Financial Research Advisory Committee Meeting

February 25, 2016

Discussion Topic: Market Structure Program

The Dodd-Frank Act broadly requires the OFR to conduct, coordinate, and sponsor research to support and improve regulation of financial markets. It also directs the OFR to investigate disruptions and failures in financial markets. We are fulfilling this mandate in part through our program on market structure.

Our program focuses on macro and micro market structure. Who are the buyers, sellers, and market makers? How many participants are on each side of the market? How easy is it to enter the market? What information do the participants have and how do they use it? How much influence do they have on price quotes and transaction prices? How are trades executed?

In financial markets, market structure varies based on the assets traded and the rules governing the market. Changes in a market's structure can have implications for financial stability. For example, nonbank financial firms may transform into shadow banks, engaging in credit intermediation as banks do but without the same oversight as banks. High frequency trading can alter trading speed, transparency, and market efficiency. After a merger, a larger surviving firm can have more influence on price. Changes in how prices are quoted can alter price volatility.

Assessing the systemic impact of market structure may require transaction-level data across markets and market participants. The OFR can meet this challenge because of its unique mandate to collect and standardize data across financial markets. Research under this program reflects this unique position.

This program has four components:
1. Identify changes in market structure.
2. Analyze interplay between innovations, regulations and changes in market structure.
3. Identify gaps in data needed to monitor changes in market structure and collaborate with primary regulators to close them.
4. Develop tools to monitor changes in market structure and evaluate policies to improve market transparency.

Questions for discussion
1. How should we prioritize the program components?

2. Where do you see changes in market structure occurring today? What risks are you most concerned about?

3. What data do we need to monitor changes in market structure? What level of data granularity is needed?