DEATH OF A SALES TRADER:

CAUSE OF DEATH:

BLOCK TRADING?

BY

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ABSTRACT

This manuscript seeks to determine the future of the block trade as well as the institutional sales trader. It does so first through the review of all relevant literature on the block trade and sales trader. The block trade, algorithmic trading, high frequency trading, alternative trading systems and regulations are the factors researched. The paper then reviews interviews that were conducted specially for the study. Five institutional stock traders were interviewed; four from JonesTrading, and one from Cantor Fitzgerald. After thorough reporting and analysis of the results the manuscript concludes. The conclusion is that fragmentation and lack of transparency has been hurting the block trade and the institutional sales trader. The block trade however will not disappear, and cause the sales trader to go extinct. Rather the sales trader will fall victim to evolution in the next 10-20 years.
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INTRODUCTION

Evolution is one thing that is constantly working around us, all day, everyday; it never rests. Things are always changing, and we do our best to keep up with change but sometimes we fall behind. Evolution is a product of change, and change a product of evolution. Our financial markets are ever-changing, the mass of moving parts always shifting; never still. The stock market accounts for a large share of this movement; prices consistently ticking in every direction. This type of change is accepted and expected. The real change however, is the type that causes those around it to evolve and adapt. In the beginning the stock market was a relatively simple machine. Throughout the years parts have been added, removed, and modified, each change affecting the parts around it. This cycle was slow at first, the machine becoming more complex, technology slowly advancing, new methods/techniques popping up, and crisis were few and far between. Then things started to change as they always do. As a result, the evolution of the stock market has been wild over the past few decades.

Electronic trading was the major advent that started up this wild time. It was the major first step, after which the market would never be the same. New trading methods and techniques were the leading edge of this change. They were enabling us to do more; it was a time of increase. Places to trade, ways to trade, and what to trade all were increasing, thus giving investors more options and lowering costs, which is good. Along with the good also comes the bad. There were more areas that could be exploited in the markets. When that occurs, regulation follows, and the other players change and evolve to protect themselves from it. It’s a cycle, and it’s never ending. We evolve to survive based on everything that is happening around us. Trading is no different, and we have seen that the ability to evolve is not without limits. Once major pieces of the securities trading industry have today disappeared. These events have
occurred as both direct, and indirect results of the advances and changes in the industry throughout the years.

There are today so many moving parts that are often unpredictable. One day a certain method is perfect, providing a great amount of utility, and the next it could be obsolete. The most relevant fear though, is not whether a system or method will go extinct; it is that as a result the traders themselves will go extinct; no longer able to provide utility competitively. This fear is prevalent because automation of trading has replaced many of the pure traders who used to fill the NYSE floor. These were the individuals that the “buy-side” (portfolio managers, asset managers, investment managers etc.) would call when they were looking to trade a stock. These were the market makers or specialists whom are today all but extinct. Their jobs were to provide liquidity, execute trades, and try to capture a spread at the same time.

Electronic Trading made the automation of trading possible. Buy-Side managers/traders could enter an order electronically and the computer would find the other-side of the transaction. Computers were able to do what humans once did; and more importantly, they were able to do so faster and cheaper. The addition of algorithmic trading, alternative trading systems, electronic communication networks, and high frequency trading was all made possible by these computers. Trading algorithms are written to follow any strategy, and do so faster than a human ever could. The buy-side trader began to use these inventions as opposed to outsourcing orders to a sales trader, specialist, or market marker. The machine became the boss in the equities business. Specialized computer programs were handling almost all of the trades and strategies that humans traditionally would. The pure liquidity and execution provider had all but vanished.

In 1982 there was no volume in the stock market, and there were two exchanges; NYSE and the NASDAQ, which was then referred to as the OTC (over the counter) market. During
that time over 90% of all trades of NYSE listed stocks went through the floor of the NYSE. Today, the traders that once packed that floor have all been replaced by warehouses that span city blocks and are filled with computers. The managers of the buy-side can take care of most of their trading in-house, push a button and the computers do the rest. There is almost no use for the 3\textsuperscript{rd} party trader who takes orders and provides best execution; almost. There is a small part of the equities business that is still handled mostly by humans known as block trading. In this form of trading the transactions occur in large “blocks” of securities and are often handled by a 3\textsuperscript{rd}-Party. This 3\textsuperscript{rd} party trader is known as the institutional sales trader, and their role is to provide liquidity and best execution. The orders that produce these trades are placed by institutional investors. These are large, non-bank entities such as insurance companies, hedge funds, management companies, and more. Since they trade in such large amounts, these investors require lower commissions, customized trading strategies, and large chunks of liquidity. The Institutional Sales traders are the ones providing those services. Their high-touch style of trading is still preferred by many institutional investors to low-touch, often automated methods. High-touch traders provide liquidity and custom tailor strategies for the best execution of trades. This allows them to minimize the market impact and therefore the cost of trades to the client as well. These factors are of vital importance when it comes to block trading. Relationships and trust are vital and they are also something computers cannot provide. This has kept the institutional sales trader from disappearing for a long time.

The sales trader has been around for many years. A sales trader is someone who sells their ability to execute trades most effectively and efficiently, known as best execution. They also sell their ability to source liquidity. Institutional Sales traders are the last major surviving species of sales trader. They mostly exist today as a part of well-established, broad based,
investment houses. There are also a number of niche-based, “Institutional Services” firms. These firms focus almost solely on institutional sales trading and providing best execution. Over the years the sales trader has evolved and adapted more than any other type of trader, which is why they are still around. Today however, questions are starting to arise about how much longer they will be able to survive. The threat of them being cut out of the process completely looms large.

The ability of the sales trader to do their job and provide utility to their clients depends on their knowledge of, and the actions of, the market around them. The latter is the reason there are questions arising as to just how long the Sales trader will be around. A large amount of emphasis has always been put on trading as efficiently as possible; who can do it for cheapest? Since 1975, when the required industry-wide commission rate was abolished, the per share commission for sales traders has dropped from around twenty-five cents to three to four cents. The argument of course is that the amount of shares being traded has increased, but will the trend continue? Will the institutions and buy-side firms that send orders to these traders eventually cut them out as things continue to advance?

There are so many factors within the market that affect the ability of the sales trader to perform their job. Studies have been conducted on a few of these factors individually. Greenwich Associate’s Kevin McPartland (2014) performed a study in which sell-side and buy-side firms were surveyed. The results of the survey were used to forecast what the sales trader of the future would look like. The study was well encompassing and looked at factors such as trader technology, regulations, customer preferences, and strategy. (McPartland 2014) Another study by the TABB group looked at the demand for, and use of block trading by institutional investors. The study was a central part of a May 2015 report that focused on the preferences of buy-side firms and managers. Through this focus, the report sought to identify the chief
motivations for block trading, which is a large part of the sales trader’s business. (Mostowfi 2015) An April 2014 article written by Andre Cappon, tells us how the brokerage world has changed. Traders used to receive fixed commissions and there was no competing for cost; then came the computers. The article gives a decent overview of how the institutional trader has evolved, but may not survive much longer. (Cappon 2014)

The number of institutional sales traders has been falling slowly, but steadily over the past decade. They often feel like they have become a dying breed. Evolution is inevitable in any aspect of life. Those who are successful will adapt and move on. The institutional sales trader has continued to succeed by providing the same service they always have. The only thing they’ve changed is how and what they provide it for. The block trade is a major part of this continued success. When it comes to blocks, man still beats machine most of the time. However, over the past decade and a half as the market environment has changed, the number and size of block trades executed has been falling. This is a major concern for the institutional sales trader.

While computers are sometimes better than humans when it comes to blocks of large securities (Apple, Disney, Etc.), most believe that the institutional sales trader will always be best when it comes to blocks of small and mid-cap securities. Those securities are usually illiquid and a successful block trade in those names will always require the high-touch that only the institutional sales trader can provide. Everyone realizes that it is natural for the number of sales traders to decline. As they have become more efficient, fewer traders can handle more of the work, which is true of any industry. However, if the block trade were to fall out of use as a style of trading, this would signal a rapid extinction for the last of the sales traders.

Institutions love to trade in blocks. They get every share at one price, it is the most cost efficient way to trade, and if executed correctly they will have minimal market impact.
Institutional sales traders love to trade blocks because it’s how they make money and what they love to do. Absent of any other factors this relationship would last forever, but that is somewhat of a fantasy given the tons of moving parts in the securities industry. Therefore, like all good things it is bound to end at some point in the future, but when, and how? The surest way for a relationship to end is for one of the parties to die. Institutions are not going die, they’re the immortal of the two. The death of the institutional sales trader and therefore the death of the sales trader in general is a much more likely event. What could cause this death? The block trade is the heart of the institutional sales trader; cut it out and they will die. That seems unlikely given how great of a tool it is for the institutional investor, given the right circumstances. So will the circumstances drive the block trade and therefore the sales trader to extinction or lead to the comeback of the block? What even are the circumstances driving the block down? What factors contributed to them? We need to know why-what-happened. Why did what happen in the past? Why is what happening now? Why could what happen in the future? If the block stays around is the institutional sales trader still safe? For how long? In short; What is the future of the institutional sales trader?

Various studies exist on the sales trader and the factors that surround them and affect how they do their job. The problem is these reports and articles have never put it all together; they don’t go deep enough. A 2013 newsletter by the then President of the Security Traders Association, Mr. Tom Carter, addresses the issue of the “need for speed” and the “race to zero latency”. Carter talks briefly about how these issues have affected the sales trader and demand for the block trade. He fails though to mention how other forms of technology and trading are affecting them at the same time. The closest research has gotten to truly putting it all together is McPartland’s 2014 report. The fatal flaw with that report is that they have assumed the sales
trader will still be around. The report looks forward with no mention of historical events, and is based solely on surveys conducted with small sample sizes, no interviews with professionals, no looks at upcoming regulation, but merely what they think will happen based on many ill-founded assumptions.

The research thus far has failed to take everything into account. There are fragments here and there but never a comprehensive look at past, present, and future. This paper will first take a look back at the history of the institutional sales trader and broker. It will analyze the advances in technology, techniques, regulations and more that have affected them over the years. It will look at what is happening presently as well. What is causing the sales trader problems, and what is allowing them to thrive. The goal is to first identify all of the major moving parts that could be affecting the block trade and institutional sales trader, from algorithms to regulations. After a thorough analysis of these factors the paper will then be able to look to the future and determine what will occur and why. Will the sales trader continue to evolve, or go extinct?

A large part of the sales trader’s commissions and business come from block trades. So focus will be put on the block trade and the factors affecting it. Many young students including myself are fascinated with sales traders, love what they do, and wish to pursue a career doing such. They are the last of the pure execution experts. They’re neutral, transaction oriented and commission based; moving sometimes millions of shares at a time. The question is though will they be around in a decade? Institutions are wondering the same thing. Is there a more efficient way for them to do business? This would probably include cutting out the sales traders. The development of the “fourth market”, in which institutions would trade directly with each other, has been happening for a while.
When you look at it, this is a question that has been partially answered by several articles and reports. The problem is that each one looks to only a fraction of the factors that affect the quality and quantity of a sales trader’s business. Furthermore, these reports are based off of impersonal surveys and methods. This paper will use some of this literature as it seeks to put it all together, first looking to each factor separately to examine the effects on sales traders and the block trade. Interviews conducted with well-tenured sales traders and other industry professionals will serve as the glue to bring all these factors together. They will allow the affects of the factors to be seen and explained more clearly. Then, an analysis of the results of the research will be conducted. After analyzing what has been collected we will look at the research as a whole and discuss several factors surrounding it before determining finally whether the Sales trader will survive or not. Will the Block Trade be the factor that finally pushes the sales trader out, or will it be something else all together?

REVIEW OF LITERATURE

In this section a review of relevant and significant works pertaining to the block trade and sales trader will be surveyed. There have been several reports produced which contain important pieces of information on various areas of block trading. The literature on the factors affecting the block trade will be reviewed in sections based on these factors for purposes of organization.

The Block

The number of block trades on the NYSE started to grow in the late 1960’s as institutional trading increased the size and volume of orders (Markham 2002). Originally block trades were often executed by institutions negotiating with each other and then reporting trades.
Most block trades would occur Off-Exchange, through crossing networks or other alternative trading systems, and it’s the same today. As order size increased, the market became more complex. Institutions started to turn to brokers who were better able to execute block trades; this eventually gave us the institutional sales traders we have today. As trading methods and technology became more advanced, institutions would often have trouble securing block execution, the growing complexities of the market making things unclear. The block grew in popularity as a good way for institutional investors to move a lot of stock without impacting the market. This of course was made possible by the “high-touch” trading performed by sales traders. Their ability to evolve and stay informed about the new evolutions in trading allowed them to continue to provide liquidity and best execution; it kept their clients coming back.

Institutional investors today have the opportunity and ability to trade through cheaper self-directed channels but more than 50% of an institutions trades will go through equity sales traders (Mcpartland 2014). Now why is this? A 2014 study by Kevin Mcpartland of Greenwich Associates tells us that the uncertainty and complexity of the markets, paired with a smarter and relationship based sales trading force is why the buy-side keeps picking up the phone. The answer given in the report is valid. That is why institutional investors send orders to broker sales traders, but McPartland’s research leaves out a glaring detail. Institutional Investors are big, and will almost always have in-house traders to take care of the usual, “ease to fill” types of orders. However, blocks are hard to execute for a lot of these investors. The uncertainty and complexity out in the markets is what makes them so. The block trade is the reason institutional investors are still going to sales traders. These large trades require access to liquidity and market information in order for best execution (lowest cost, lowest impact) to occur. They also require the style of “high-touch” trading that only institutional sales traders can provide, via trust, and a strong-
relationship. The report omits the block completely; the word block is mentioned only once and it’s in a different context. Simply put, McPartland (2014) fails to mention the one thing that has kept institutional investors calling up Sales traders instead of using automation. This report is a prime example of the flawed research that has surrounded the institutional sales trader and the block trade. There is a little amount of literature available on this topic, and even a smaller amount within that is actually useful.

The only entity that has reported on the block more than once in the past few years has been TABB Group. TABB Group is a financial market research and strategic advisory firm focused exclusively on capital markets. In May 2014, they produced a report on the block trade. Authored by Larry Tabb, (2014) the report opens by saying that block trading has lost its honor among institutional investors. That the block was once a very important tool for buy-side traders, but has now been almost forgotten. Figure 1 shows the downward trend of average on and off-exchange trade sizes from 2004-2014, and illustrates well the dire situation the block has fallen into (see Appendix A). The report then provides details as to why the block has lost it place, identifying the issues and broadly what caused them. Although the report lacks depth pertaining to the issues it mentions, it provides a good starting point from which to go deeper. The report is also regarded by many institutional investors and sales traders as accurate. The important thing to understand from this report is that actual institutional investors and sales traders were consulted, those who have dealt in blocks the most throughout history.

The hardest part here is to pin down the issues that have and are currently affecting the block. A 2013 speech by Tom Carter, an institutional sales trader and then President of the STA (Security Traders Association), provided great insight of the issues at hand. Addressing many securities-industry professionals, Carter (2013) states that a number of issues affect how sales
traders do business everyday and he continues to review those issues. The entire point of this paper is to analyze issues affecting the block and sales trader through the years. Then we will be able to see how they have evolved and determine whether or not the machine will finally win.

**Algorithmic Trading & The Block**

Algorithms are such a common feature in trading today because they have made the process so much more efficient that it would be irrational for traders/brokers not to utilize them. In trading, an algorithm is a mathematical model that is custom built to analyze quotes along with trades and identify liquidity opportunities. Then they take that information and make intelligent trading decisions (Rao 2006). Originally algorithms were used to solely identify opportunities in the market. They would do so based on the fundamental analysis of a security. The algorithms would tell them if it was over or undervalued and traders would act on this information (Read 2012). No longer were humans needed to calculate proprietary information. All investment houses began to use the same computerized models to estimate value. Then, in the early 1990’s, algorithms began to analyze the behavior of stocks throughout the day. They would search for opportunities that were much more short-term. These types of opportunities did not last very long and had to be acted on immediately. As Read (2012) said in his article on the history of Algorithmic trading, “no longer could an investment company afford to wait for a human to execute the trade a computer recommended” (p. 3). The computers and algorithms were then programmed to act immediately after identifying an opportunity. Algorithmic trading took off at this point. By 2010, algorithmic trading accounted for the majority of equities trades. It had also become increasingly popular in the Futures and Options Markets as is evidenced in
Figure 2 (See Appendix B) Eventually, a single computer could do what would’ve been the job of 100 traders years ago, and at a fraction of the cost.

Even though algorithms have almost removed humans entirely from the process of trade execution, they are not directly an enemy of the block trade. The markets have evolved in the past decades by introducing everything from decimalization to fully electronic exchanges. The affects were also widespread; costs fell, commissions lowered, and algorithms became a great tool for institutional investors. Using algorithms, institutional sales traders could control how their client’s orders were executed to ensure they were minimizing costs. For the institutional investor/sales trader the object of Algorithmic trading is not totally to maximize profits, but rather to control execution costs and market risk (Avellaneda 2011). The most efficient and least impactful way for block trades to be executed is to “do the deal upstairs” or “cross stock”. A cross occurs when a broker (institutional sales trader) is able to execute a trade within their own client network; when the buyer is a client, and the seller is a client at the same price, which is often different from the market price. The two parties transact “upstairs” directly through the broker’s crossing network, so the trade never “hits the floor” of the exchange (goes through the open market). Although the deal must be reported, the price is not so the market impact risk is zero. When institutional sales traders are not able to find the other side of a trade in the upstairs market and cross, depending on what their client wants, they may then take it to the floor (market). If this is the case, the traders will choose an appropriate algorithm based on what the customer’s strategy is (Carter 2013). The algorithms help the institutional trader get block trades done a fraction at a time and minimize market risk. The algorithms can be programed to trade based on an average price, time-period, and much more. This is known as “working” an order over time.
Algorithms are of great aid to the institutional sales trader, at least when they are the ones using them. Algorithms identify and execute trades in milliseconds, based on the information they are receiving. While institutional traders use algorithms to get the best execution they can for their client, other traders use them to best execute profits for themselves. The faster an algorithm is able to operate, the faster it can search the markets, find opportunity, and execute trades to take advantage of that opportunity. Although there are many algorithms out there, many are trying to take advantage of the same events in the marketplace; whoever does so first is going to profit the most. The speed with which these computers are able to connect with exchanges is directly correlated to how profitable they can be; the faster they are, the more the advantage over the rest of the market. This developed what is known as the “need for speed”. The bigger the computer, the more direct the connection to the exchanges. This meant the algorithms could trade faster. The big investment houses were best suited to take advantage of this because they had the most capital. Algorithms may be useful to institutional traders but they have also spurred issues such as internalization and the “need for speed”. This resulted in a new method of trading known as High Frequency Trading, which was made possible by algorithms. According to Carter (2013), High Frequency Trading led to most of the issues affecting the ability of the institutional sales trader to do business. Co-location, Data Feeds, due process for all, maker/taker fees and payment for order flow; all of these things are slowly eroding the block.

**High Frequency Trading & The Block**

High Frequency Trading, known in the industry as HFT, is not defined in any of our securities laws or regulations. HFT is not so much of a trading strategy but more an application of the latest market technology in several areas. These areas are access to markets, data access,
and the routing of orders. High Frequency Traders look to maximize the returns of established trading strategies. (Gillan 2015) While no clear definition exists there are several attributes of HFT that help describe it. A 2015 report from Price, Waterhouse and Cooper lists these attributes. First, “the use of extraordinarily high-speed programs for generating, routing, and executing orders” (Gillan 2015, p.4). Another is the use of “co-location” services, which come out of arrangements between High Frequency Traders and trading centers or their representatives. In these arrangements, exchanges will rent space to market participants (traders) so they can physically place their servers in close proximity to the exchanges/centers. By doing so, the time between order placement and execution, also known as latency, is reduced by microseconds (Gillan 2015). The faster they can get it done, the more money they can make. The 2015 report continues with several more describing factors of HFT. It includes the establishment and liquidation of positions in incredibly short periods of time, the submission of large volumes of orders that are cancelled shortly thereafter, and the practice of ending the day as close to a flat position as possible. HFT is a product of the technology and circumstances of the past decade and a half and seems to be hurting the block trade.

The biggest negative impact that HFT has had on markets and institutional investors specifically is that is has eroded their confidence. Anuj Agarwal (2012) of Cap Gemini tells how HFT has negatively impacted institutional investors through various predatory strategies and actions. High Frequency Traders will look to front-run large institutional orders, which adversely affects institutional trader’s ability to provide best execution. While one of the perceived positive impacts of HFT has been increased liquidity, much of this liquidity is “phantom” and not dependable. Gillan (2015) says, HFT has created “two-tiered trading markets” which benefit those investors with faster access to trading data, at the expense of others (p.5). Through these
actions, HFT has decreased the transparency of the markets, making investors less confident in the markets.

This drop in transparency has likely led to the drop in the amount of large block trades; as we know, HFT was made possible in part by the advent of algorithms along with other advances in technology which allowed it to gain immense popularity in the early 2000’s. Figure 3 shows that during the same time the percent of shares traded in blocks had been falling dramatically (See Appendix C).

**Alternative Trading Systems and The Block**

An alternative trading system, know as an ATS, is a non-exchange venue to match the buy and sell orders of its users. Many ATS’s are particularly designed to match trades of very large quantities. Institutional Traders will often use them to find the other-side of a trade. By using ATS’s for large block trades, traders avoid having to take them to the floor. This allows them to better protect the information around their order. This is especially important for trades involving securities which are thinly traded. Large orders can greatly impact the market for these securities. Electronic Communication Networks (ECN’s) and crossing networks are the ATS’s most commonly used by the institutional sales trader. Most block trades occur off of exchanges through an ATS.

ECN’s and crossing networks have been of great aid to the institutional sales trader and are used constantly to execute trades. Another form of ATS known as a Dark pool has helped protect the trader’s information as well, but it is also starting to hurt them and the block. A Dark pool is an anonymous exchange with a complete lack of transparency. Dark pools were created primarily to facilitate block trading by institutional investors trying not to impact the market with
large orders which would increase their costs. By trading in dark pools, institutional traders could avoid the risk of predatory algorithms such as “hunter-seeker” algorithms and other block adverse strategies. (Picardo 2015)

Dark pools originated in the late 1980’s and today account for over 40% of all U.S. stock trades daily. Scott Patterson (2012) tells us that dark pools were originally designed for institutional investors as a safe haven from the hunter-seek algorithms. However, by the late 2000’s most of these dark pools had been infiltrated by “Bots”, the computerized trading systems. This led to the problem of dark pools filled with predator algorithms, which were designed to front large orders (Patterson 2012). Many of the Dark pools out there today are not playing fairly by possibly giving more information to some than others. What Dark pools are doing is causing an even further lack of transparency to investors, destroying their confidence in the prices of securities. This is especially true for those securities, which trade heavily in the dark pools (Gillan 2015). Lower confidence in prices and market transparency seem very likely to be adding to the woes of the block and institutional sales trader.

**Regulations & the Block**

Trading Regulation has been a big part of the block trade, though not usually directly. Many of the factors affecting the block today have also been affected by regulations. There are two main regulations that have effected the trading world and the block over the past few decades: Regulation of Alternative Trading Systems and Regulation New Market System. The Regulation of Alternative Trading Systems, known as Reg ATS, was imposed in 1998, and Regulation New Market System, known as Reg NMS, was introduced in 2005.
Reg ATS was enacted to protect investors and resolve concerns arising from the use of alternative trading systems. It required stricter record keeping and demanded more intensive reporting once a trading system reaches more than five percent of the trading volume for a given security (SEC 1998). Agarwal (2012) tells us how Regulation ATS restricted the monopoly of the NYSE and NASDAQ, which gave rise to electronic trading platforms serving as ATS and other venues. Reg ATS has adversely affected the block trade ever since it was enacted, this was brought to my attention by several traders in the industry before this study began but there is very little literature available on it.

Reg NMS looked to improve the exchanges with improved fairness in price execution as well as the displaying of quotes and access to market data. Regulation NMS is comprised of four main components: the order protection rule, the access rule, the sub-penny rule, and market data rule. The main part of this regulation is the order protection rule, also known as the trade-through rule. Reg NMS is clearly one of the major regulatory events of the past few decades but its direct affects, if any, on the block were hard to discover in any available literature.

**METHODS**

Information on the past, present, and future of the Institutional Sales trader and Block Trade is highly fragmented and scarce. From a couple of reports, we’re able to see the downward trend of the block through graphs and charts. Along with this data comes a paragraph or two citing the general factors affecting the block. Upon trying to dig deeper into these factors, plenty of information was available but very little about how they are affecting the block trade and therefore institutional sales trader. Every report loves to include a chart about the falling numbers of the sales traders as of late, or the declining amount of block trades. Then you’d get a
useless paragraph along with these graphics stating nothing but the obvious and not explaining why. More information was needed to bring all this fragmented information together and properly forecast the future of the sales trader. We need to know, why what is happening.

The only way to get the high quality of information needed to fill in the blanks between the visual trends and general explanations was to go to the institutional sales traders themselves. This was an invaluable method of research for several reasons. Those interviewed were well experienced and established. They provided great history on the effects of various factors throughout the years, and the evolution of the sales trader. The specialization of some of these traders in areas like regulation, algorithms, and client demands allowed for certain interviews to focus in on a specific area affecting the block. A big focus was the changing demands and concerns of the “client”, or buy-side managers in response to these ever-changing factors. Most helpful was the discovery of the detailed effects of certain factors on the block that were not available anywhere else.

There was, however, one noticeable drawback of this method. Bias was inherent in several of the traders interviewed around some of the franker questions. This is expected, as even if they believe it, most traders would not readily admit they are going to be replaced by computers, especially the CEO of a company. This was noticed mainly in the first company of traders interviewed. The bias was attributed to the fact that the life of the company, the bulk of their business, depends on the institutional client and the block trade. To mitigate this bias, questions were changed over time to not appear as threatening and an interview was obtained with a sales trader in a company which operates in many other areas of trading as well.

As stated, traders from two of the very best companies in block trading were interviewed. The majority from JonesTrading Institutional Services, the industry leader in block trading, a
firm that focuses almost purely on institutional trading. For over forty years, JonesTrading’s sole focus has been creating liquidity and trading blocks for their institutional accounts. They follow a traditional style of matching clients using a high-touch, personal, relationship-based model. This strategy continues to best their electronic and automated block trading competitors such as Liquidnet. The second firm is a competitor of the first, also one of the top firms in block trading using a similar high touch model, but operating in many other financial areas as well; Cantor-Fitzgerald. In Figure 4, TABB Group spoke to buy-side traders to determine which firms were best at trading blocks in 2015, you can find both firms highly ranked (see Appendix D). The interviews were recorded or occurred via email. They were reviewed to determine which questions and answers were most relevant. Those determined to be so were transcribed and are reported here honestly. For copies of the entire interviews please contact the author.

**RESULTS: WHAT ACTUAL TRADERS ARE SAYING**

**Tom Carter, Managing Director, JonesTrading Institutional Services:**

Mr. Carter Started his work at JonesTrading is 1993. In 2013 Carter served as the 77th Chairman of the Security Traders Association, a unique trade organization which represents securities industries professional’s interests with legislators, regulators, and others. Mr. Carter continues to provide educational outreach to members of congress and is a part of continuous discussions with the SEC on market structure issues. He has obtained his Series 7, 24, 55, 63 industry licenses. The interview with Mr. Carter was conducted via email, due to the nature of his responses they will be presented in narrative form.
As an industry leading expert on Regulations past, present, and future this was a central topic of the discussion with Mr. Carter. He explained that the two major Regulations affecting the block in the past and present are Regulation ATS and Regulation NMS (T. Carter, personal communication, February 9, 2016). We know that Regulation ATS in essence took away the monopoly power of the NYSE and NASDAQ, but what else? Reg ATS was aimed at protecting investors and increasing the transparency of the markets, but it failed. Carter thinks that “the greatest disaster is the fragmentation that is the hallmark of our current market structure.” He also calls Reg NMS “a disaster”, saying it was the glue that was supposed to fix the mess that Reg ATS started and bring the market together, but it just furthered the problem. Reg NMS “hurt the block because it created even more fragmentation,” Carter says. When asked why these regulations are not effective and are hurting investors and the block Carter explained further. Government Regulations miss the mark because they are Rules-Based Regulation: “it’s run by a set of arbitrary rules created by government officials typically with very little real world experience.” Carter said that Principles Based Regulation is more effective, based on overarching core principles which guide decisions. “Rules miss their mark because of their specificity or because they haven’t boxed in the real issue,” he said (T. Carter, personal communication, February 9, 2016).

The interview continued when Carter was asked about why so much fragmentation has been caused that is hurting the block. He said that Reg ATS and NMS opened the doors for so many new venues. “Today there are over 40 dark pools, 12 exchanges and god knows how many ATS’s- all these different execution points are supposed to interact (according to Reg NMS) - but they don’t- each order is internalized first.” He explained that brokers and exchanges will use algorithms to rout the orders they receive internally. This means trades are executed at a better
cost for the broker. These orders are only sent to the market if they can’t be accomplished in house. Also, if a block is traded in a Dark Pool it was never exposed to the market, so there is no transparency. That is the main issue, he said, Transparency. When asked if there is regulation on the way to fix the fragmentation, Carter cited the fact that it has taken over fifteen years to even begin to correct the mistakes of Reg ATS. “The SEC will take years to get anything on the books”, he says. In closing, Carter spoke about HFT. They cause volatility which is hurting the block trade. Institutions are afraid to place the block orders, and when they do it’s hard for sales traders to execute them because of all the movement. I asked if there is any regulation on the way. He said yes, “HFT is not a registered investment advisor and enjoy freedoms a traditional money manager does not. They have taken advantage of this repeatedly. SEC is close to leveling the playing field but will the regulator miss the mark or get inundated with lobbyists and have the message muddled?” (T. Carter, personal communication, February 9, 2016).

William “Packy” Jones, President and CEO, JonesTrading:

Mr. Jones started in the securities business in 1978 working for Jefferies & Co. Inc. In 1980 he went to work for Newhard Cook and in 1982 he joined Jones & Associates and has worked every position in the firm. In 2004 he assumed the role of Executive Chairman and CEO, reorganizing the firm under the name JonesTrading Institutional Services LLC. A lot of the conversation with Mr. Jones centered around the evolution of the institutional sales trader and the industry (W. Jones, personal communication, December 22, 2015). Due to the nature of the in-person interview with Mr. Jones and his responses, the results are presented in a question-answer format with analysis and explanation after major points.
When he first joined JonesTrading in 1982, things were just starting to get institutional he told me. Pre-1975 you were required to charge a certain commission rate, after that the “handcuffs came off” as he explained, and you would discount commissions to get business. After the crash of 1987 everything was great, everyone was buying and there was lots of trading going on. He also added that JonesTrading has made money every month they have been in business; they have infrastructure costs but no risk costs. Then Mr. Jones commented on the decline of the block and physical trader and how Jones has evolved and continued to thrive over the years. “When you’re reactionary it’s more difficult to be successful, it’s almost better to predict, we’ve just stayed true to our colors. Take care of your client, hire the best people, do what you’re good at.” He continued with, “It’s all a matter of asking the right question, you ask the right question, you get the right answer.” (W. Jones, personal communication, December 22, 2015). The most important thing to the institutional trader is liquidity, the 2nd most is information.

When getting into a discussion about Regulation NMS and the block, Mr. Jones said that as a result of the regulation we entered into more of a retail market. He also touched on some of the factors discussed earlier in the paper.

You have decimalization, stocks trading at much smaller and tighter spreads, at the same time the development of HFT’s, also around the same time the exchanges went from utilities to for profit. So now the exchanges, their client wasn’t the broker and stuff as it had been in the past, their client was now the high frequency guy who wanted to co-locate and sit right next to them and would pay a fortune for that. This set up the whole thing of the HFT and the preying on orders and selling order flow, it made the market a lot more fragmented. So people [institutional managers, traders] don’t trust anyone
anymore, so instead of putting an order in one place, they would go all over. The market was all over the place and still is. [...] I think there still is a transparency issue and that’s what the regulators are looking at (W. Jones, personal communication, December 22, 2015).

Decimalization was one of the affects of Reg NMS which lead to the tighter markets Mr. Jones was Referring to. It can be seen in his response how HFT, ATS, and other issues covered in the literature review have affected the block trade and trader. Colocation, payment for order flow, maker/taker pricing; all issues touched upon in Tom Carters 2013 speech that was previously mentioned. It’s becoming clear that this is all causing a high level of fragmentation in the markets. A lack of trust is building in the markets because of the questionable and manipulative practices that were, and still are, occurring.

1. On Reg NMS’s affect on JonesTrading, the Institutional Sales Trader and The Block:

Because of NMS, a lot of clients went away, market makers went away, specialists went away, so information was at a premium, there was no information or there was misinformation. [...] During NMS fragmentation made it very difficult for them to get things done, which was great for us because we knew how to access the market and could still cross stock. [...] Reg NMS was probably an experiment that could’ve done better (W. Jones, personal communication, December 22, 2015).

Regulation NMS seems to have affected the block trade and sales trader negatively. It has greatly contributed to the disappearance of the physical trader. However, it seems that the mess created by Reg NMS in terms of fragmentation and lack of transparency actually helped
Jones Trading in a way as well. While their clients were having trouble seeing through the fog, Jones still had relatively clear market insight and access. This meant Jones and institutional sales traders in general were still providing utility and maybe were not as adversely affected by Regulation NMS as thought. However, there is some hard feelings towards Reg NMS as Mr. Jones expresses his final thought on it.

2. On how the institutional sales trader has evolved from the days of the specialist to today:

   It really hasn’t changed, the key, as it was then and is now, is how to make the right call and use the right system. Back then, say you had a broker who was close with the specialist in X stock, that broker was good friends with this guy [specialist] so he would get the inside look about who was buying, selling, and how the stock was trading. [...]. Therefore, this would enable the client to get his trades executed and be protected when things were trading on the NYSE. It’s the same thing today but it’s just more electronic. We know if we were going to be trading X stock then we will use Y or G algorithm, maybe a dark pool, or go upstairs and find the other side of the trade. (W. Jones, personal communication, December 22, 2015).

3. When asked about all of the alternative trading systems, exchanges, flow of information and how they are hurting the block, Mr. Jones did not seem too concerned:

   Like we were talking about before, the HFT’s were getting more information than others, so you have to be careful. What we’ve found is that if there is an algorithm, dark pool, that we are using that is not playing fairly, then we turn it off and go to the next one. There’s 44 venues out there, and as far as dark pools go you move onto the next one and see if you can find some volume.
4. On why clients have, and will continue to send orders to the traders at Jones and elsewhere:

   Frankly, we do 6-7 Billion shares a year, so we have a lot of opportunity to find out what works and what doesn’t and we can asses it, and figure it out [.....] A lot of our clients, particularly the smaller ones, don’t get all that volume so they don’t see it as easily as we do, so they ask us all the time, who do we use for this, who do we use for that. I just say, its always changing, if I told you what it is today, next week it could be different so I’d soon not tell you because I don’t want to lie to you (W. Jones, personal communication, December 22, 2015).

The Large volume of trades that Jones executes gives them valuable information and experience which they provide to their clients as part of their service. It allows them to know how to provide liquidity and best execution given the objectives of their client. The ever-changing markets means something that worked yesterday may not work today. This keeps clients coming back because the institutional sales traders at Jones and elsewhere provide liquidity and best execution that these traders and managers would not be able to access and accomplish on their own.

5. On how they will keep evolving and whether or not the institutional sales trader will survive as the last pure execution specialist:

   Do your job well, respect people, and you’ll do business with them. Not everybody, but a lot of them (W. Jones, personal communication, December 22, 2015).
Costel Goga, Head Research Analyst, JonesTrading:

Mr. Goga is the Head Research Analyst for JonesTrading. He started working at Jones in 2001, and is currently in the Dallas office. Due to the nature of the in-person interview with Mr. Goga, the chosen results are presented in a question-answer format with analysis and explanation following major points.

1. On how Reg NMS effected Jones and whether they had to adapt or not.

"We did at the beginning, but it was a quick process, it was still easy to print [Trade] blocks of the illiquid names, mid-cap, small-cap, arbitrage trades."

2. Would you say Regulations have worked generally towards or against the block?

Generally, against the block, introducing pennies- people weren’t as tied to one or two cents when I started. The markets were deeper, people would buy up an eighth or a sixteenth, people weren’t as tied to one or two cents. Those things have changed trading, making it hard to trade blocks because people tend to get very wedded to the price on the screen. Also there are so many marketplaces now, when I started there was one exchange, and upstairs. Now there is so many more venues, dark pools, making it so much more fragmented making it harder to trade blocks. You don’t know what else is out there because there is no way to efficiently find markets, people are spread so thinly in so many different places. Fragmentation, penny markets, have hurt the block. Reg NMS a little, but it really just kept people from printing things out of line [away from the market price] (C. Goga, personal communication, January 22, 2016).

Prior to Regulations ATS and NMS there was more trading going on at different prices than what was being currently quoted in the markets. Clients were more flexible in terms of
prices they would trade at, making it easier to get things done. The spread tightened due to the direct and indirect effects of these regulations throughout the 2000’s to present day. As a result, clients became less flexible on price which led to less big block trades occurring. This trend is clear in Figure 1 which was touched on earlier (see Appendix A). The regulations led to more venues which led to fragmentation in the markets. It became hard for traders and managers to access markets and liquidity. They then lost trust and confidence in available market information; all hurting the block.

3. On Technology as a whole over the years and the block:

Technology has just gained a lot more total involvement; technology isn’t that conducive for trading blocks. High Frequency and other things have moved in and are dominating trading, you don’t know where the volume is. There’s so many algorithmic type trading systems out there, so its just become a lot more difficult to know what the real markets are and who wants to do what. There’s a lot of electronic trading that’s muddling up the picture and the true scene (C. Goga, personal communication, January 22, 2016).

Technology seems to have not directly affected the block trade but rather it has done so indirectly. The development of algorithms, HFT, ATS, and more have all affected the block. They made it harder to find volume and get market information. All of the new moving parts have made it difficult to see why, what, is happening; which is why institutional sales traders get paid.

4. High Frequency Traders obviously haven’t been helping, how would you say they’ve hurt the block?
They are making markets, but their market making is so thin that prices are moving around so much and they contribute to volatility, and it’s hard to trade blocks when there’s a lot of volatility because people are not comfortable with the prices because of wider swings (C. Goga, personal communication, January 22, 2016).

The contribution of HFT to the level of volatility in the market has really hurt blocks. HFT has lowered managers and traders trust and confidence in the marketplace. If they are not confident and do not trust the price on the screen, traders aren’t going to put in orders for large blocks of stock unless they can cross it. This is where the institutional sales trader can still provide utility, by crossing stock, but even at a firm like Jones, crosses only account for an average of 30% of their trades, and that’s the highest in the industry. For a further illustration of the effects of Volatility on the block trade see Figure 5 (See Appendix E)

5. So is the buy-side craving more information than usual because of this?

I think people are under the impression they are getting less [Information] because of wild volatility and a lot of volume on the tape that’s unexplained, that they can’t point to who’s doing what, and where. So I think people are under the impression that they have a lot less knowledge regarding price action in the markets, and what’s really going on, and what the real markets are (C. Goga, personal communication, January 22, 2016).

6. So that’s because of things like Dark pools and anonymous type trading things. They don’t know where the liquidity may or may not be?

Yes
7. Anything on the horizon, as an analyst, maybe regulation wise, or anything that could help or hurt block trading?

   I think if they reign in a lot of the High frequency guys that are basically moving things around violently and spoofing and doing other things, that will help to some degree. Otherwise we just need more transparency in the markets and I’m not sure that’s anytime soon on the horizon, there really hasn’t, as far as I know to solve these problems.

   I think the biggest thing is the volatility because of so many alternative trading systems and so much fragmentation in the market. That to me is the number one thing that hurts, you just don’t know where; where to go and where everyone is. The chances of meeting if there are two highways are much better than if you have twenty-seven (C. Goga, personal communication, January 22, 2016.)

Howard Mann, Institutional Sales Trader, JonesTrading:

   Howard Mann has been working at JonesTrading Dallas for 15 years, since 2001. My conversation with Mr. Mann was brief and chiefly yielded a good explanation of the trade-through rule of Reg NMS and other self-explanatory answers about Jones and the industry.

   1. How did Reg NMS affect the block?

      Reg NMS, I don’t think it negatively affected our ability to trade blocks. I think it actually was a benefit to the sellers. You had to satisfy the book, if you want to trade a block at four dollars and its bid out loud at four ten and there’s 65 thousand shares bid between 4 and 4.10, your selling 900 thousand and you fill the book, your client will get 65 thousand shares above the print price, and the balance is at the print price (H. Mann, personal communication, January 22, 2016.)
Explained here is the trade-through rule which is a part of Reg NMS. The trade-through rule makes a trader “satisfy the book”, even when doing a deal upstairs. In this example, Mr. Mann explains it as such….

Say your client has given you a sell order:

ACE Seller of 900k @ $4.00. The current highest bid in the market is $4.10. Suddenly, you find another client who gives you a buy order: $4.00 Buyer of 900k shares ACE. Under Reg NMS before you execute this trade, and make commission on these 1.8 million shares, you have to consult the book. In order to print [trade] the block at $4.00, you have to satisfy the book for that security. The book is a list of all the bids and offers out in the market. For ACE, it shows there are a total of 65k shares bid for at different prices between $4.10 and $4.00. To satisfy the book on this trade and transact the block at $4.00, the buyer would have to purchase the exact number of shares that would’ve been available to the seller at each price in the market place. So 65k shares will be traded between $4.10 and $4.00, to satisfy the book, and the remaining 835k @ $4.00. This would be the case if we were dealing with an illiquid security. For a highly liquid security, the book between 4.10-4.00 could be millions of shares. This is another reason why NMS hurt institutional sales traders; there was no point for clients to call them to trade these highly liquid names any more, you’d never make it through the book.

2. Jones is one of the only firms in the country that focuses solely on big block trades, institutional sales trading, what makes you so successful?

Relationships and Trust. When you start talking about that kind of size there has to be a lot of trust. You want to get out of something small [illiquid]? Call Jones and they will find you buyers.
3. So you think firms are going to continue to outsource their big block trades. Traders are going to continue to call people like Jones?"

*Well with technology and evolution things are always going to change. For 15 years there’s been Algos [Algorithms], Liquidnet, Instinet, some of the big houses have tried to make automated systems, crossfinder and things like that where blocks would trade and they haven’t negatively affected us. There’s always going to be a better idea and a better way, but right now its kind of come back to us. We’re goanna ride it out and hope the human touch is still it.*

4. How has algorithmic trading affected how you do your job?

*I think the algorithms have aided me, I mean they help us too. I use them, they’re great ways to trade. You want to source as many different platforms as you can to find liquidity. The last thing you want to do is have a [market] impact, you want to look at the screen and trade your stock and have it not change it at all (H. Mann, personal communication, January 22, 2016.)*

**Shawn Blakeslee, Senior Partner, Institutional Sales trader, Cantor-Fitzgerald:**

Mr. Blakeslee began his career at Cantor in 1986. After interviewing all those that I did at JonesTrading I felt it was important to get the answers of a trader at a much larger and broadly based firm. Having so many years of experience in the industry, my conversation with Mr. Blakeslee centered on the evolution and outlook for the institutional sales trader. Due to the nature of my email interview with Mr. Blakeslee and the nature of his responses, they have been presented in question-answer format, with analysis and explanation of key points as well.
1. Would you agree that because of their ability to evolve and continue to provide best block execution institutional Sales Traders have survived while all the other pure "order takers" or execution experts have gone nearly extinct, and moved to offer a consolidation of services, or went to work in house/upstairs?"

   We’ve survived, but increasingly where we are needed is in the secondary and tertiary stocks. Often, these stocks “trade by appointment”, and holders of the stock are often found in places where the traditional dark pools and brokerage firms can’t reach. If an institution has a million shares of Pfizer for sale, they can easily sell it the more traditional venues and dark pools without significantly impacting the stock’s price. However, many of the smaller cap stocks are held by corporate insiders, family and friends, and small and mid-cap managers that are less transparent and accessible. Often their stock is held at smaller trust banks or obscure money managers which aren’t particularly active. Often these shares might have restrictions (Rule 144, etc.) which require extra legwork to trade. That’s where a Cantor or Jones can shine. We work hard to trade the crumbs that fall between the cracks. We run more efficiently and can be profitable even without the blocks of low hanging fruit (million share blocks of Pfizer, etc.) being accessible (S. Blakeslee, personal communication, February 15, 2016).

   Over the years the institutional sales trader has survived, but are more so needed where they provided the most utility: in highly illiquid securities. If a client/institution wants to trade a block of a highly liquid security, technology has made it so they can do that themselves and will
not send the order to the institutional sales trader nearly as much. However, due to the nature of many of the smaller securities to be illiquid and their markets hard to access, the institutional sales trader still gets business from these. Even without as many of the big trades in the big names, firms can still run efficiently enough to be profitable, for now.

2. Your outlook and why for the block and sales trader?

   Developing technologies are wringing new efficiencies in the markets, and various algos are incredibly efficient at mimicking human logic and quickly taking or hitting a stock. However, they still require monitoring by a human being. Additionally, there are applications where algos ARE NOT the best way to buy or sell a block, either because of illiquidity, wide spreads, or accessing the right venue to trade something. So far, anyway, the customers still rely on me, though admittedly most of the time it’s on those “hair-on-fire” days when they need extra pairs of eyes and hands to help work the orders on their blotter. For my biggest customers, I’m one of their go-to guys on those busy days, or when they’re looking for information on a company that isn’t easily acquired. There is still a need to have a sales trader weed out the relevant news, the reliable rumors, and dig deep for obscure reasons why a stock might be up or down. I see it in our bond trading, too; customers still want to be serviced (S. Blakeslee, personal communication, February 15, 2016).

The high-touch model of service provided by the institutional sales trader is still valued by many institutions. Trust is hard to establish and come by, especially with the markets how they are today. Customers still trust and send business to the institutional sales trader because of the massive about of distrustful things occurring in the markets. Mr. Blakeslee admits that a
good amount of the business received will be on busy days when clients need help getting things done, but its business nonetheless. The sales traders still provide utility to their clients and they have continued to survive because of it.

3. The fate of the purely execution based niche firm like Jones? Is it different than the guys working for bigger firms like cantor?

Conventional wisdom is that a firm needs to be full-service and provide Investment Banking and Research. While this can certainly help get paid, there are still some customers that have free commissions to pay for best execution. This term is becoming more marginalized with algos but I still see where I can game and be better than the algos on a consistent basis. My customers see it and still keep me around.

4. Anything else you’d like to add concerning the sales trader and the block?

Kind of like self-driving cars, algos and automation are good at handling tactical decision making but the skilled block trader is still king when it comes to strategic thinking. With self-driving cars, one of the biggest hurdles they’ve encountered is the computer’s inability to cope with all the variables attendant with merging into traffic, be it at a Yield sign or freeway onramp. That’s a good metaphor for the tussle going on between the algos and me. If all you’re trying to do is track the market, then putting an algo in VWAP mode (Volume Weighted Average Price), TWAP (Time-Weighted Average Price), or POV (% of Volume) all work fine. But even then, things can happen and a high-touch trader must still monitor the order. When there is news out and a stock is in a fast market, or there is news, or the stock needs to be traded against options, futures, or some sort of arbitrage, the human is better (S. Blakeslee, personal communication,
Man still beats machine when it comes to sourcing liquidity and providing best execution for block trades. The machine may be able to think faster than man but it cannot outthink or outperform man when it comes to complex situations.

5. On his career at Cantor-Fitzgerald:

We’ve had a lot of fun, gotten into a lot of trouble, and are still going. In the past few years a lot of guys have seen their business fall way off, and we often feel like a dying breed. Still, for now at least, I still have a job and am making enough money that I feel that I’m still compensated for having to wake up at 3:00am, and the toll that takes on my body (S. Blakeslee, personal communication, February 15, 2016).

BEYOND THE WORDS

There was much reading between the lines to be done in the research conducted. This is not to say that what the subjects said was not truthful or honest, but only that it need be looked at in the correct lighting. What spurred this analysis of the results beyond the words was something that occurred during my last round of interviews with JonesTrading. While seeking advice from a well experienced trader at JonesTrading he/she told me something that truly pivoted the viewpoint of this paper. This person has wished to remain off the record in saying, “If you’re looking for a job this is a great place to work, but if you were my own son I would tell you to look elsewhere. I’m not sure how long we are going to be around for.” Suddenly I saw all the research I’d conducted in a whole new light.

Those couple of sentences were key to my analysis of the research. I realized that I
myself was biased; I liked block trading, I wanted it to thrive, but that is not why we’re here.

Taking a step back I analyzed the research from the middle of the aisle. Mr. Jones was an excellent resource; incredibly well-respected in the industry. His making time in his busy schedule to meet was much appreciated. However, could I realistically expect the CEO of a company that is purely involved in institutional and block trading to say anything against it? The affects of that on company moral would be devastating. Could the traders of Jones really be expected to remain unbiased? An indictment of their way of life could show complete lack of faith to the ownership and clients if revealed. Suddenly, red flags were popping up everywhere. It seems that in reality you don’t always get the right answer when asking the right question.

The traders I had interviewed thus far were happy to comment on the effect of events past on the block. Nevertheless, when it came to forecasting the future they either provided vague answers or did not answer at all. In the interest of the professionalism and respect that this report is being conducted refrain will be taken in pointing out specific examples. This development is part of what led me to seek out an interview with Mr. Blakeslee. As a senior partner in a large and well-established company, his testimony was free of the restraint and bias encountered previously. This did not mean that the previous research that had been conducted for this report had become useless, but rather made it more useful. So in hindsight, maybe Mr. Jones was right, maybe we did get the right answers after all.

**CHIEF TAKEAWAYS**

**Regulations Miss the Mark:**

Regulations in the securities markets over the past couple decades have certainly not helped the block trade. The problem being that they have not done what they were supposed to
do. Regulations ATS and NMS, as predicted, are the chief subjects that traders are talking about. The effects they have had and are having on the block trade are indirect, but they are still there. These regulations led to the fragmentation of the markets, decreased transparency, and increased volatility, none of which has supported the block trade.

Tom Carter was clearly the most knowledgeable on the subject while the others seemed to know some as well. From what he and others said, several things were clear about the future of Regulations and Block. Unless a major change occurs in the way regulations are drafted, they will continue to miss the mark. Regulations will never directly affect the block one way or the other. But they will continue to affect it indirectly. These indirect affects will most likely continue to be negative, or at best, not positive for the block. Unfortunately, not even some traders realize the indirect affects regulations have had on the block. If you can’t point out the cause of something, how can you ever hope to fix it?

**High Frequency Frequently Hurting:**

High Frequency Trading is adding a lot to the woes of the block and those trading it. Their style of trading has contributed to the high levels of fragmentation in the market today. HFT has created trust and confidence issues and managers aren’t comfortable putting in those big orders for blocks anymore. Yes, there is possibly some regulation coming for HFT’s but it will not be gone completely. The volatility they create will never reduce, it will only increase as things are only going to get faster and faster as time moves on. The block is going to continue to suffer immensely from the actions of HFT. This suffering maybe reduced if regulation is implemented successfully, but the odds of that occurring anytime soon while also being successful are very low. In the mean time, the need for speed will continue and volatility will remain. The block and therefore the institutional sales trader are going to continue to hurt
because of it.

**Human Touch is Still King:**

As Mr. Jones (personal communication, December 22, 2016) said, “The most important thing to the institutional trader is liquidity, the 2nd most is information.” The need for both of these factors combined is a large part of what has kept humans in the game. In Figure 6, Woodbine Associates (2015) ranked 43 brokers based on their ability to source natural liquidity, JonesTrading was #1 (see Appendix F). The lack of transparency in the markets for small and mid-cap stocks has institutional managers and traders craving more information and liquidity. Although, as Mr. Blakeslee (personal communication, February 15, 2016) mentioned, it is increasing only in those types of securities that clients are contacting the institutional sales trader. This has led firms like Jones to thrive during this time because they specialize in the hard to trade names. What must be realized though is that technology has made it so the clients are no longer sending large orders of the large securities because information and liquidity has become so readily available. Trading systems have made it cheaper for the clients to take care of these large trades in-house. So when we say the Human touch is still king, it is only so in a small area; a niche.

**CONCLUSION**

The high-touch relationship based model of the institutional sales trader is still attractive to buy-side managers and traders. Although it is increasingly when it comes to the illiquid names they are still picking up the phone and calling people like Tom Carter at Jones, or Shawn Blakeslee at Cantor. The ability of the sales trader to evolve and adapt allows them to continue to operate efficiently and profitably. There has been a decent reduction in the overall quantity of
institutional sales traders but firms like JonesTrading have thrived during this time because they do their job so well. Over the next decade the outlook is great for the institutional sales trader. Their transaction oriented nature gives them much less market risk than those on the buy-side. However, in the thorough analysis conducted in this paper, the long term is not as friendly.

“We often feel like a dying breed”, Mr. Blakeslee (personal communication, February 15, 2016) said in his interview. The reason for this is because the institutional sales trader is a dying breed. Regulations are going to continue to miss the mark, which may not hurt the block, but will certainly not help it. High Frequency Traders are not going anywhere. Regulation may be passed to limit them but the “Need for Speed” is on, and no one is hitting the brakes. These two factors will continue to add to the fragmentation and lack of transparency in the markets. Investor confidence in prices will continue to go down as a result. Afraid to get hurt by what they can’t see, Institutional Managers and Traders will no longer want to stand up at a given price and put in block orders. The market factors causing the block to suffer will only intensify.

Regulations and High Frequency Traders are not the only reason for this downward trend. The fourth market in which institutional traders directly trade with each other, cutting out the sales trader, will continue to grow. This will result from the continued growth and advances of technology. There will be no slowing down the innovation of the markets. As we continue to progress, information will become more widely available and markets more easily accessible. The markets will always move towards efficiency, the supply chain will shrink, and the institutional sales trader will be slowly cut out.

The evolution of the sales trader as a pure execution specialist will reach the end of it’s track. Doing their job well and respecting people will not be enough to do business with them anymore. As Mr. Jones (personal communication, December 22, 2015) said, “Anyone who is
successful will adapt and move on.” Unfortunately, this will mean moving on from what they have known for half a century. To stay successful, the consolidation of services will be key for the institutional sales trader. Whoever does it best will be among the last few firms standing and just might continue to thrive because of that. Right now that firm would be JonesTrading. As for everyone else, in the next 10-20 years the institutional sales trader, and therefore the sales trader will be highly endangered, and all but extinct. The block will still be around however, trading either in the fourth market or through an automated crossing system. The block will continue to be a great tool for institutional managers and traders. The disappearance of the block will in the end not be the crushing blow for the sales trader. The sales trader will disappear because of one of the most unstoppable forces of human behavior.

**Death** of a Sales Trader

**Cause of Death:**

*Block Trading*

**PROGRESS**
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APPENDIX A: 2004-14 AVERAGE TRADE SIZE ON vs. OFF EXCHANGE

**APPENDIX D: TABB GROUP BEST IN BLOCKS SURVEY 2015**

![Image](image.png)

APPENDIX E: THE EFFECTS OF VOLATILITY ON LARGE BLOCK TRADES

Exhibit 5
VIX vs. % Blocks Over 100,000 Shares

Figure 5. The effects of Volatility on Large Block Trades. Reprinted from *Truing the Block: A Framework for Re-architecting the Trader’s Toolkit*, by L. Tabb, V. Bogard, 2014. Copyright 2014 by The TABB Group, LLC. Reprinted with Permission.
Figure 6. Top 43 Brokers When it Comes to Sourcing Natural Liquidity. Reprinted from *Independent Survey of Equity Execution Services*, by Woodbine Associates, Inc.