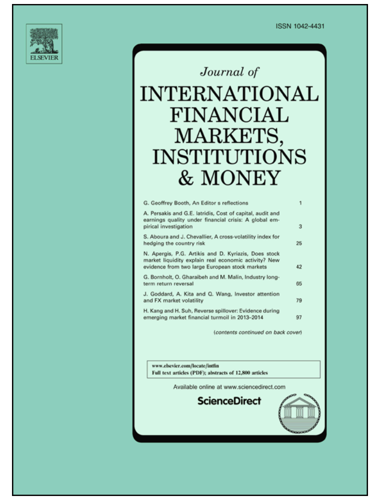

Curbing the Growth of Stock Trading? Order-to-Trade Ratios and Financial Transaction Taxes

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Curbing the Growth of Stock Trading? Order-to-Trade Ratios and Financial Transaction Taxes[◊]

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Abstract: The growth of financial markets provokes regular debate, particularly in Europe, and in the aftermath of the global crisis a number of reforms have been proposed. In particular, two regulatory measures have been put forward: order-to-trade ratios and transaction taxes. This paper aims to quantify the impact of such initiatives. To do so, I consider market liquidity and volatility in the Italian Stock Exchange (*Borsa Italiana*) over the 2011-2013 period, which provides a unique opportunity for empirical assessment: first, a penalty for high order-to-trade ratios (OTR) was implemented in April 2012; second, a transaction tax on securities (STT) was introduced in March 2013 on Italian large and mid-caps; third, this tax was extended to derivatives in September 2013 (FTT). No other country has gone so far in terms of financial market regulation. I identify causality via a difference-in-difference approach (with German firms and Italian small caps, when appropriate, as control groups) and a regression discontinuity design. I find that neither the OTR nor the STT/FTT had a meaningful impact on market liquidity or volatility. There was however a substantial drop in OTC trading.

Keywords: Financial transaction tax; Securities transaction tax; Tobin tax; Order-to-trade ratio; High-frequency trading; Liquidity; Volatility; Italian Stock Exchange; *Borsa Italiana*.

JEL Classification: F38, G21, H25.

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