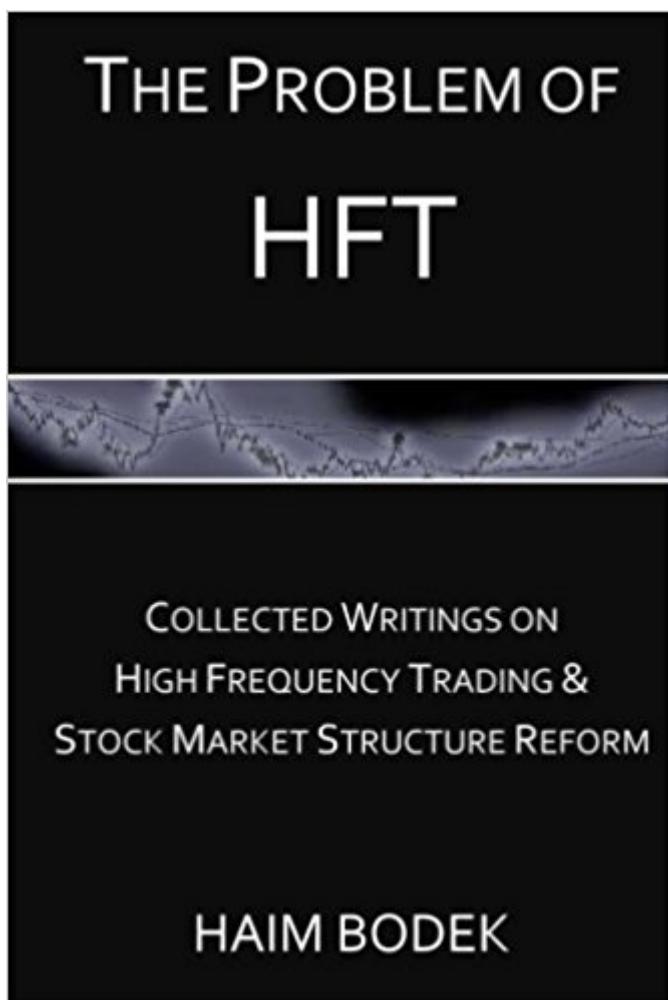


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# The Problem Of HFT - Collected Writings On High Frequency Trading & Stock Market Structure Reform



## Synopsis

This book explores the problem of high frequency trading (HFT) as well as the need for US stock market reform. This collection of previously published and unpublished materials includes the following articles and white papers: 1. The Problem of HFT - explains how HFTs came to dominate US equity markets by exploiting artificial advantages introduced by electronic exchanges that catered to HFT strategies2. HFT Scalping Strategies - describes the primary features of modern HFT strategies currently active in US equities as well as the benefits these strategies extract from the maker-taker market model and the regulatory framework of the national market system3. Why HFTs Have an Advantage - explains the critical importance of HFT-oriented special order types and exchange order matching engine practices in the operation of modern HFT strategies4. HFT - A Systemic Issue - a discussion of the latest industry and regulatory developments with regard to exchange order matching practices that serve to advantage HFTs over the public customer5. Electronic Liquidity Strategy - proposes a conceptual framework for institutional traders to achieve superior execution performance in HFT-oriented electronic market venues6. Reforming the National Market System - proposes a 10-step plan for strengthening the operation of the US equities marketplace in order to serve the needs of long-term investors7. NZZ Interview with Haim Bodek - addresses current topics and proposals for US equities market structure reforms8. TradeTech Interview with Haim Bodek - addresses the current status of the HFT special order type debate

## Book Information

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## Customer Reviews

"Today the US Equities market is comprised of 13 Exchanges, 50 dark pools and a host of internalizing brokers. ... Haim Bodek has both been on the front lines of understanding the penalties

of not fully comprehending this complexity, but also helping bring this complexity to light. This book is a must read by anyone attempting to fully understand the challenges of professionally competing in today's complex and challenging electronic trading environment." - Larry Tabb , Founder & CEO Tabb Group "This is a must-read for any trader in the markets. It's that simple. Mr. Bodek is shining a light onto the troubling games and unfair practices that have actually come to serve as the foundation of our high speed marketplace." - Sal Arnuk, Co-Founder Themis Trading LLC & Co-Author Broken Markets" Haim Bodek lays out the problems created by the explosion of High Frequency Trading."- Ted Kaufman, Fmr. U.S. Senator from Delaware" Haim Bodek's book is a much-needed insight on high-frequency trading and the architecture of securities markets. Accessible to outsiders and free of hype, this book offers a concise analysis of relevant concerns and advances thought-provoking proposals for regulatory reform."- Stanislav Dolgopolov, Assistant Adjunct Professor, UCLA School of Law

The adverse impact of controversial HFT-oriented special order types upon the institutional investor is now a center stage topic in the US equities market structure debate. Exchanges Get Close Inspection - Scott Patterson & Jean Eaglesham, WSJ, 11/19/12 Analysis: Complaints rise over complex U.S. stock orders - Herbert Lash, Reuters, 10/19/12 For Superfast Stock Traders, a Way to Jump Ahead in Line - Scott Patterson & Jenny Strasburg, WSJ, 9/19/12 See my website [haimbodek.com](http://haimbodek.com) for links to these articles as well as more information on my role in alerting regulators and industry to a number of unfair and discriminatory practices that have enabled HFTs to exploit exchange order matching engines. Follow me on Twitter: @HaimBodek.

This book, as advertised, is a collection of articles published in various professional forums. So it should be no surprise that it contains a lot of industry jargon, acronyms, and assumptions about the knowledge level of readers. I know a fair amount about general software, hardware, electronics, telecommunications, and computerized trading, having worked in all of those fields in my life, but I still probably only understood 70% of what was said in this book. I felt that most of the book was concerned with special order types on the exchanges, but the implications and proper (or improper) use of all those order types were not known to me. More to the point, there were no detailed examples in the book that explained the issues to readers such as myself. Many issues were mentioned, and many, many order types were mentioned, but I don't think the book did a good job of explaining (even in general) how any of them worked. Mostly the book would mention or identify something, and claim that it gave an unfair advantage to someone, without ever explaining to the

reader why that was the case. Perhaps these things that I am missing are general knowledge in the professional forums in which these papers were originally published. But I think this book is weaker because of the lack of explanations. I thought the best part of the book was the authors list of 10 suggestions for reforming the current electronic markets. They all made sense to me. I thought the weakest part of the book was the authors writing style. I found that many of the sentences required two or three readings to dig past the awkward wordings and phrasings to find the meaning. I would not recommend this book to anyone except a professional who understands the many software order types used within the industry.

Haim did a great job highlighting the more complex issues around the micro-structure of American financial markets. Avoiding the typical complaints that are heard, Haim dives into the deep connections around exchanges, certain High Frequency Traders, and the order types created for those specific traders. What I found to be the most shocking was under the section The Alpha in an Order Type. Haim addresses the knock-on effects created by Reg-NMS in which certain order types were created to help HFT during specific market conditions so as not to hinder the traders strategies. The most shocking part is found at the number three slot in a list of innovations which served to preference HFT over the public. Traders who were entering orders and expecting to be "makers" wound up having their orders flipped into those that would be identified as "takers", resulting in a fee being paid. This is not a public order type and subjects non-HFT investors and non expert-network connected traders to manipulation through order types that are not part of the public record. This type of catering to HFT creates an issue around disclosure as some traders have no way of knowing about this type of back-door manipulation. These order types are not the generic Limit, Market, AON, etc. They were specifically created for specific market conditions for specific traders and the only way to know them is to have cocktails with an exchange head. Think of it like this: in chess there are specific move sequences all players understand and accept. Players can only use the standard pieces and move them only in accordance with the rule book. However, lets say that with one move away from checkmate, the other player introduces a new movement ability to win the game, you'd call him a cheat. The chess piece (order type) can only be used a certain way, altering it subjects the integrity of the game to depreciation. Haim walks through the complexity of this and what it means for traders who may be identified as "uninformed". It takes guts for someone to put themselves on the line and make information like this public for all to see. Many of us address these things on blogs or among ourselves, limiting the ability of someone who isn't "inside" or "in" finance to gain an understanding of these new knock-on complexities created

through the implementation of Reg-NMS. The Problem Of HFT makes this available to everyone who can read or listen to an audiobook. Anyone who is willing to share this information and subject the investors world to more honest discussions on the structure of our market from routing to order types should be listened to. You will not find another book packed with as much information as this. The collections of articles and papers is enough to bring anyone up to speed on the underground complexities about HFT that are not addressed in WSJ or IBD. A must read for professional Wall Street insiders and for mom and pop investors. No one should make another trade until they have read this material! For a cost less than the commission charged by discount online brokers traders and others alike can finally understand what happens to their order once it is sent into the fragment matrix which is the American financial market.

High frequency trading is all about speed, right? Turns out, not quite. Yes, speed is a prerequisite, but to quote Haim Bodek: "the US stock market had become almost exclusively a special order type game." In other words, to play the game, you need to understand the "plumbing" of the markets, the special order types, and how they work under the hood -- without that, you'll almost always lose against the new breed of HFT traders. The problem is, these order types are neither consistent, documented, or regulated. As a result, few firms "in the know" get guaranteed returns, at the cost of all the other market participants. The system is broken and Haim Bodek provides a rare glimpse into this world...If you're not familiar with the space, I would recommend starting with "Dark Pools" by Scott Patterson first, and then coming back to these essays. Haim's work assumes that you're familiar with the field, the jargon, and the general problem, but it's also nothing a little research can't fill in.

After reading two other books on HFT ("Crashshoot Investing" and "Dark Pools"), I decided to delve further into it with a more technically oriented book. All three books are excellent, but Haim Bodek's book is written primarily for professional fund managers and traders. It's a short read, and will give institutional money managers good insight as to what is going on with stock market plumbing. The SEC should also take a look at it.

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