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Designated Market Makers Still Matter: Evidence from Two Natural Experiments ☆

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Abstract

Independent technological glitches forced two separate trading halts on different U.S. exchanges during the week of July 6, 2015. During each halt, all other exchanges remained open. We exploit exogenous variation provided by this unprecedented coincidence, in conjunction with a proprietary data set, to identify the causal impact of Designated Market Maker (DMM) participation on liquidity. When the voluntary liquidity providers on one exchange were removed, liquidity remained unchanged; when DMMs were removed, liquidity decreased market-wide. We find evidence consistent with the idea that these DMMs, despite facing only mild formal obligations, significantly improve liquidity in the modern electronic marketplace.

JEL Classification. G14, G24

Keywords. Market Makers, HFTs, Liquidity, Obligations, Trading halt

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