine. We will arrange for whatever visits you wish to conduct with floor traders, other Exchange members, Exchange officials, and staff members of the SEC if you wish. You may talk to any of them privately and confidentially, as you believe desirable."

Accordingly, the study was approached in the following principal steps.

Review of trading rules. The trading rules were studied and interpretative conferences held with officials of the Floor Department of the Exchange.

Study of floor operations. The survey team devoted approximately 50 hours to observing operations on the Floor and to discussing with members on the Floor the way in which all categories of participants in the market function.

Statistical analysis. Various statistical tests were applied to the floor trading activity in an effort to define the relationship of floor trading to price change.

Review of reports and floor trading data. Pertinent reports were obtained and reviewed, and surveillance data of the Exchange were examined and analyzed where appropriate. Explanations of surveillance procedures were obtained from officials of the Floor Department, and conferences were held with members of the Department of Research and Statistics regarding analyses of statistical data.

Conferences with NYSE members, allied members. Approximately 75 commission brokers, specialists and floor traders were interviewed to ascertain their policies, methods and practices in conducting their operations on the Floor and to obtain their opinions on the performance and responsibilities of floor trading.

Review of Special Study. The section on floor trading was reviewed and the facts, implications and conclusions were carefully considered. Also, other parts of the Special Study having a bearing upon floor trading were reviewed.

Questionnaire on member trading. To obtain full benefit of the experience of commission brokers, specialists, odd-lot brokers, floor traders and other members, a questionnaire dealing with floor trading was prepared and sent to all members. Approximately 900 questionnaires were completed and returned, and the results, together with the questionnaire form, appear in the Appendixes.

Interviews with other experts. Beyond the foregoing steps, over 40 interviews were conducted with individuals regarded as reliable sources of information on the execution of orders on the NYSE. These included traders and officers of investing institutions such as banks and investment companies, individuals now or formerly associated with the SEC and SEC Special Study, and officials of the Federal Reserve.

The mass of data thus assembled was carefully examined and interpreted, and opinions, conclusions and recommendations were formulated for presentation in this report.

ARRANGEMENT OF THIS REPORT

I - Introduction (this chapter)

II - Member Trading Practices And Problems - which explores policy variation by firms and extent of participation by members in this activity

III - Floor Trading Operations - which analyzes floor trading activities from both a statistical and qualitative point of view,

IV - Floor Trading And Price Trends - which examines statistically the relationship of floor trading with price stability and price trends

V - Opinion Regarding The Floor Trading Section Of The Report Of The Special Study Of Securities Markets - which reviews the Special Study of the Securities and Exchange Commission and expresses opinion on its findings regarding floor trading

VI - Conclusions And Recommendations

II - MEMBER TRADING PRACTICES AND PROBLEMS

Trading by NYSE members for their own or their firm's account has traditionally been separated into transactions initiated on the Floor of the Exchange and those initiated off the Floor. This has provided an important point of differentiation for trading activity, but has also engendered a number of problems in defining what constitutes a floor trade. Also, there appears to be some confusion at times over the category into which a member trade falls.

This chapter will examine the volume of member trading; trading policies and practices of members and member firms; conflicts of interest which may arise; the ethical problem of floor trading; and the internal and public relations problems arising from floor trading. Some general observations are then made regarding certain larger aspects of the problem.

VOLUME OF TRADING

In 1937, on-floor trading volume represented 6.8 per cent of twice-total round lot volume on the NYSE. It declined to slightly more than 3 per cent in 1946, and in 1962 was 2.3 per cent of twice-total volume. In recent years, it has generally remained within the range of 2 to 3 per cent. Off-floor trading, on the other hand, in 1962 accounted for just under 5 per cent of twice-total volume. Since 1937, it has ranged from 2.9 to 6.1 (in 1949) per cent. For the two categories combined, member trading currently accounts for between 7 and 8 per cent of twice-total volume on the NYSE.

FIRM PRACTICES AND POLICIES

Exhibit II-1, prepared from the results of the questionnaire sent to all members, depicts the answers of the respondents to the questions of how often they traded on the Floor and off the Floor, for their own or their firm's account. Completed questionnaires were received from approximately two-thirds of the membership (895).

NEW YORK STOCK EXCHANGE

QUESTIONNAIRE RESPONSES, ALL MEMBERS TRADING FOR OWN OR FIRM'S ACCOUNT

		OFF FLOOR						
		ALMOST DAILY	ABOUT ONCE OR TWICE A WEEK	ABOUT ONCE OR TWICE A MONTH	A FEW TIMES A YEAR	NEVER	NO ANSWER	TOTAL
ON FLOOR	ALMOST DAILY	12	17 (13)	7 (4)	41 (14)	24 (3)	1	102 (34)
	ABOUT ONCE OR TWICE A WEEK	-	8	11	32	14	-	65
	ABOUT ONCE OR TWICE A MONTH	1	6	11	20 (1)	16	1	55 (1)
	A FEW TIMES A YEAR	9	5	8	134	80 (1)	1	237 (1)
	NEVER	25	17	23	130	217	6	418
	NO ANSWER	1	-	1	4 (1)	1	11 (1)	18 (2)
TOTAL		48	53 (13)	61 (4)	361 (16)	352 (4)	20 (1)	895 (38)

NOTE: Figures in parentheses indicate responses from members whose principal activity is floor trading.

Exhibit II-1 shows that among floor traders, of whom 34 trade almost daily on the Floor, 13 also trade about once or twice a week off the Floor, and only 3 of the 34 never trade off the Floor. On the other hand, 12 members who said floor trading was not their principal activity stated that they trade almost daily, both on and off the Floor. Nine of the 12 are commission brokers from various-sized firms. In addition to the 34 floor traders trading almost daily on the Floor, 68 other members fall into this category, including 37 commission brokers, 10 $2 brokers, and nine specialists.

This exhibit, plus numerous interviews with Exchange members and information gathered from Form 82's (a form submitted daily to the NYSE to report all floor trades) is evidence that, while the so-called full-time floor trader may be responsible for a large percentage of the floor trading volume, a significant number of members whose principal activity is not floor trading are engaging in it quite frequently. Another important point is that more than 300 members responding to the questionnaires trade both on and off the Floor with varying frequency.

Member trading on-floor is subject to more restrictions than member trading off-floor. NYSE Rules 108, 109 and 110 place restrictions on transactions originating on the Floor, but do not apply to member orders originating off the Floor. An off-floor order, upon reaching the Floor, is accorded the same status as a public order. In addition, although the Exchange rules are quite explicit in defining the physical boundaries of the Floor and the difference between an on- and an off-floor order, there still remains a gray area which has led to considerable confusion on the part of some members regarding on-floor and off-floor trades. A questionnaire comment from a specialist sums up the problem and explains how he and many others interviewed resolve it: "I never use off-floor trading rules for my own or firm's account. It is my feeling that, if I or my partners are on the Floor, there is a gray area where the conflict with the rules can occur. Since both firm and personal trades are rare, I find it simpler to have the time and tick recorded on every transaction."

Floor traders, because of their presence on the Floor of the NYSE, are generally considered to have an advantage over members trading from off the Floor. Paradoxically, there exists an area in which the true floor trader is at a distinct disadvantage compared with other members. A number of member firms which conduct an active trading operation, for their firms' account, in stocks listed on the NYSE, will typically have one or more partners on the Floor or they may use the services of a $2 broker; at the same time, they may have one or more partners off the Floor following the ticker tape and other market information sources. While evidence indicates that these firms are very careful to observe the rules regarding what is on-floor and what is off-floor, they nevertheless have the advantage of a broader scope of trading operation.

CONFLICT OF INTEREST

An area of which the Exchange and its members are keenly aware is conflict of interest. Regarding the conflict which may arise when a member trades for his own or firm's account, on or off the Floor, and also handles public orders as part of his activities, the NYSE has rules of long standing to ensure that public orders receive preferential treatment. For instance, Rule 92 prohibits a member from trading for an account in which he has an interest if he has an unexecuted customer's market order.

A number of member firms dealing with the public, and keenly aware of the potential conflict, have imposed restrictions on their members over and above the NYSE rules. Some firms prohibit entirely their floor members from engaging in floor trading. Orders for their accounts must be entered outside of trading hours; some firms stipulate that members' orders must go through the order desk the same as any other order. Other firms prohibit members from carrying securities in a margin account. Another policy sometimes adopted requires members to pay full commission on all trades for their own account. It appears that the intent of all these restrictions is to ensure that public orders handled by these firms are executed in a manner which results in the fairest treatment possible for the customer, and that firm members are expending their time and effort in the customers' behalf.

As the questionnaire results and information from interviews show, a sizable number of floor members do trade for their own account and also handle customer orders. One of the main contributions which the floor trader can make is to be willing and able to step into a hectic market situation, and by his activity help dampen any excesses. It is during these periods of unusual market conditions, when the floor trader is most needed, that a broker engaged in handling customer orders will, by reason of executing them first, be least likely to conduct his floor trading activities in a constructive manner.

However, since there are numerous occasions when the transactions of commission brokers, acting on their own behalf, do contribute to price continuity, the problem consists of finding a means whereby these members, with the capital and the desire to engage in transactions for their own account, may be enlisted constructively to improve the operation of the auction market - but with such activity, at all times, governed by the well-established principles which determine conflict of interest.

THE ETHICAL PROBLEM

An intensive effort was made to determine how members conduct themselves on the Floor of the Exchange, especially when trading for their own account. The Wall Street adage, "A broker's word is his bond," is in general regarded not as a hackneyed slogan, but as a code under which Exchange members transact their business. Despite this high ethical code, there are some areas which need improvement and clarification. In the questionnaire, members normally on the Floor were asked if they had observed any instances of questionable floor trading practices. Of 679 members who responded to this question, 231 answered yes. Members were allowed a multiple selection when answering what specific practices they had observed. The two most common practices answered were congregating by floor traders and dominating markets. Nine floor traders observed instances of other floor traders congregating in certain stocks, as did 52 specialists, 91 commission brokers and 18 $2 brokers.

The term "congregating" may mean that a member was physically inconvenienced by a large number of traders and others at a particular post, or it may mean that the presence and activity of these persons tended to make transactions of other brokers more difficult to execute. While 179 members observed instances of congregating, 98 members observed instances of floor traders dominating the market. There were a lesser number of other questionable practices, but the questionnaire, observation and many interviews indicate that the main problem does not seem to be one of individual ethics. Rather, the problem is inadequate surveillance by Exchange governors and officials. Also, members complain that rules are not uniformly interpreted by those charged with this responsibility on the Exchange Floor. It is normal to expect some differences of opinion within any group of men or the interpretation of difficult regulations, but the problem seems to extend beyond the normal differences that might be expected and suggests the need for improved surveillance procedures.

INTERNAL AND PUBLIC RELATIONS

The NYSE is unquestionably the foremost institution of its type in the country. In terms of securities traded on the Exchange and the prestige surrounding it, it far surpasses all other markets in the United States. Not surprisingly, the Exchange expends much effort and money to educate those working for its member firms, and to inform the investing public of the merits of the auction market. Unfortunately, one area which has been almost totally neglected in these education and public relations efforts has been the role of the floor trader. Consequently, financial writers, investors, off-floor Exchange members and registered representatives of member firms tend to aim many of their criticisms of the Exchange at this category of member. Lengthy interviews with many of these people show they have little or no understanding of the contribution which a constructive group of floor traders can and often does make on the Exchange Floor. Thus a lack of understanding has contributed to a negative feeling toward this group and has focused on the unconstructive aspects of floor trading.

GENERAL OBSERVATIONS

It seems significant that, of an estimated average of 850 members active on the Floor each day, only 33 are classified as floor traders. Further, statistics presented in the Special Study* show that, since 1935, the number has varied between 22 and 34. Engaging in floor trading activities requires a combination of competence, capital and inclination. Since many others possess both competence and capital, the unanswered question becomes, Why do not a substantially larger number make floor trading a full-time occupation if it possesses the various advantages for profitable operation cited by the Special Study?

It also is significant that, while transactions of floor traders are scrutinized to ascertain the extent to which they exert a stabilizing effect, there is no corresponding analysis (as difficult as that may be) of some of the principal causes of price fluctuations generated by "public orders." It is entirely possible that large speculative accounts are factors; it is equally true that information and rumors circulate with amazing rapidity, and that many speculators in and out of brokerage house board-rooms are motivated as if they were acting in concert. The resulting "public orders" are entered and executed with little regulatory restraint, whereas floor traders - if they are the individuals on the other side of the transaction - must conduct themselves within the prescribed limitations of Rules 108, 109 and 110. It would seem possible that, even with the described advantage of "feel of the market" gained through presence on the Floor, the floor traders may frequently be committing their capital on much less positive information than possessed by speculators (nonmembers).

*Appendix VI-H Table 3

Among still other significant points which should be considered is the impact on the auction market (and the participants who may be trading for their or firm account) of orders for the account of securities dealers engaged in the "third market" - orders which are classified as "public orders" because they are from nonmember firms. Taking the broad point of view leads to an awareness that the practice of trading of members for their own or firm's account can be improved, as will be discussed in further detail in the next chapter; but it can also be argued that the special advantage may be more in theory than in actuality, and that an action promulgated" in the public interest and for the protection of investors," however well-intentioned, may be comparable to class legislation unless the origin of "public orders" is as well-defined as the statistics on floor trading.

These observations are made as a preface to the discussion of floor trading operations because they should be recognized and understood when such operations are examined on a statistical basis.

III - FLOOR TRADING OPERATIONS

The first section of this chapter points out the diversity of floor traders' activities and how these affect the functions they perform. The second section discusses floor trading and market liquidity.

A - DIVERSITY OF FLOOR TRADERS' OPERATIONS

Although all floor traders have access to the same facilities, the survey findings reveal that each trader has a trading pattern peculiar to himself.

CHARACTERISTICS OF TRADERS

One major category is characterized by how much time a member devotes to trading. For some, it is a full-time occupation, and all their efforts are directed to trading. At the other extreme are the members whose principal activity is not trading, but who execute an occasional transaction for their own accounts.

Floor traders can also be categorized according to the amount of capital they have. There appears to be a strong correlation between capital and the type of trading operation a member conducts. Members with large sums of money can take larger positions in individual stocks and be active in a broader number of securities than members with relatively less capital. And in acquiring or liquidating large positions, a trader is almost forced to buy on weakness and sell on strength in order to get in and out of a position profitably. Thus the larger the trader, the more likely he is to act in a stabilizing manner.

A third differentiating characteristic of floor traders is the manner in which they move about the floor and enter their orders. There are some who prefer to stand in a crowd, develop a feel of what's going on, acquire some stock and perhaps even continue to remain at the post and liquidate. Others will approach a post, buy or sell almost immediately (if the rules permit) or leave an order with the specialist and move on. Of course, there are many variations of these patterns and traders may change their own pattern frequently, but, in general, members tend to be of one type or the other.

A less precise distinction between traders, and one which correlates with, but is not limited to, the amount of trading capital available, is the member's inclination to buy on weakness and sell on strength. Basically, a trader must go with the over-all trend of a stock. However, within each major trend, frequent price reversals occur which may be of only momentary duration or of greater magnitude. Some traders utilize these reversals to acquire or sell stock and as a result perform a counter-speculative function. Opposed to this is the trader who typically buys stock in a rising market, reaching above the last sale and hopefully sells later at a higher price. The net effect of this speculative trading is not constructive to the market although it may be profitable to the trader.

An area which is similar to the previous characteristics, but is important to examine by itself, is the participation of floor traders in handling large blocks of stocks which come to the Floor. This is termed a distributive function. For example, the holder of a sizable block of stock wants to liquidate it as quickly as possible, but without forcing the price down too sharply. For several reasons, the specialist may not wish to buy the entire block himself and one or more floor traders will step in and buy a portion of it. The entire block will probably then sell at a discount from the previous sale. Depending on the size of his position and his intentions, the trader will gradually liquidate or distribute the stock much as the specialist would do so. This function, which the Special Study praised in its report under the heading of "Quasi-Specialist," is most constructive to the market and generally profitable to the trader.

While there are many additional characteristics which distinguish floor traders, the last one to be discussed here is the trader's investment objectives as a function of time. At one extreme is the short-term trader who is likely to be in and out of a position within a day and unlikely to carry any sizable position overnight. This may be dictated by his capital and frequent use of the daylight margin requirements, or may be his personal preference or both. Conversely, there are members of whom the term "trader" is a misnomer, for while they buy and sell for their own account, they are interested strictly in long-term capital gain. In between is a category of member traders who will take a position in a stock, typically remain long, but increase or decrease their position from that base as long as they are still confident of price strength in the stock. Their aim is to convert a portion of their position into a long-term capital gain, but they will take numerous short-term gains and losses in the meantime.

NEW YORK STOCK EXCHANGE

CHARACTERISTIC BEHAVIOR OF LARGER FLOOR TRADERS IN TERMS OF BROAD FUNCTION BEING PERFORMED

	Function			
	Speculative	Counter-Speculative	Distributive	Investment
Motivation	"Looks interesting"	"Public overdoing it"; help out at a difficult opening	"Clean up a block"	Six months plus
Anticipated Price Trend	Usually, short-term increase; sometimes, short-term decline	Short-term reversal, up or down	Short term stable to rise	Long term advance, perhaps with income
Collaboration With Specialist	None	Usually; sometimes not	Always	None
Inventory Position	Usually, short term long; sometimes, short term short	Usually, short term long; sometimes, long term long, or short term short	Short term long	Long term long
Accuracy Of Anticipation	One half of the time	Two thirds of the time	Three quarters of the time	No indication
Effect On Market	Usually tends to accentuate swings	Can dampen swings in most cases if anticipation is correct	Can prevent decline and lead to temporary rise	None
Market Behavior Without Floor Trading				
Volume	Slightly less	Somewhat less	Somewhat less	Not noticeable
Continuity	Slightly less	Somewhat less	Not noticeable	Not noticeable
Spread	Slightly greater	Noticeably greater	Questionable	Not noticeable
Swing	Slightly less	Somewhat more	Questionable	Not noticeable

Note: Short term (few hours to few weeks); long term (six months or more).

What this qualitative analysis suggests is the potential value to the market of the counter-speculative and distributive functions, as opposed to the speculative function. In their counter-speculative and distributive activities, the fewer and larger floor traders are typically employing more capital, and employing it more profitably. In speculative activities, all floor traders are typically employing less capital (per transaction) and employing it less profitably. It was this phenomenon of the market place which reminded one $2 broker to observe on his questionnaire: "Wall Street Proverb: All traders die broke."

B - FLOOR TRADING AND MARKET LIQUIDITY

DEFINITIONS OF LIQUIDITY

"Liquidity" is the single most important attribute of the auction market in securities, and, historically, stock markets have been measured according to the liquidity they provide. No investor would trade his cash for securities if the mechanism to liquidate, to convert his securities back to cash, did not exist.

The New York Stock Exchange is the foremost facility in the world for accomplishing this conversion, and its defense of floor trading's contribution to liquidity is probably the major reason why floor trading has been permitted to continue. So successful has the Exchange been in achieving liquidity for its listed securities, that this fundamental economic and financial term, in modern Wall Street usage, has taken on a wider meaning, including the concepts of "continuity" and "stability" as well. Thus, in addition to a standing mechanism for converting securities into cash, the Exchange undertakes to ensure that each conversion will take place at a price reasonably close to the preceding price for a given security (continuity), and that fluctuations in these prices will be held to a minimum (stability).

With only rare exceptions in recent years, the New York Stock Exchange has maintained its ability to provide the basic opportunity to liquidate - a cash bid at some price - for all sellers on all occasions. Its efforts to provide continuity and stability as well, regardless of the amount of stock offered and elapsed time required for the sale, have given "liquidity" a somewhat changed meaning. It now connotes what might better be called "fluidity," meaning sheer volume of trading during a given time period and characterized by bids and offers close to the last price. This fluidity, provided it is sufficiently balanced between those wishing to sell and those wishing to buy, is the most important ingredient in the modern auction market even though its meaning is broader than that of "liquidity," meaning "opportunity to liquidate." Much of the controversy over floor trading revolves around the liquidity-liquidation versus liquidity-fluidity concepts.

LIQUIDITY AS THE OPPORTUNITY TO LIQUIDATE

The Exchange's rules specifically provide that, in a situation where investors generally would wish to liquidate, floor traders too may liquidate without restriction. Accordingly, floor traders are under no formal requirement to contribute to liquidity within the stricter definition of that term (i.e., maintain the market's ability to accommodate liquidation), nor would it be possible to impose such a requirement. A floor trader, to protect his capital like any other investor, would react to such an obligation by seeking to evade it in times of unbearable stress, or by refraining from floor trading altogether.

The Special Study has criticized the role of floor trading in periods of market stress, maintaining that "it disappears when it is needed most." The interviews, statistical studies and the questionnaire returns for the present study agree that, as a rule, members on the Floor will be found on the sell side in periods of liquidation. They indicate also, however, that a handful of the large floor traders regularly step forward to buy in times of crisis.

Exhibit III-2 presents a summary of floor trading on November 22, 1963, the day of President Kenned assassination, and on the following trading day. The exhibit compares purchases and sales by the five floor trading accounts most active on November 22 with all other floor trading and with total volume. The time periods examined are:

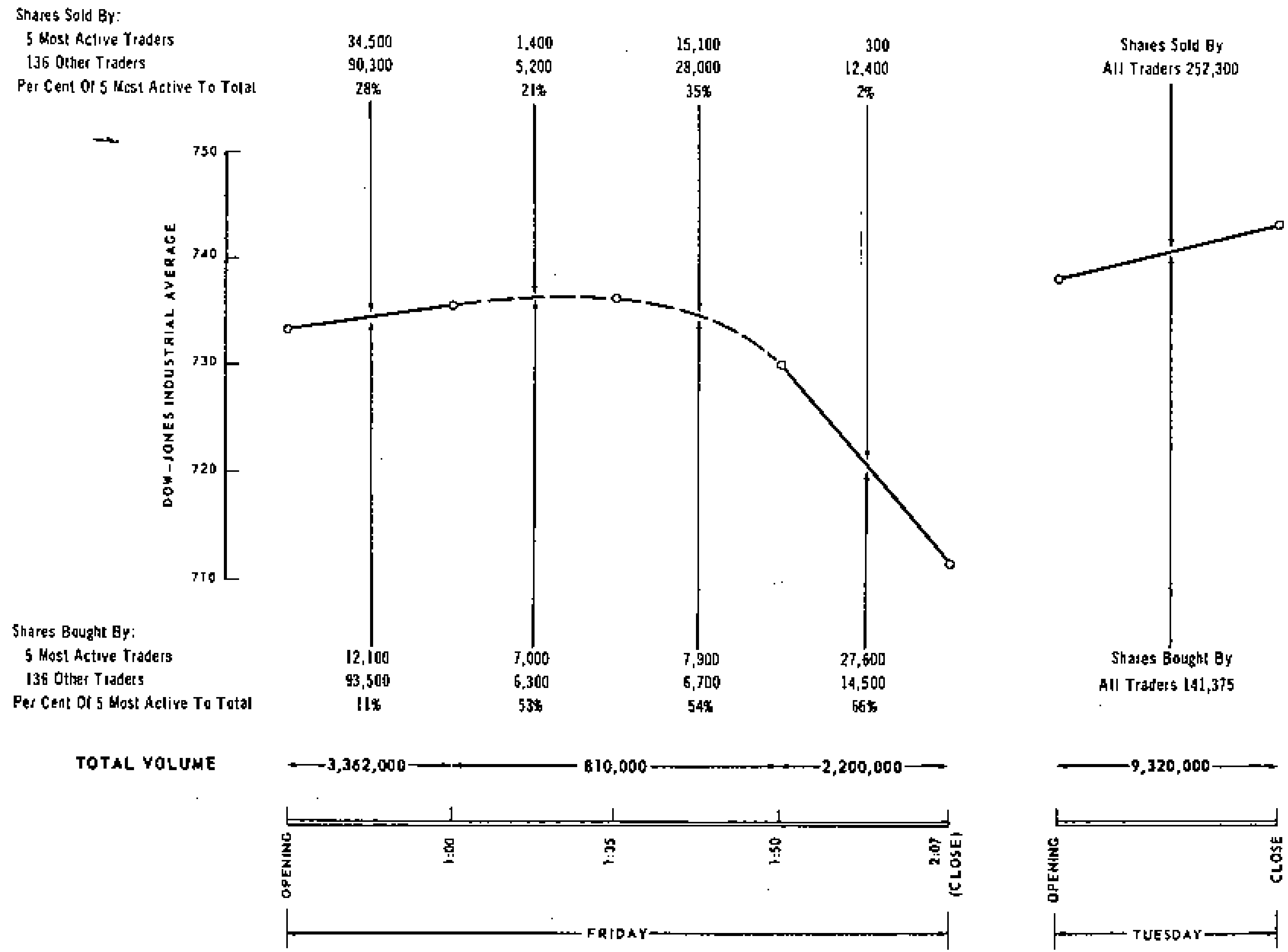
- The opening to 1:00
- 1:00 to 1:35, at which point reports of the 1:31 shooting first began to reach New York
- The 15 minutes from 1:35 to 1:50
- The final 17 minutes of trading, from 1:50 to the early closing of the Exchange at 2:07.

The exhibit clearly shows the difference in performance between the well-capitalized floor traders on the one hand and the smaller floor traders, when considered in the aggregate, on the other. The five largest traders were especially prompt to sell during the first vague reports of the shooting, and accounted for 35 per cent of all floor trading sales during the period from 1:35 to 1:50. Nevertheless, while buying

EXHIBIT III-2

FLOOR TRADING ON THE NEW YORK STOCK EXCHANGE

FRIDAY, NOVEMBER 22 AND TUESDAY, NOVEMBER 26, 1963



during this period about half as many shares as they sold, their purchases accounted for fully 54 per cent of all floor traders' buying. The difference is considerably more pronounced during the severe decline in prices of the final 17 minutes of trading. During this time, the five largest traders bought 27,600 shares, or two thirds of total floor trading purchases, while selling only 300 shares.

During the entire period from 1:35 to the close, the five largest accounts were net buyers, while all other traders, in the aggregate, sold.

Relatively large trading capital and unusual risk-taking ability appear common to all five of these traders, and the interviews with them revealed two major, related motives for their actions.

- First, panic liquidation is likely to be followed by a sharp price reversal.

- Second, competence at his occupation requires that a floor trader act on this conclusion.

The market opened stronger the following Tuesday and prices advanced during the day. Floor traders supplied stock into the rising trend, selling considerably more shares than they bought.

LIQUIDITY AS FLUIDITY

While only the larger traders appear to step forward to help in times of panic liquidation, it is these same traders who contribute most to a fluid continuity of markets and hence to liquidity in the more commonly used sense. An important illustration of this contribution is at the daily opening. The larger floor traders (as well as off-floor traders) are frequently called upon to help offset an imbalance of buy and sell orders in order to maintain closer continuity with the previous day's closing price. The Exchange staff has recorded many of these occasions, and a commission broker's statement is typical of many: "Generally the good, well-capitalized floor traders are very helpful in either taking a (long) position or (going) short to supply stock, particularly on delayed openings or reopenings." The floor traders involved, of course, hope to reduce their positions at a profit when the imbalance corrects itself.

On the floor of the Exchange, and in securities dealing generally, narrowness of the spread between bid and offer is a critical measure of a market. Of necessity, whenever a floor trader, or any member, buys on his own bid or sells on his own offer, he will have outbid or underoffered the competition and so acted to "close the market." Several questionnaire respondents pointed out the advantage of this condition, including a commission broker who replied: "If the specialist system is to be maintained as the basis of the auction market on the Exchange, the floor trader is the only real competition for the specialists in the maintenance of close bids and offers." And again, in the words of a specialist: "If all specialists were always able and willing to make good bids and offers, then traders might not be necessary, but (the specialists) are not. The traders help fill the gap."

Although their trading accounts for only some 2 to 3 per cent of twice-total volume, floor traders are uniquely able to provide such competition by reason of their ability to profit from fractional price changes. Thus a trader might seize an opportunity to outbid a specialist and succeed in buying, and then immediately offer the stock to new buyers at a price under that of the specialist's offer, though at an eighth or quarter profit to the trader. Market liquidity, in the sense of continuity and fluidity, is clearly served by such a transaction.

A trader's purchase on another member's offer, or a sale on another member's bid, does not in itself act to close the spread. It does, however, provide "the other side" to a transaction. Moreover, inasmuch as the other member's bid or offer, in order to have had the floor, must have represented a narrowing of the otherwise available spread, and assuming the quote straddled the last price, the trader completes a transaction that represents the closest continuity possible.

LIQUIDITY VERSUS STABILITY

The most popular defense of floor trading frequently advanced by NYSE members is that all buying and selling, in that it contributes to the momentary price, or "liquidity," has a beneficial impact on the market in general. This defense involves a contradiction. That the modern tendency to equate liquidity with continuity, or often sheer volume, can fundamentally contradict price stability has been pointed out by the Special Study and may be illustrated as follows: last sale 50, an all-time high for stock XYZ, and quoted now 49-3/4 to 50-1/2 as floor trader A enters the crowd. If A buys the stock offered at 50-1/2 he is applauded for providing liquidity - that is, for providing the other side of a public limited order to sell that might not otherwise have appeared. Ignored, however, is the fact that his purchase, executed on an up tick and at a new high, would usually be defined as a destabilizing influence. The frequent occurrence of this kind of situation and its influence on at least the momentary direction of price trend have been recognized by the Exchange and by the SEC, and have led to severe restrictions on floor traders' buying, despite the concomitant impairment of the fluid concept of "liquidity."

A second contradiction is found in the historic argument over concentration raised by the SEC. Floor trading is necessarily concentrated in relatively few stocks. It is, of course, precisely in such stocks that one may expect to find speculators of all kinds, attracted to them by the same motive. The Cresap, McCormick and Paget study revealed that 49 per cent of all floor trading during a two-week period was concentrated in 5 stocks - all of which were regularly on the "most active" list, characterized by sharp price reversals and as popular among speculators in brokerage house board rooms as among floor traders. It is in just such stocks, however, that imbalances of buying and selling most frequently occur, and where constructive trading (i.e., to offset imbalances) is most needed. These are the stocks, for example, that subject specialists to their most severe tests and often provide their greatest profits.

The argument that concentration is undesirable is a somewhat contradictory one. Both the SEC and a great many questionnaire respondents have accused floor traders of congregating and dominating the market for a stock. It seems inconsistent to require, then, that they trade in inactive stocks, where a solitary trader might necessarily dominate the market and stand guilty of price manipulation. Although it would be impossible to conceive of floor trading, or any other speculative trading, concentrated in other than speculative securities, floor trading may nevertheless be measured according to its influence, if any, on price trends in these stocks. If floor trading does, or can be made to, dampen price swings, it is precisely in the active, volatile stocks that floor trading is needed most.

IV - FLOOR TRADING AND PRICE TRENDS

Regarding the over-all relationship of floor trading to price trend, all observers and all statistical studies have agreed on one point only: floor traders' buying and selling activity is sometimes with the trend and sometimes against. The NYSE and SEC disagree on whether it is more often with or against, and on a method for measuring the trend itself.

A - METHODS OF MEASURING PRICE TREND

TICK TEST METHOD

As an indication of trend, the Exchange employs tick tests, wherein a transaction at a price higher than the last price is considered to have occurred on a plus tick (+), and a transaction at a price lower than the last price, on a minus tick (-). If a transaction occurs at the same price as that of the last transaction, but that price is higher than the last different price, a zero-plus tick (0+) has been posted. A zero-minus tick (0-) is the reverse. All sales on + and 0+ ticks and all purchases on - and 0- ticks are considered by the NYSE to be stabilizing transactions according to the "straight tick test."

All short sales are prohibited by NYSE rules from execution on 0 or 0- ticks, and floor traders are restricted under certain circumstances from buying on + and 0+ ticks. Nevertheless, various statistical samples have shown that, on the straight tick test, floor traders' stabilization rates fall mainly within the range of 40 per cent to 60 per cent.

In its sections on Specialists and Floor Traders, the Special Study has raised significant objections to the tick test. The Study points out, first, that this measurement shows only the relationship of a price to its next preceding price and gives little clue to any longer-term price trend. It also points out that all purchases on the bid and all sales on the offer are necessarily stabilizing, according to the straight tick test, whenever the quoted market straddles the last transaction price, as it frequently does.

and that the Exchange ordinarily does not use the straight tick test at all. Rather, a more liberal formula is employed wherein purchases on + and 0+ ticks, whenever executed at prices below the preceding day's close, are also regarded as stabilizing. The rationale for this liberalization is sound and understandable, for it seeks to regulate only those destabilizing purchases that might tend to force prices higher than those posted in the past. Nevertheless, the relation between tick and trend is a tenuous one, as will be shown in a later section.

CLOSE-TO-CLOSE METHOD

The SEC has customarily measured floor trading by its relation with changes in prices from one trading day to the next. This approach is illustrated in Exhibit IV-1, where reported floor trading is compared with daily price change in certain stocks. The stocks selected were those in which floor trading exceeded a predetermined minimum percentage of total volume, as measured by the Exchange's normal surveillance standards. The period from September 23 through October 4 was selected because it embraced 10 consecutive trading days that:

- Occurred after Labor Day but before the tax-selling season

- Included no holidays

- Saw the Dow-Jones Industrial Average first decline (from 746.06 to 732.79), and then advance (back to 744.68).

The exhibit shows that floor traders, in the aggregate, bought more shares than they sold of 74 stocks out of a total of 105 stocks that experienced one-day advances during the 10-day period. Floor traders were, on balance, sellers of 26 of the 105 advancing stocks, and, in five of these stocks, traders bought exactly as many shares as they sold. Of 86 stocks that experienced one-day declines, floor traders were net buyers of 41, net sellers of 41, and their purchases exactly offset their sales in 4. When total floor trading in all stocks is considered, the exhibit shows that floor traders bought or sold in the same direction as the Industrial Average on 5 of the 10 days selected.

EXHIBIT IV-1

NEW YORK STOCK EXCHANGE

FLOOR TRADERS' NET PURCHASES AND SALES COMPARED TO CLOSE-TO-CLOSE CHANGE IN PRICE

SEPTEMBER 23 - OCTOBER 4, 1963 (TEN BUSINESS DAYS)

		TRADERS WERE				TRADERS WERE				
DATE	STOCKS THAT ADVANCED	NET BUYERS OF:	NET SELLERS OF:	TRADING NETTED ZERO	STOCKS THAT DECLINED	NET BUYERS OF:	NET SELLERS OF:	TRADING NETTED ZERO	DOW-JONES INDUSTRIAL AVERAGE	ALL FLOOR TRADERS, ON BALANCE:
September 23	9	7	2		10	8	2		Declined	Bought
24	18	12	6		6	2	4		Advanced	Bought
25	0	-	-		21	6	12	3	Declined	Sold
26	5	3	1	1	14	8	6		Declined	Sold
27	15	11	4		3	2	1		Advanced	Bought
30	9	5	3	1	6	2	3	1	Declined	Bought
October 1	13	10	3		5	2	3		Advanced	Sold
2	7	5	1	1	9	5	4		Declined	Bought
3	20	15	4	1	4	1	3		Advanced	Bought
4	9	6	2	1	8	5	3		Advanced	Sold
TOTAL	105	74	26	5	86	41	41	4		
Per cent of stock-days with trend		70%					48%			
Per cent of days with trend										50%

Note: The stocks selected were those in which floor trading volume exceeded minimum NYSE surveillance standards.

The day-to-day definition of trend has been severely criticized by the Exchange, and for sound reasons. The Exchange argues that price change is fundamentally unrelated to arbitrary time periods. In consequence, the close-to-close method fails to measure floor trading during the often sharp price fluctuations that occur during the average trading day. To this should be added the observation that, in general, the trading tactics of any group of speculators are determined by amount of price change, not by time periods, and the close-to-close method therefore fails to measure the great bulk of trading operations.

PRICE TREND AND PRICE LEVEL

While serious objection can be raised to both the tick and the close-to-close measurement of trend, the classical concept of "informed speculation" - i.e., merely buying low and selling high - is also inadequate to an understanding of trading and trend. As Exhibit IV-2 indicates, the price level at which a purchase and sale occurs, although it alone determines profitability, bears no relationship to price trend. In the exhibit, various familiar speculative concepts are shown in oversimplified form. These might be expressed in brokerage office language as follows:

A-1 "XYZ shouldn't go much lower; let's buy it." Followed by, "We have a profit; let's take it before XYZ turns down."

B-1 "XYZ shouldn't go much lower; let's buy it." Followed by, "We have a loss, but the price is now a little better than it has been; let's sell before it goes down again."

A-3 "XYZ should go even higher; let's buy it." Followed by, "We have a profit and XYZ now seems to have turned down; let's sell."

B-3 "XYZ should go even higher; let's buy it." Followed by, "We were wrong and have a loss; let's sell before XYZ goes down even further."

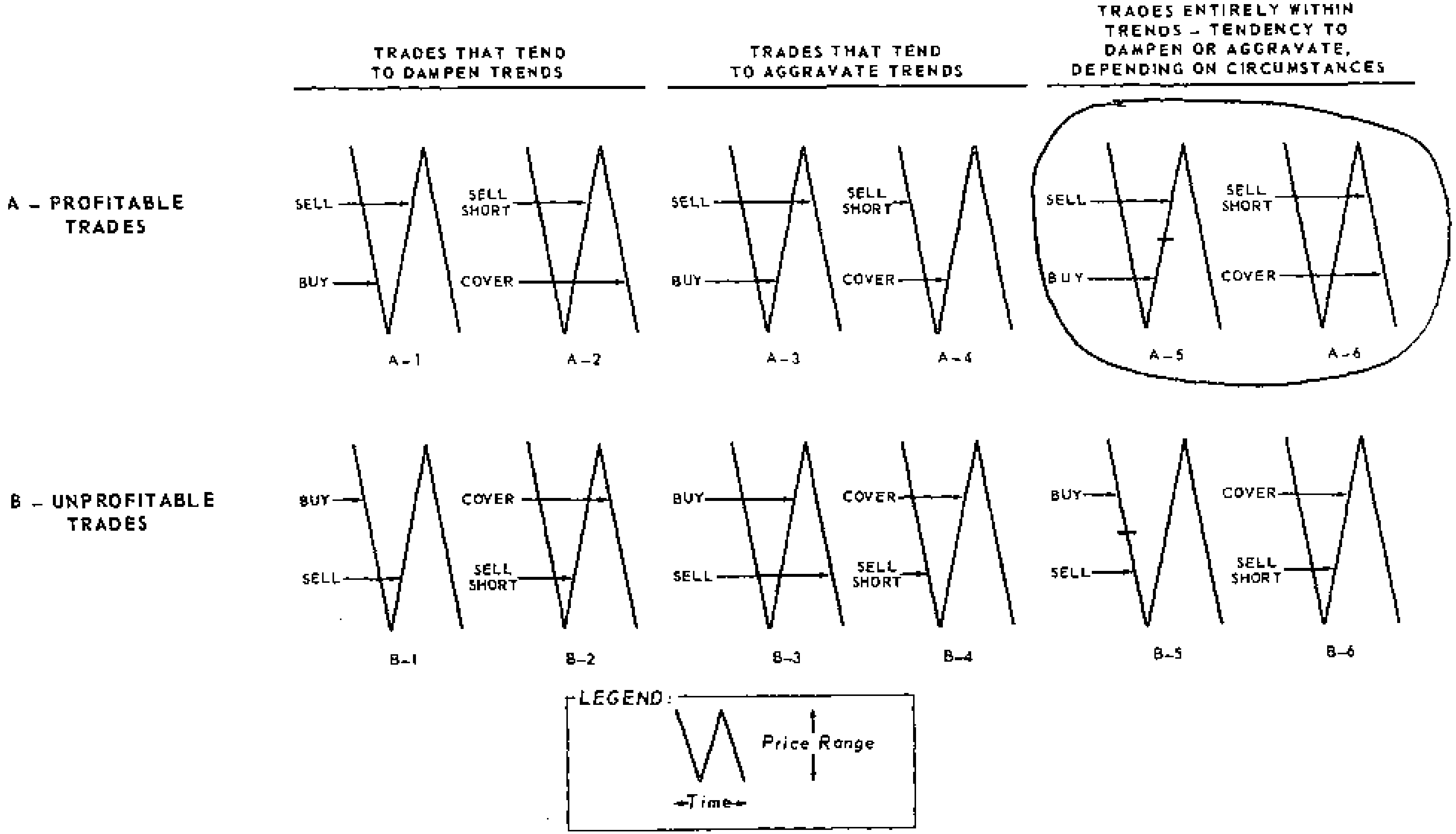
A-5 "XYZ should go even higher; let's buy it." Followed by, "We have a profit; let's take it before XYZ turns down."

B-5 "XYZ shouldn't go much lower; let's buy it." Followed by, "We were wrong and have a loss; let's sell before XYZ goes down even further."

EXHIBIT IV-2

NEW YORK STOCK EXCHANGE

ROUND-TRIP TRADES TENDING TO INFLUENCE TRENDS, BY PRICE LEVEL AND POINT IN TREND



The even-numbered illustrations show the analogous short operation.

Transaction A-3, while profitable, is seen to aggravate the trend and is the goal for which many speculators (both on and off the Floor) regularly strive under the concept, "Buy with the trend and let your profits run." B-1, on the other hand, illustrates a transaction where both the purchase and sale were made against the trend, even though the transaction was unprofitable. Nevertheless, speculative transactions that are both unprofitable and aggravating to the trend, as illustrated by B-3, are apparently often the lot of the nonprofessional. This is clear inasmuch as transactions A-2 and A-1, which offset B-3, are precisely those that the specialist is obliged most regularly to perform and, if performed skillfully, from which he derives a large portion of his trading profit. Similarly, many floor traders can and do profit from this kind of counter-balancing transaction.

A-5 illustrates a round-trip transaction completed entirely within a trend. While the purchase is made with the trend, just as in A-3, the subsequent sale offsets statistically whatever influence on the trend the purchase may have had. Nevertheless, a body of evidence exists that transaction A-5, and the similar short transaction illustrated in A-6, can exert a destabilizing influence on prices under certain circumstances. The statutes outlawing price manipulation were designed to prevent just such circumstances, and charges even today of congregating and dominating markets are raised against operations that might be illustrated as in A-5 and A-6.

Under other circumstances, however, transactions such as these are a necessary and legitimate obligation of the dealer function. It is through transactions of this kind that dealers often adjust their positions in order to be able to dampen anticipated further public excesses. In Exhibit III-2, for example, the larger floor traders were seen to sell at the beginning of the sharp decline on Friday afternoon and then, with reduced long positions or even short positions, return their capital to the market heavily on the buy side at a lower point in the decline. The fact that this constructive operation is potentially just as profitable as a skillful manipulative operation is the principal source of the continuing controversy regarding the floor dealer activity.

It is agreed that floor trading is sometimes with and sometimes against the trend. As illustrated here, it also often occurs entirely within a trend. Inasmuch as individual floor traders have survived in business, floor trading must necessarily be conducted along the lines of A-1 through A-6 more often than B-1 through B-6. Statistical analysis alone, however, cannot establish whether any one kind of trading (such as floor trading) can cause trend, influence trend, or merely coincide with trend. Within the limits of this reservation, it is possible to examine the relationship of floor trading to price trend in terms of direction of traders' balances.

B - PRICE REVERSAL TREND ANALYSIS

METHOD OF MEASURING TREND

The "price reversal" definition of trend used in Exhibits IV-3 through IV-7 avoids the faults of both the tick test and the close-to-close formula. Borrowed from Wall Street point-and-figure technical analysis, it defines trend as any price movement that exceeds a predetermined minimum, disregarding time. Thus, if a one-point minimum has been set, and an upward moving price reverses and turns down, a downtrend is not assumed to have been established unless the downward movement continues for at least one full point before the price starts up again. If, on the other hand, the downward movement continues for a full point or more, a downtrend is assumed to have been established, and it remains intact until the price reverses and turns upward for at least one full point.

FLOOR TRADING IN CHRYSLER

Chrysler common was by far the most actively floor-traded stock during the 10 trading days September 23 - October 4, when floor traders bought and sold a total of 644,100 shares, or 16.1 per cent of twice-total volume. Exhibit IV-3 presents a chart of its price action during this period. The one-point price reversal analysis cancels out all price fluctuations smaller than one full point. Shown also are the net balance of floor traders' total purchases and sales during each trend, regardless of the price level of transactions.

While a trader is, of course, unable to foretell the direction or duration of a price movement at the instant of the transaction, this exhibit and the others of the series nevertheless show how normal floor trading activity relates to price trends.

The total of all shares floor-traded during each trend was considerably higher than the net figure, inasmuch as:

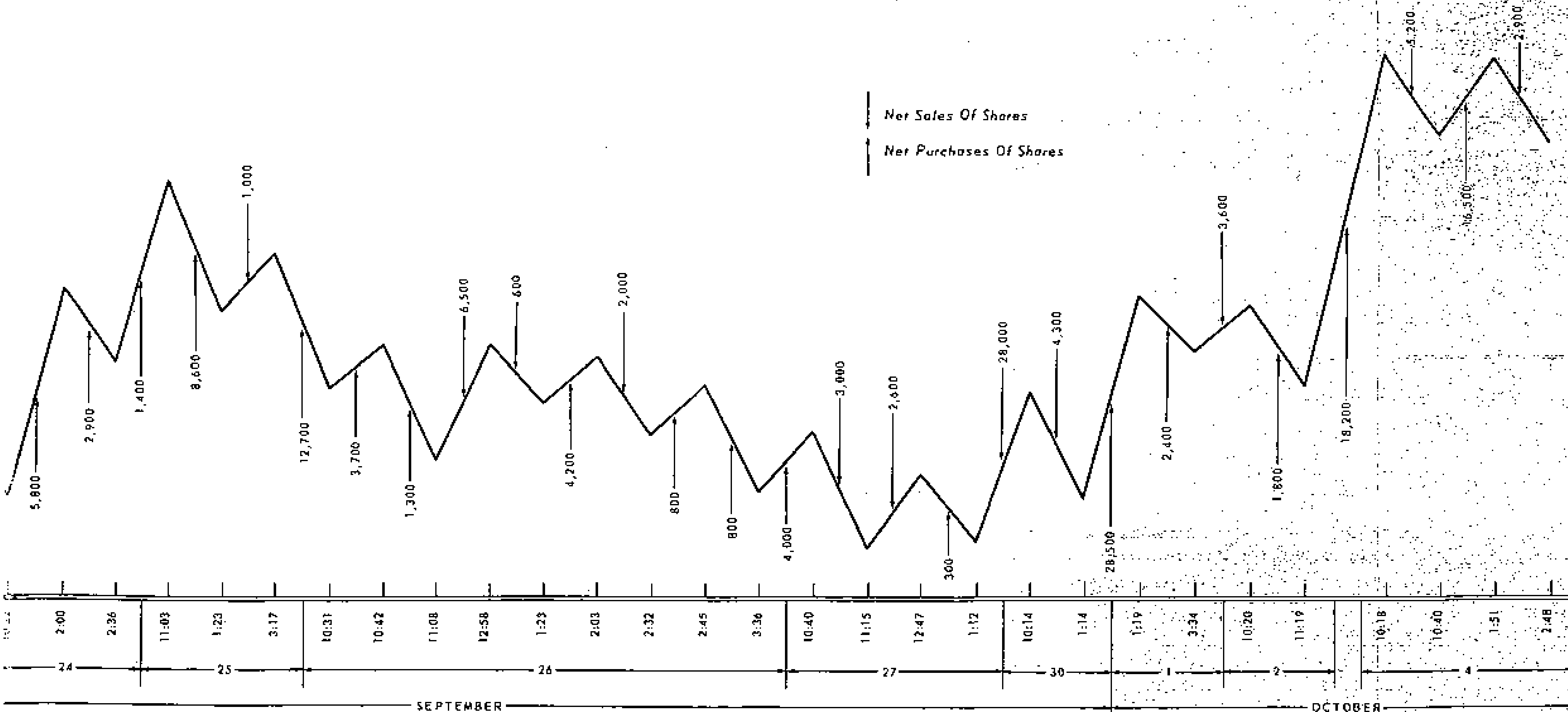
- Some traders bought and sold entirely within the trend on many occasions (as in the profitable trades A-5 and A-6, and the unprofitable trades B-5 and B-6, of Exhibit IV-2).

NEW YORK STOCK EXCHANGE

FLOOR TRADING IN CHRYSLER CORPORATION COMMON STOCK

SEPTEMBER 23 – OCTOBER 4, 1963 (TEN BUSINESS DAYS)

(Trends Based On One-Point Reversal, With Floor Traders' Net Purchases And Sales During Each Trend)



… because no significant price reversal occurred.

- Floor traders, like other traders, seldom agree and, typically, some traders were buying and others were selling during each trend.

While the price reversal analysis presents a clearer picture of the aggregate activity of floor traders during each price trend, it confirms the conclusions of other methods of analysis: floor trading is neither uniformly with the trend nor against. In Exhibit IV-3, floor traders, in the aggregate, traded with 18 price trends and against 13.

The selection of a one-point minimum reversal is based solely on observation of the in-and-out tactics of most floor traders and is accordingly arbitrary. Exhibit IV-4 shows price action in Chrysler for the same period with all price fluctuations of less than two points not shown. Here, where only larger price trends are shown, floor traders appear to act more often in a counter-balancing fashion and, in the aggregate, traded against four of these seven price trends. This exhibit, however, like the others of this series, includes a bias against the traders, in that where traders bought or sold at the exact point of reversal, their transactions were considered to have taken place during the <u>ensuing</u> trend. Thus, shares purchased at the precise end of a downtrend and beginning of an uptrend, even though they may have helped end the decline, are assumed to be <u>with</u> the trend.

Exhibit IV-4 also shows that, while the floor traders traded heavily against the over-all downtrend from 11:03 on September 25 to 11:15 on September 27, they traded even more heavily with the uptrend that began at 1:14 on the 30th of the month. Interestingly, traders operated chiefly as buyers during both trends, perhaps reflecting the general "bullishness" for Chrysler prevalent in Wall Street during this period.

<u>FLOOR TRADING
IN HIGH VOLTAGE</u>

High Voltage Engineering common was widely regarded as a speculative favorite during this same period and was the third most actively floor-traded stock; traders bought and sold 210,000 shares, or 15.7 per cent of twice-total volume. (In Sperry Rand common, which ranked second in floor trading activity, traders accounted for only 7.0 per cent of twice-total volume even though they bought and sold 287,100 shares.)

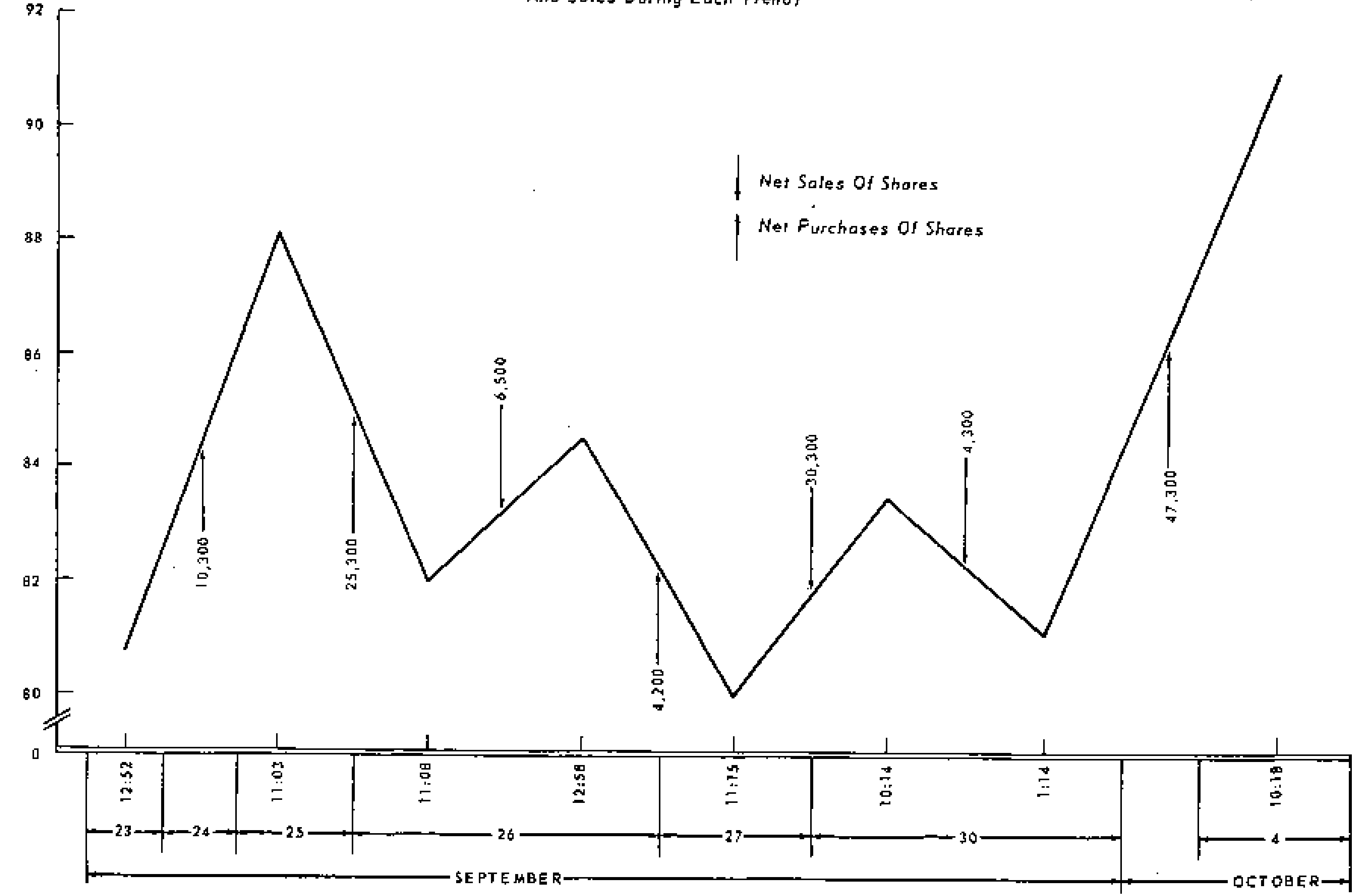
NEW YORK STOCK EXCHANGE

EXHIBIT IV-4

FLOOR TRADING IN CHRYSLER CORPORATION COMMON STOCK

SEPTEMBER 23 – OCTOBER 4, 1963 (TEN BUSINESS DAYS)

(Trends Based On Two-Point Reversal, With Floor Traders' Net Purchases And Sales During Each Trend)



Note: October 1 – 3 are not shown because no significant price reversal occurred.

In Exhibit IV-5, which shows price action for High Voltage during the sample period, all price reversals of one-half point or larger have been recorded because of the lower price of High Voltage in relation to Chrysler. Floor traders, considered in the aggregate, are seen to have traded with 45 trends and against 19.

Exhibit IV-6 shows floor trading in High Voltage with all fluctuations smaller than one point eliminated. Floor traders, on balance, acted in the same direction as the trend on 12 occasions and against the trend on 13 occasions.

AGGREGATE FLOOR TRADING

The analysis of floor trading in High Voltage and Chrysler is presented in somewhat different form in Exhibit IV-7. Here, the net buying or selling of each floor trader during each trend was determined, and the results totaled. In addition, the exhibit shows the total number of traders who:

- More often than not traded with the trend

- More often than not traded against the trend

- Traded generally as often with the trend as against.

Finally, a comparison of these totals with the grand total of shares floor-traded, or with the grand total of floor traders active in these stocks, reveals the number of shares traded, and the number of traders operating, entirely within the trend.

The tables indicate that slightly more shares were traded against price trends in Chrysler of at least one point, and, when only larger trends are considered, traders were more likely to be trading against than with. Of greater interest, however, is the finding that, even when all trends as small as one point are considered, more than two-thirds (438,000 out of 644,100) of all shares floor-traded were bought and sold entirely within trends. Shares traded within trends make up a progressively larger portion of the total as the minimum reversal standard is increased; and if a three-point standard (not shown graphically) is used, well over 90 per cent of all shares bought and sold by floor traders are shown to

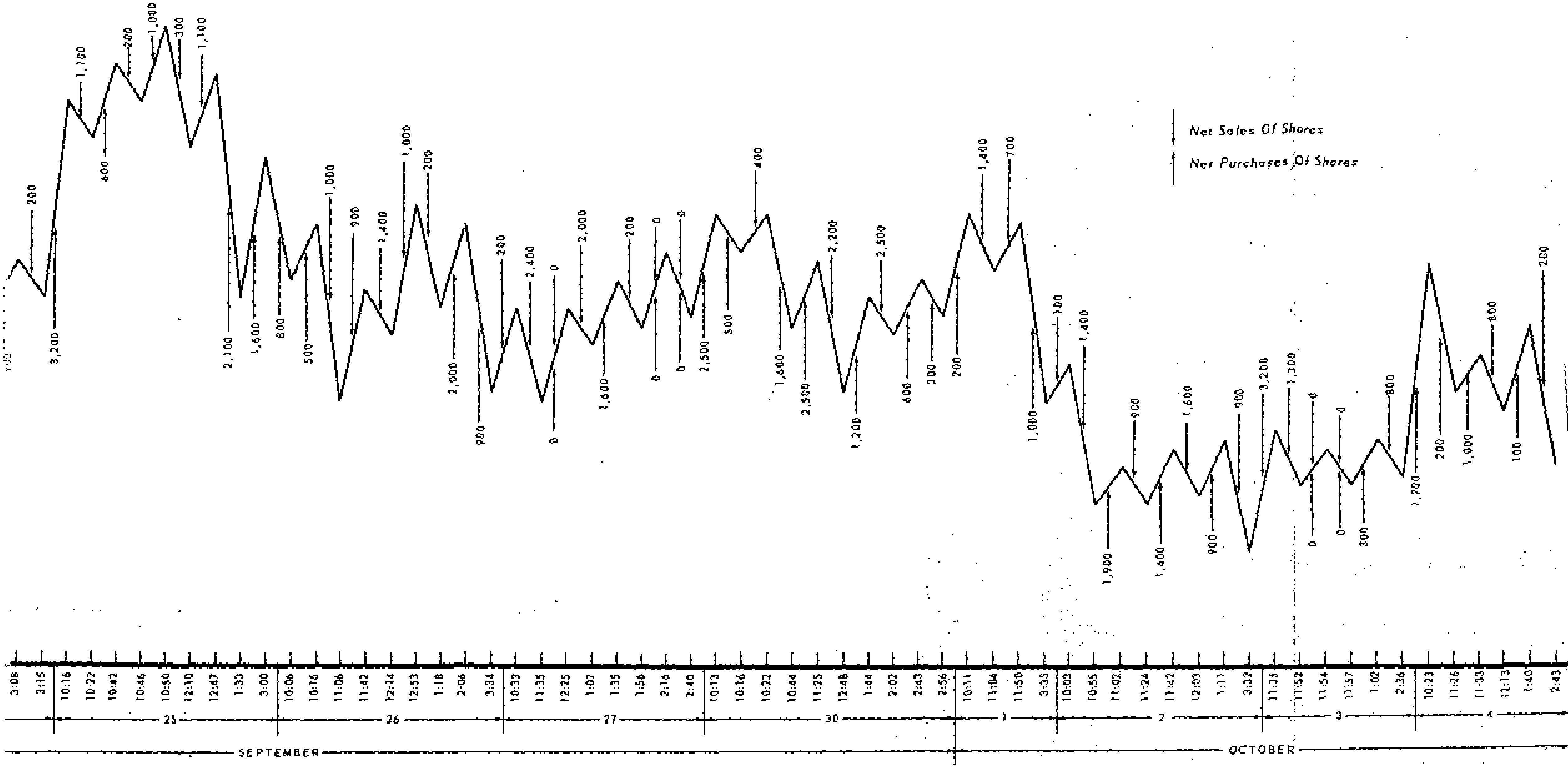
EXHIBIT IV-5

NEW YORK STOCK EXCHANGE

FLOOR TRADING IN HIGH VOLTAGE ENGINEERING CORPORATION COMMON STOCK

SEPTEMBER 23 – OCTOBER 4, 1963 (TEN BUSINESS DAYS)

(Trends Based On Half-Point Reversal, With Floor Traders' Net Purchases And Sales During Each Trend)



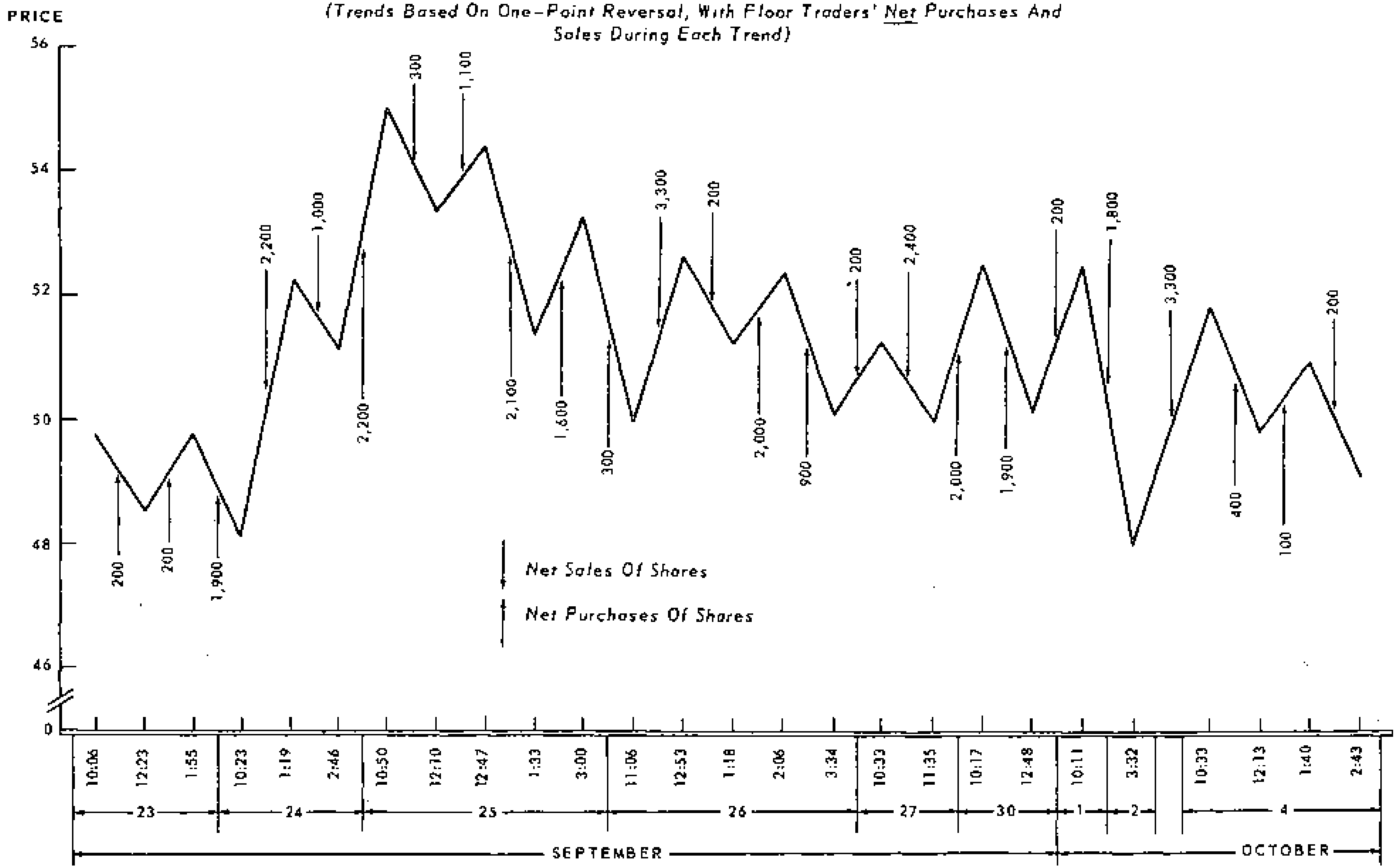
NEW YORK STOCK EXCHANGE

EXHIBIT IV-6

FLOOR TRADING IN HIGH VOLTAGE ENGINEERING COMMON STOCK

SEPTEMBER 23 – OCTOBER 4, 1963 (TEN BUSINESS DAYS)

(Trends Based On One-Point Reversal, With Floor Traders' Net Purchases And Sales During Each Trend)



Note: October 3 is not shown because no significant price reversal occurred.

EXHIBIT IV-7

NEW YORK STOCK EXCHANGE

CHANGES IN FLOOR TRADERS' BALANCES IN RELATION TO PRICE TRENDS

SEPTEMBER 23 - OCTOBER 4, 1963 (TEN BUSINESS DAYS)

	AGGREGATE CHANGE IN FLOOR TRADERS' BALANCES, IN SHARES				NUMBER OF TRADERS WHO HAD CHANGES IN BALANCES				
PRICE REVERSAL TREND	WITH TREND	AGAINST TREND	WITHIN TREND	TOTAL	USUALLY WITH TREND	USUALLY AGAINST TREND	AS OFTEN WITH AS AGAINST	WITHIN TREND	TOTAL
A - CHRYSLER CORPORATION COMMON STOCK									
One-Point	102,400	103,700	438,000	644,100	44	31	3	13	91
Two-Point	34,100	53,800	556,200	644,100	18	35	1	37	91
Three-Point	9,900	34,100	600,100	644,100	20	13	0	58	91
B - HIGH VOLTAGE ENGINEERING CORPORATION COMMON STOCK									
Half-Point	82,400	51,800	76,000	210,200	33	19	8	4	64
One-Point	35,700	35,400	139,100	210,200	20	18	3	23	64

have been offset entirely within the trend. Of the 91 floor traders active in Chrysler during the two-week period, more seem to have traded usually with the trend than against. The table shows, however, that 58 of 91 traded entirely within trends of three points or larger.

In High Voltage, floor traders are shown trading largely in the direction of the half-point reversal trends, but, despite the extreme narrowness of the price trends recorded, over one-third of shares floor-traded were purchased and sold entirely within trends. As in Chrysler, however, floor trading tends more in the direction of activity against the trend as the maximum reversal standard is increased.

In addition to showing that floor trading is neither always with the trend or always against, the tables amply demonstrate the narrow in-and-out tactics of most floor traders and support the contention that floor trading contributes to the "fluid" concept of liquidity.

TRADING WITHIN THE TRENDS

In view of the finding that a very large portion of floor trading takes place entirely within price trends, a one-point price reversal analysis of Chrysler is shown in Exhibit IV-8 wherein trading during each half of each trend is distinguished. The halfway point in each trend is determined as the mid-price between high and low, and, if the mid-price was recorded more than once, as the occasion closest to the mid-point in time that the mid-price was posted. (This method is similar to that used by the SEC in its report on NYSE floor trading dated July 1946 and presented on pages 520 and 521 of the Appendix to the Report of the Special Study - Part 2.)

The present exhibit provides a general idea of the over-all profitability of aggregate floor trading during each trend and indicates that floor trading can fall into each of the situations shown in Exhibit IV-2. On the basis of its similar 1946 studies, and referring to situations such as shown in A-6 if Exhibit IV-2, or between 2:46 and 3:36 (ticker tape time) on September 26 in Exhibit IV-8, the SEC concluded that ". . . floor traders initiate or contribute to the early stages of a decline by selling on balance, then in many cases tend to retard the decline to which they contributed." The Exchange contends that this kind of transaction is rather a legitimate dealer function of decreasing an inventory position in order to step in when possible and try to stem a decline brought on by others' selling. Neither position can be supported statistically; the actuality will depend on many circumstances, including the situation in the crowd and the general condition of the market.

EXHIBIT IV-B

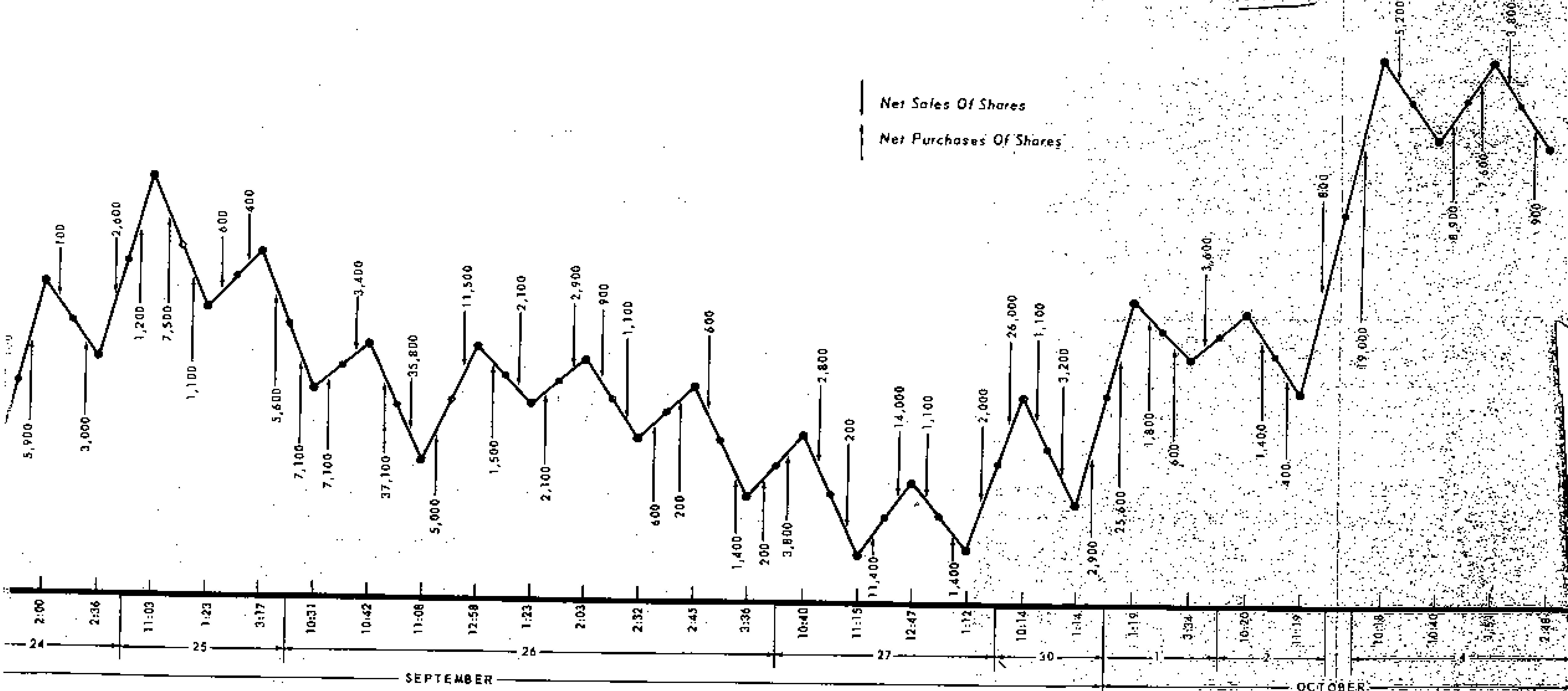
NEW YORK STOCK EXCHANGE

FLOOR TRADING IN CHRYSLER CORPORATION COMMON STOCK

SEPTEMBER 23 – OCTOBER 4, 1963 (TEN BUSINESS DAYS)

(Trends Based On One–Point Reversal, With Floor Traders' Net Purchases And Sales During First Half And During Second Half Of Each Trend)

40 with trend
18 Vs
2 EVEN



cause no significant price reversal occurred.

DETERMINED TO BE AN ADMINISTRATIVE MARKING
E.O. 12065, Section 6-102
By ... NARS, Date ...

RELATION OF TICK TO TREND

Exhibits IV-9 through IV-11 examine the relation of tick to trend for two standards of price reversal in Chrysler and one standard in High Voltage. The days or longer periods selected for analysis were those in which the greatest price volatility occurred - i.e., in which the greatest number of reversals were recorded. Table A in each of the three exhibits indicates that, of <u>all</u> shares floor-traded, whether bought or sold, transactions during uptrends are generally more likely to occur on + or 0+ ticks and transactions during downtrends on - or 0- ticks. It is interesting to note, however, that there appear to be frequent opportunities to buy on - and 0- ticks during uptrends, and to sell on + or 0+ ticks during downtrends.

Table B in the three exhibits presents these findings more concisely. Here, purchases during downtrends and sales during uptrends are considered "against the trend"; purchases on - and 0- ticks and sales on + and 0+ ticks are considered "stabilizing." All three exhibits show, in a general way, that transactions against the trend usually occur on stabilizing ticks. They also show, however, that transactions with the trend are just as likely to occur on stabilizing ticks as on destabilizing ticks. Table B of each exhibit also shows similar results in terms of individual traders. Those traders who operated primarily in a counter-balancing way against the trend almost always operated primarily on stabilizing ticks. Those who operated usually with the trend were as likely to execute their trades on stabilizing ticks as on destabilizing ticks.

CONCLUSION

The relationship of floor trading to price trend clearly reveals the dissimilarity between various kinds of floor traders and floor trading on different occasions and under varying circumstances. The charges raised by the SEC on frequent occasions accurately describe a portion, but far from all, of floor trading. The Exchange, on the other hand, has not formally recognized either that these negative conditions exist, or that some floor trading is performed as a legitimate dealer operation and makes a clear contribution to the market. Rather, the Exchange has merely complied with the SEC as expeditiously as possible in restricting all floor traders and all floor trading indiscriminately.

EXHIBIT IV-9

NEW YORK STOCK EXCHANGE

FLOOR TRADERS' PURCHASES AND SALES OF CHRYSLER CORPORATION COMMON STOCK IN RELATION TO TICK AND PRICE TREND

SEPTEMBER 26, 1963

A - DISTRIBUTION OF SHARES TRADED DURING ONE-POINT REVERSAL TRENDS

	SHARES BOUGHT			SHARES SOLD			ALL SHARES TRADED		
	ON UP TREND	ON DOWN TREND	TOTAL	ON UP TREND	ON DOWN TREND	TOTAL	ON UP TREND	ON DOWN TREND	TOTAL
On + or 0+ tick	18,500	2,800	21,300	24,300	8,200	32,500	42,800	11,000	53,800
On - or 0- tick	19,400	11,600	31,000	6,000	8,100	14,100	25,400	19,700	45,100
TOTAL	37,900	14,400	52,300	30,300	16,300	46,600	68,200	30,700	98,900

B - TICK TEST STABILIZATION VERSUS TENDENCY TO INFLUENCE TREND

DISTRIBUTION OF SHARES

	TRADED ON STABILIZING TICKS	TRADED ON DESTABILIZING TICKS
Traded Against Trend	35,900	8,800
Traded With Trend	27,600	26,600

NUMBER OF TRADERS

	FLOOR TRADERS WHOSE PURCHASES AND SALES WERE:		
	USUALLY ON STABILIZING TICKS	EVENLY DISTRIBUTED	USUALLY ON DESTABILIZING TICKS
Usually Against The Trend	14	1	2
Evenly Distributed	5	6	4
Usually With The Trend	10	1	10

EXHIBIT IV-10

NEW YORK STOCK EXCHANGE

FLOOR TRADERS' PURCHASES AND SALES OF CHRYSLER CORPORATION COMMON STOCK IN RELATION TO TICK AND PRICE TREND

SEPTEMBER 25 - 27, 1963

A - SHARES TRADED DURING TWO-POINT REVERSAL TRENDS

	SHARES BOUGHT			SHARES SOLD			ALL SHARES TRADED		
	ON UP TREND	ON DOWN TREND	TOTAL	ON UP TREND	ON DOWN TREND	TOTAL	ON UP TREND	ON DOWN TREND	TOTAL
On + or 0+ tick	29,200	9,300	38,500	48,900	9,900	58,800	78,100	19,200	97,300
On - or 0- tick	28,400	10,300	38,700	14,400	9,600	24,000	42,800	19,900	62,700
TOTAL	57,600	19,600	77,200	63,300	19,500	82,800	120,900	39,100	160,000

B - TICK TEST STABILIZATION VERSUS TENDENCY TO INFLUENCE TREND

DISTRIBUTION OF SHARES

	TRADED ON STABILIZING TICKS	TRADED ON DESTABILIZING TICKS
Traded Against Trend	59,200	23,700
Traded With Trend	38,300	38,800

NUMBER OF TRADERS

	FLOOR TRADERS WHOSE PURCHASES AND SALES WERE:		
	USUALLY ON STABILIZING TICKS	EVENLY DISTRIBUTED	USUALLY ON DESTABILIZING TICKS
Usually Against The Trend	20	1	4
Evenly Distributed	12	5	4
Usually With The Trend	8	1	7

EXHIBIT IV-11

NEW YORK STOCK EXCHANGE

FLOOR TRADERS' PURCHASES AND SALES OF HIGH VOLTAGE ENGINEERING CORPORATION COMMON STOCK IN RELATION TO TICK AND PRICE TREND

SEPTEMBER 25, 1963

A - DISTRIBUTION OF SHARES TRADED DURING HALF-POINT REVERSAL TRENDS

	SHARES BOUGHT			SHARES SOLD			ALL SHARES TRADED		
	ON UP TREND	ON DOWN TREND	TOTAL	ON UP TREND	ON DOWN TREND	TOTAL	ON UP TREND	ON DOWN TREND	TOTAL
On + or 0+ tick	8,800	2,500	11,300	12,500	7,700	20,200	21,300	10,200	31,500
On - or 0- tick	6,800	8,900	15,700	5,600	1,900	7,500	12,400	10,800	23,200
TOTAL	**15,600**	**11,400**	**27,000**	**18,100**	**9,600**	**27,700**	**33,700**	**21,000**	**54,700**

B - TICK TEST STABILIZATION VERSUS TENDENCY TO INFLUENCE TREND

DISTRIBUTION OF SHARES

	TRADED ON STABILIZING TICKS	TRADED ON DESTABILIZING TICKS
Traded Against Trend	21,400	8,100
Traded With Trend	14,500	10,700

NUMBER OF TRADERS

	FLOOR TRADERS WHOSE PURCHASES AND SALES WERE:		
	USUALLY ON STABILIZING TICKS	EVENLY DISTRIBUTED	USUALLY ON DESTABILIZING TICKS
Usually Against The Trend	10	0	0
Evenly Distributed	7	3	5
Usually With The Trend	7	0	4

V - OPINION REGARDING THE FLOOR TRADING SECTION OF THE REPORT OF THE SPECIAL STUDY OF SECURITIES MARKETS

This chapter will discuss the section of the Report Of The Special Study Of Securities Markets dealing with floor trading on the NYSE.

During the study and the preparation of this report, the Report Of The Special Study was used extensively, especially the sections on floor trading. The historical perspective it provided, the statistical compilations and the channelling of arguments for and against floor trading all were extremely helpful.

The findings and conclusions of this study agree in part with the Special Study and disagree in part; the most important difference is in approach. Rather than abolish floor trading, as recommended by the Special Study, a better solution is felt to lie in the preservation of the constructive aspects of floor trading. There exists a need, which is likely to increase, for mobile capital on the Floor of the Exchange, ready and willing to flow toward market imbalances - _if_ this capital is channelled in a responsible and properly controlled manner.

FLOOR TRADERS' ADVANTAGES

The Special Study finds that members trading for their own account on the Floor of the NYSE have a place advantage over all others not on the Floor. Arguments have been advanced to demonstrate these advantages, as well as counter arguments regarding the advantages of being off the Floor. The present study has concluded that there are certain advantages to a member's presence on the Floor of the NYSE, but that these advantages are not inherently bad. If properly controlled and constructively used, it is felt that they can be of value to the orderly functioning of the auction market.

Similarly, the cheaper cost of trading on the Floor, while irrefutably an advantage, does not contravene the interests of the investing public if the trader enjoying this cheaper cost can act in a manner which will benefit the investing public at large.

FLOOR TRADING RULES

The Special Study presents a detailed and lucid chronological summary of the evaluation of NYSE floor trading rules. These rules have undergone many changes and modifications in the past, and reflect the concern of the SEC about the propriety of floor trading and the response of the NYSE to the problem. An examination of the evaluation of these rules is convincing evidence that the SEC has carefully considered the implications of the complete abolition of floor trading. Armed with a clear mandate to set aside floor trading, the SEC heretofore has selected the alternative course of sponsoring numerous rules set up by the Exchange to control, rather than eliminate, floor trading activities.

This study concurs, in large part, with the opinion of the Special Study concerning the complexity of the current floor trading rules, especially the clarification of Rule 110 and the vagueness of Rule 110 itself. The present rules and those which they have replaced have all been aimed at restricting the activities of the floor traders. Some of the restrictions which have been imposed through the years include a limitation on the amount of stock floor traders can buy under certain conditions, a proviso that stock might not be sold at a profit for two days after its purchase, a daylight trading rule to curtail in-and-out trading, and a number of others.

Over the last 30 years, the SEC has sought to eliminate or severely curtail the activities of the floor trader, on the premise that these activities are bad in themselves. The NYSE, in a defensive posture, has sought to justify the floor trading group on the principle of free enterprise, and has given ground only as it became necessary. As long as these mutual attitudes prevail, no rules adopted by the Exchange, no matter how well-written they are or specific they may be, will be satisfactory.

The recommendations of this report and the proposed rules covering them recognize a distinction between types of floor trader activity, and attempt to utilize the constructive aspects and eliminate the undesirable. It is proposed to accomplish this not only with rules, but with performance requirements and measurable quantitative, as well as qualitative, standards.

similar to those made by a great many members regarding this same issue: "There are some traders who only follow volume and thus add more (volume) trying to scalp a 1/4 or so. Most (traders), however, are a great help to specialists and (to) the public under normal circumstances, and are invaluable under extraordinary circumstances and in special situations. I think a fairly large minimum capital (requirement) might help." The criticism that floor trading tends to contribute to market imbalances is discussed more thoroughly below.

The third criticism deals with liquidity in the sense of providing the opportunity for liquidation. This point is also well-taken, for selling by floor trading during times of market crises is in no way restricted under current NYSE rules. Those traders who buy on such occasions do so only at their own discretion and, as indicated in Chapter III, such buying is concentrated among the more expert, better-capitalized floor trading accounts. The fact that these traders do buy on such occasions, however, the Special Study has failed to recognize.

RELATIONSHIP OF FLOOR TRADING TO PRICE TREND

In its discussion of floor trading's relationship to price trend - i.e., its effect on price stability - the SEC successfully demonstrates the inadequacies of the tick test formula for measuring floor trading activity. While these criticisms appear valid, the tick test remains the only regulatory tool yet devised that can be applied in most market situations. As such, there has been no effort to discontinue its use. The Special Study goes on further to discuss the contradiction involved in the Exchange's argument that all floor trades, whether tending to destabilize or not, are beneficial inasmuch as they contribute to liquidity. This point was discussed in Chapter III of the present study.

The importance of the net balance studies conducted by the SEC and the Special Study, however, is significantly impaired by their fundamental confusion of price trend with time period. Thus, in comparing traders' balances at selected points in time, and then comparing changes in those balances with changes in prices, little indication is provided concerning actual trading during the period between the selected points in time. Studies of this type are presented on pages 214-17, 403-05, 411 and 412 of the Report Of The Special Study. Changes in floor traders' net balances are usually considered only in the aggregate, and are compared either with changes in the standard market indexes or with price changes in individual stocks.

vs Aux. Specialist

It should be stressed that the recommended function of "registered dealer" would be quite different from that of the "auxiliary specialist" as proposed by the Special Study of the SEC. The role suggested here would preserve the important features of individual initiative and judgment in the use of member capital, rather than permitting such capital to be employed only when and if required by one or more specialists. Under this alternative, capital its owners desire to employ in speculative risk-taking would soon disappear from the Exchange operations.

The functioning of the "registered dealers" in improving the continuity and stability of prices should present a partial answer to the question "... of just what is the role of the specialist in auction markets, and what is the adequacy of the protection that an investor has when he participates in that market."* At the same time, it is necessary to be utterly realistic and recognize that the "registered dealers" - and the specialists as well - will not be able and should not be expected to utilize their capital to support market prices when an avalanche of selling is created by professional speculators (nonmembers) who, being motivated by a crisis or the same set of conditions, decide to liquidate by unloading their holdings on someone else.

Essentially, "registered dealers" - i.e., members and member firms who qualify and register - would have trading privileges which in some respects would be broader than those now possessed by floor traders and in other respects would be more stringent, particularly in the area of qualitative and quantitative standards of performance. The underlying philosophy is that, instead of tightening the restrictions on trading to the point of inflexibility, the really constructive approach is to grant the necessary freedom to conduct trading operations within the scope of prescribed standards of performance designed to stress transactions of a stabilizing type.

These carefully considered recommendations also foresee the need for fully effective surveillance procedures which should be established and administered by the Exchange to ensure conformance with the standards.

*Chairman Staggers of the House Subcommittee at the hearing on February 7, 1964, as reported in The Wall Street Journal of February 8, 1964.

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The "registered dealers" would have to become accustomed to their role and the performance standards under which they would function. At the outset, these standards should be high enough only to ensure reasonable performance. In a trial period of at least a year, the Exchange, in the light of experience, should then raise the standards where advisable and within the limits of feasibility to gain maximum improvement in the functioning of the auction market.

The following recommended rules incorporate some regulatory features which have been embodied in other rules of the NYSE for many years. The purpose of doing so is to present the concept of the "registered dealer" function, together with the scope and limitations of the activity, without the need for cross reference to other rules.

RECOMMENDATIONS ON
TRADING OPERATIONS

Recommendation

1. A member activity known as the "registered dealer" (or some other appropriate term) should be established by the Exchange.

a. Such members and member organizations would be registered by the Exchange to deal in stocks generally, only after meeting the following qualifications:

- Detailed familiarity with performance requirements for "registered dealers" as ascertained through appropriate examination

- Expressed intent to engage in risk-taking with the objective of improving the continuity and stability of the market

- Established reputation for, or, in the case of new members, a commitment to engage in, trading practices which are consonant with fair and orderly markets

Explanation

The study disclosed that floor traders employ a wide variety of trading tactics. While some traders merely seek to exploit, and often aggravate, temporary market imbalances or price swings, others perform a dealer function very like that of the specialist, seeking to profit from counter-balancing transactions. Those traders who regularly or occasionally operate in this counter-balancing fashion, unlike the specialists, do so presently under no charter from the Exchange and participate in the market only as their own interests dictate. This floor dealer activity should be recognized, chartered and promoted by the Exchange and put to constructive market purposes.

The argument could be made that comparison with the direction of the market averages is somewhat unrealistic, inasmuch as floor trading ordinarily is heavily concentrated in only a few stocks, and accounts for an insignificant percentage of twice-total Exchange volume even on relatively inactive days. Nevertheless, while the net balance test, like the tick test, is far from conclusive, studies based on it have shown a general pattern of aggregate floor trading with the direction of daily price changes in individual stocks.

Despite the consistent finding, by every measurement, that a substantial portion of floor trading takes place in counter-balancing fashion against price trends, neither the SEC nor the officials of the Exchange have sought to devise methods for channelling all, or most, floor trading into useful activities of this kind. The following comments indicate that many Exchange members would welcome a program of this kind: "More floor trading would be better if it were the right type - stabilizing trader." Another commission broker commented in regard to the volume of floor trading: "Same amount as done by certain traders, but less by smaller traders who can create violent swings in price."

It can be noted here that the only initiative to steer more floor trading into stabilizing patterns has come from the floor traders themselves. Some of the larger traders have arranged meetings among floor traders to stress their responsibilities in the auction market.

The other important measurements of floor trading's relation to price trend presented by the SEC and the Special Study have been transaction-by-transaction studies in individual stocks. While most of these studies published in the Report Of The Special Study date from the years 1944-46, a rather thorough analysis was made of floor trading in Sperry Rand common on January 25, 1961, when the news of the passing of a dividend was announced at 2:32 in the afternoon. The analysis, which is presented on pages 363-65 of the Report Of The Special Study, shows one large floor trader engaged in heavy liquidation throughout the day and the relatively insignificant dealings of all other floor traders. However, this particular trader had already decided to liquidate his position before knowing the news, and merely continued to do so after the news was released.

SUGGESTED "AUXILIARY SPECIALIST" ROLE

The Report Of The Special Study found that floor traders often act as "quasi-specialists" in some of their activities on the Floor, and recommended a study of whether it would be feasible to create a category of "auxiliary specialists" with minimum capital requirements, who would be permitted to assist in the purchase or sale of large blocks of stock on the floor at the "unsolicited request of a specialist." As envisioned by the Special Study, the "auxiliary specialist" would occupy a passive role and act only when called upon.

The observations in this survey lead to the conclusion that this sporadic activity would be impractical.

The recommendation concerning the role of "auxiliary specialist" in effect recognizes the function of mobile, speculative risk-taking capital employed in trading operations on the Floor, and at the same time proposes limitations which would make it ineffective.

However, this concept might possess value if properly adapted to the needs of the auction market by creating a specifically designed function to provide a constructive force operating under established standards of performance and suitable means of surveillance. The needs of the auction market - i.e., liquidity, continuity and stability - have been discussed at length. They are well-known and regarded as old arguments to be accorded little weight unless recast in the light of new conditions.

Therefore, it is essential to consider two important developments which currently have a pronounced effect upon the market for listed stocks and in the future undoubtedly will create added pressures upon the Exchange as it endeavors to maintain orderly markets.

The first of these developments is the institutional investor. In 1949, institutional investors' holdings of NYSE listed companies were estimated at under \$10 billion, or less than 13 per cent of the market value of all NYSE listed stocks. By year-end 1963, they had expanded to more than \$82 billion or 20 per cent of the value of NYSE listed companies. This growth shows no signs of slowing.

The second development is the speculative interest present in the market place. Results of the NYSE annual public transaction study are reproduced in Exhibit V-1. The five tables in Exhibit V-1

NEW YORK STOCK EXCHANGE

TRENDS IN MARKET PARTICIPATION
For Selected Periods From 1952 Through 1963

Period	Table 1 - Percentage Distribution Of All Public Volume By Income Groups			Table 2 - Percentage Distribution Of All Public Volume By Investment Motivation		
	Under $10,000	$10,000-$25,000	$25,000 And Over	30 Days Or Less	1 To 6 Months	Over 6 Months
1952-54	34-35%	31-34%	31-34%	8-17%	19-28%	56-74%
1955-58	30-31	36-38	32-33	13-16	20-29	55-67
1959-63	16-26	40-44	35-40	9-17	25-32	51-65
1963	16	44	40	17	32	51

Period	Table 3 - Percentage Distribution Of Public Margin Volume By Income Groups			Table 4 - Percentage Distribution Of Public Margin Volume By Investment Motivation			Table 5 - Public Margin Volume As A Per Cent Of Total Public Volume
	Under $10,000	$10,000-$25,000	$25,000 And Over	30 Days Or Less	1 To 6 Months	Over 6 Months	(All Income Groups And All Investment Motivations)
1952-54	31-36%	31-37%	27-35%	15-24%	28-35%	41-57%	24-43%
1955-58	27-29	39-40	32-34	21-25	27-37	41-47	34-40
1959-63	13-23	43-47	34-41	17-26	33-42	35-46	32-59
1963	13	46	41	24	41	35	59

examine trends in market participation by income groups, the investment motivation displayed and the use of credit (margin) to effect transactions. As a means of comparison with 1963, the 12 NYSE public transaction studies from 1952 to 1963 have been grouped into three periods, and the ranges for each period are shown.

The five tables in Exhibit V-1 bring out the following facts.

- Table 1 indicates that the participation of the lower income group (usually the more conservative investors) has been halved; the higher income groups are clearly more of a factor in today's market than they used to be.

- Table 2 indicates that the investment motivation is shifting from the longer term (over six months) to the shorter term.

- Table 3 shows that the lower income group is more of a cash customer than the higher income groups, whose share of public margin volume has increased even more than their share of total public volume (margin and cash).

- Table 4 shows that short-term investment is proportionately more supported by margin than it used to be; the converse is true for longer-term investment.

- Table 5 indicates that the total public volume is increasingly supported by margin transactions.

In short, compared with 1952, today's typical individual stock market investor is likely to be wealthier, more interested in short-term developments, and more inclined to use credit to finance his transactions.

Some aggregate financial figures support the trends evident in NYSE's public transaction studies.

1. Customers' net debit balances (the amount of NYSE member firms' credit used to purchase or carry securities for customers) reached a 33-year high in November 1963 of over $5.6 billion.

2. NYSE member borrowings from commercial banks and trust companies (brokers' loans) of $5.1 billion in December 1963 rank below only the 1928 and 1929 peaks. It is one third above 1962's high.

3. The total short interest reported by NYSE firms in NYSE stocks reached a 33-year high of over 7 million shares in December 1963.

As the previously quoted figures show, both institutional holdings of NYSE listed securities and the speculative interest in listed companies are at high levels and likely to go higher. The NYSE must be prepared to meet the needs of these two groups of investors, each quite different from the other's, and herein lies the area where a professional NYSE member trader can assist in meeting this need. He can help meet it both by aiding in the cleanup of large blocks of stock typical of the institutional investor's transactions, and as a counter-speculative force to dampen price trends and imbalances which more typically are the product of the speculative interest.

RECOMMENDATIONS OF THE SPECIAL STUDY

The Special Study follows previous findings of the staff of the SEC that members dealing on the Floor for their own accounts enjoy advantages of time, place and commission over all others trading from off the Floor. Further, the Special Study asserts, floor traders bear "... no responsibilities or obligations in relation to the market as a public institution." Also, statistics were presented to demonstrate that floor trading has produced adverse effects on market prices. The Special Study makes the point that these findings do not appear to conflict with the Exchange's own views, inasmuch as its attitude has been defensive and its rules concerning floor trading have been made with the sole purpose of restricting activities that are of private benefit only.

The conclusions of the CMP study differ from these, mainly concerning floor trading's effect on the public interest and on the market. The CMP findings, based on interviews, questionnaire returns and statistical studies, are that some, though not all, floor traders and floor trading exert a beneficial effect on the market.

As a result of its findings, the Special Study recommends that floor trading in general be phased out of existence. A positive recommendation is added, however, that the possibility of an "auxiliary specialist" function be studied, wherein certain large floor traders, after meeting capital and other requirements, would be available to participate in block transactions "at the unsolicited request of a specialist."

With these recommendations, the CMP study differs strongly. The findings of the CMP study indicate that the Special Study's recommendations would:

- Indiscriminately abolish, along with the negative elements of floor trading, the floor trading functions that have been determined to provide a constructive influence in the market.

- Drive from the Floor the large amounts of needed capital employed by the more active traders. The "auxiliary specialist" concept, which on the surface appears to have merit, could not, as a practical business matter, survive in a purely passive role.

Off-floor

- Be impossible to implement. Trading will take place, whether on the Floor or off the Floor, and the abolition of "floor trading" would merely create more "off-floor" trading, either as member or nonmember activity, not subject to control by the Exchange.

Consequently, it is necessary to register disagreement with much of the argument and with the conclusions of the Special Study. It is felt that the Special Study could more usefully have defined the areas in which floor trading activities should be improved to overcome the adverse aspects and to make the presence of mobile, speculative risk-taking capital more broadly applicable to the functioning of the market.