# Equity Trading Practices


## Equity Trading

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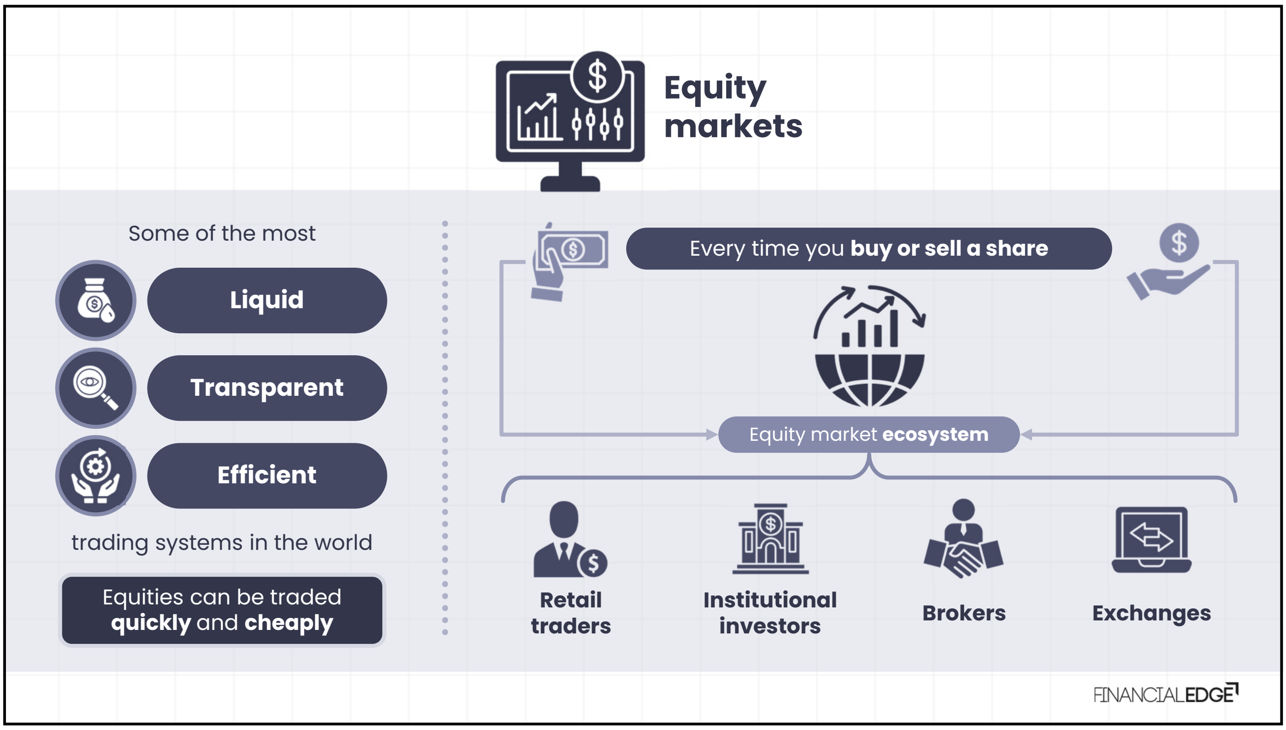
Equity markets
Some of the most
Liquid
Transparent
Efficient
trading systems in the world
Equities can be traded quickly and cheaply
Every time you buy or sell a share
Equity market ecosystem
Retail traders
Institutional investors
Brokers
Exchanges
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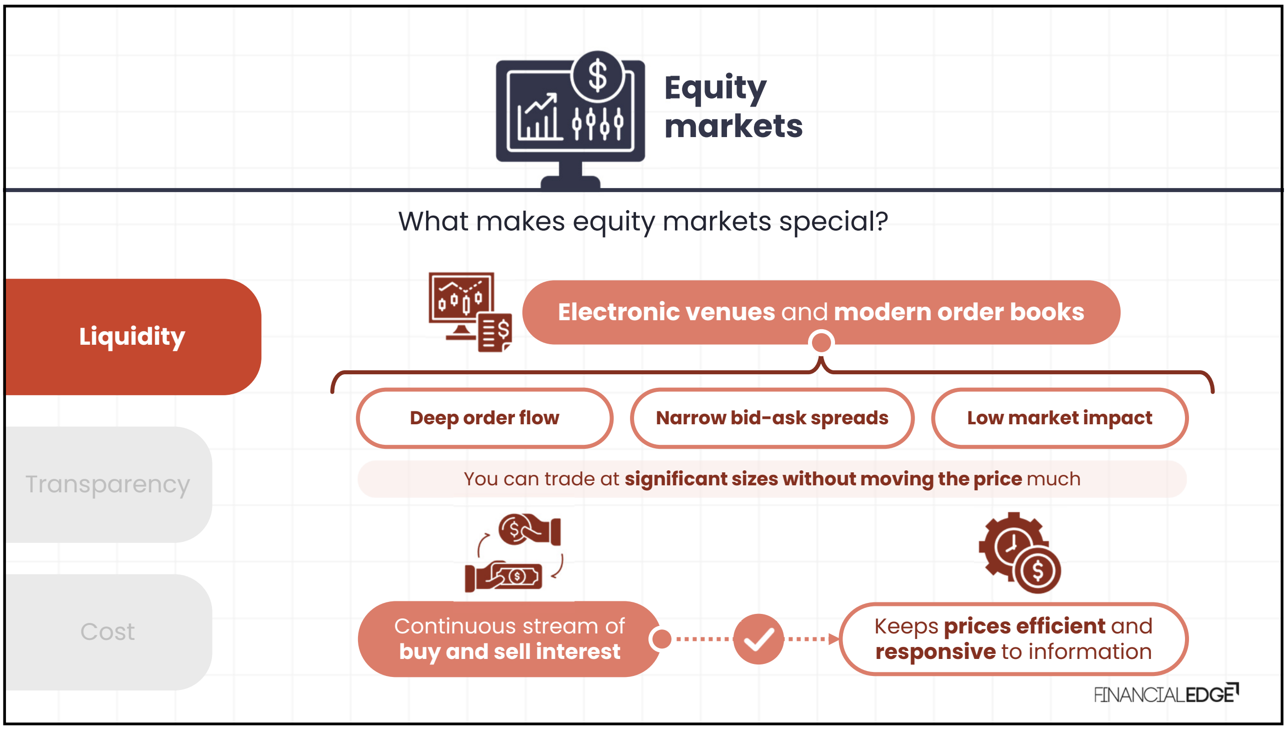
Equity markets
What makes equity markets special?
Liquidity
Transparency
Cost
Electronic venues and modern order books
Deep order flow
Narrow bid-ask spreads
Low market impact
You can trade at significant sizes without moving the price much
Continuous stream of buy and sell interest
Keeps prices efficient and responsive to information
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## Equity markets

What makes equity markets special?

Liquidity

**Transparency**

Cost

**Public markets mandate pre- and post-trade transparency**

| Published in real time | Exceptions |
|---|---|
| Quotes | Dark pools |
| Trades | Temporary trading halts |
| Official prices | |

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## Equity markets

What makes equity markets special?

Liquidity

**Transparency**

Cost

**Exchanges run under clearly defined rulebooks**

- **When** trading occurs
- **How** trading occurs

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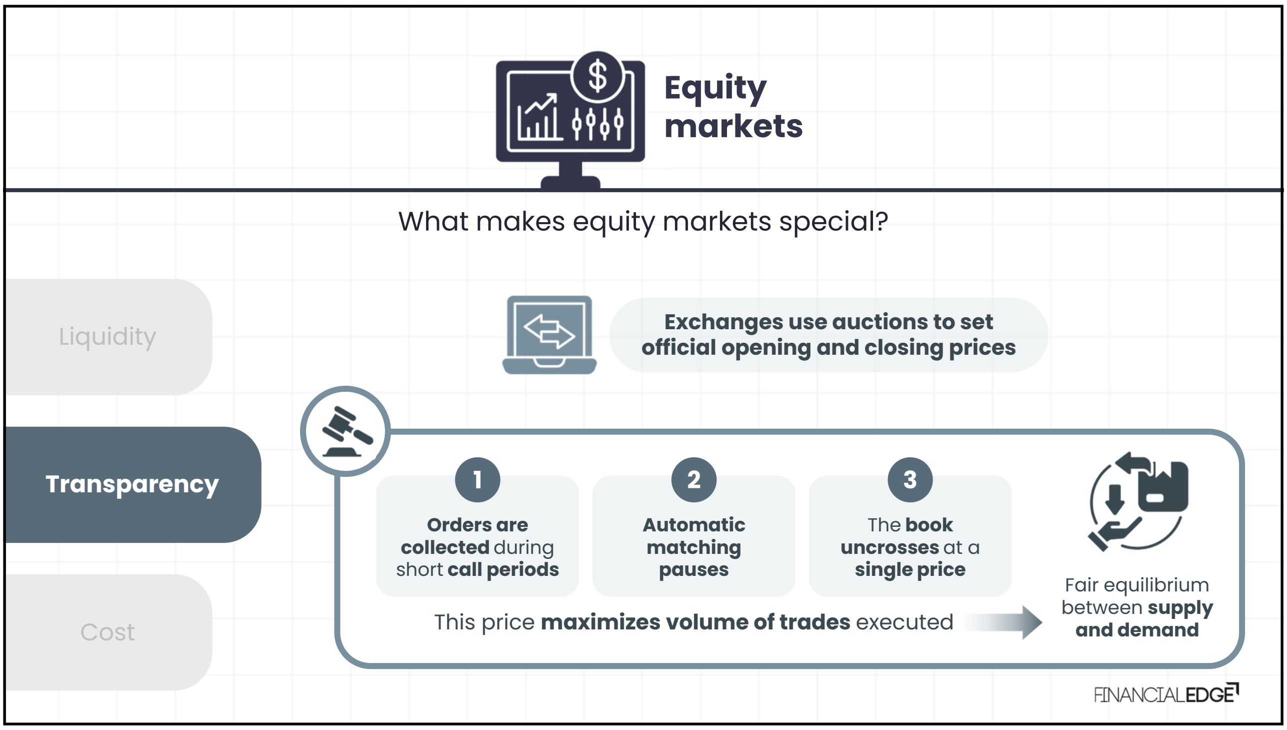
Equity markets
What makes equity markets special?
Liquidity
Transparency
Cost
Exchanges use auctions to set official opening and closing prices
1 Orders are collected during short call periods
2 Automatic matching pauses
3 The book uncrosses at a single price
This price maximizes volume of trades executed
Fair equilibrium between supply and demand
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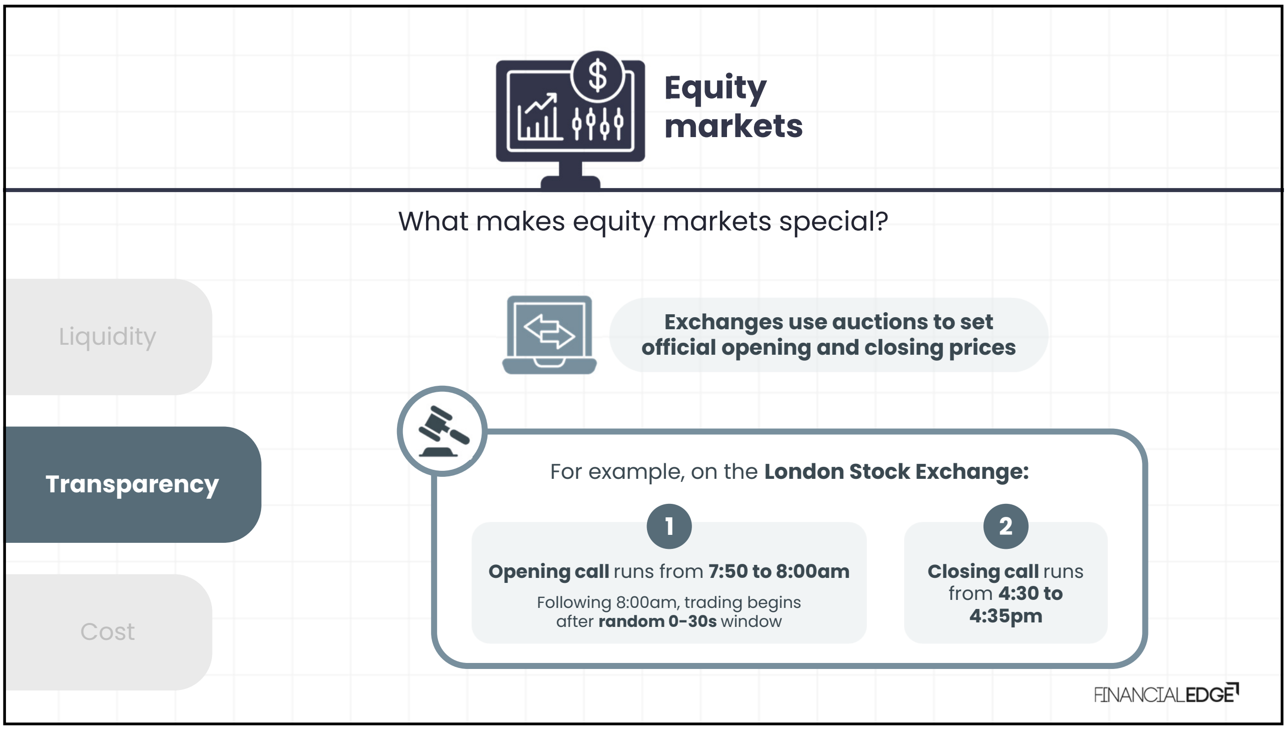
Equity markets
What makes equity markets special?
Liquidity
Transparency
Cost
Exchanges use auctions to set official opening and closing prices
For example, on the London Stock Exchange:
1 Opening call runs from 7:50 to 8:00am
Following 8:00am, trading begins after random 0-30s window
2 Closing call runs from 4:30 to 4:35pm
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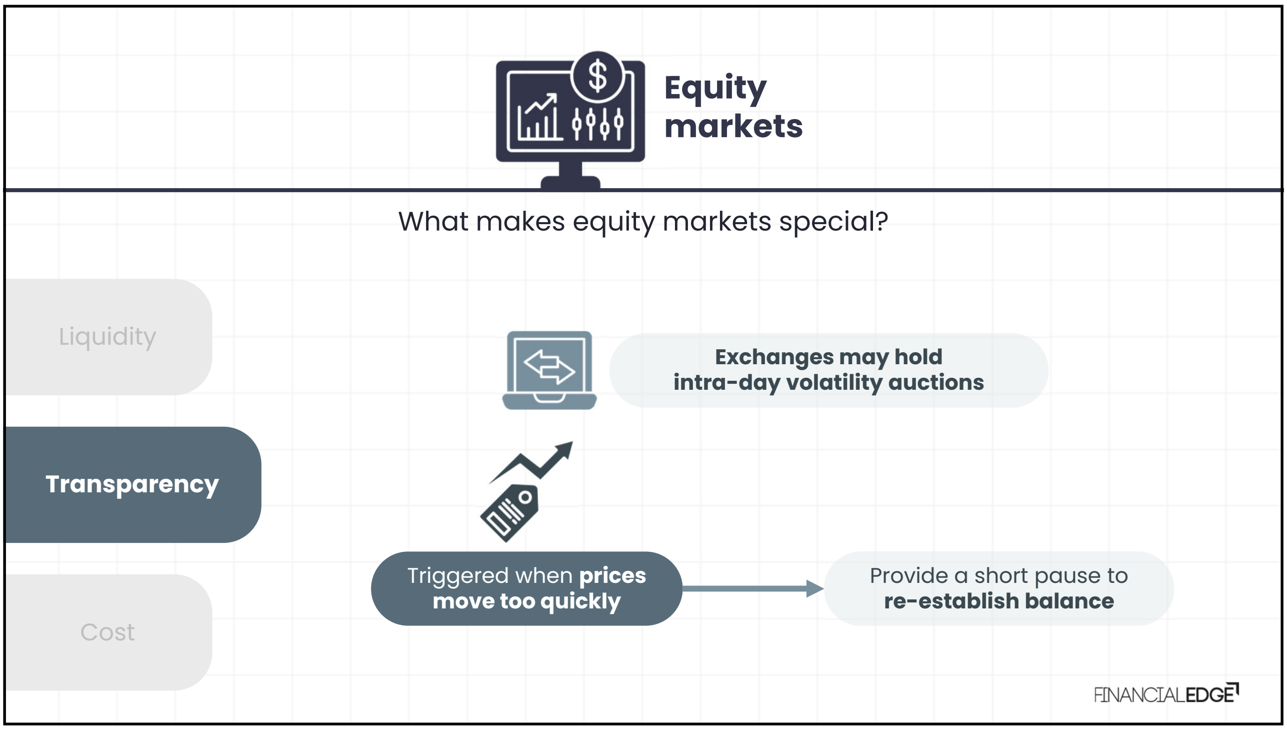
Equity markets
What makes equity markets special?
Liquidity
Transparency
Cost
Exchanges may hold intra-day volatility auctions
Triggered when prices move too quickly
Provide a short pause to re-establish balance
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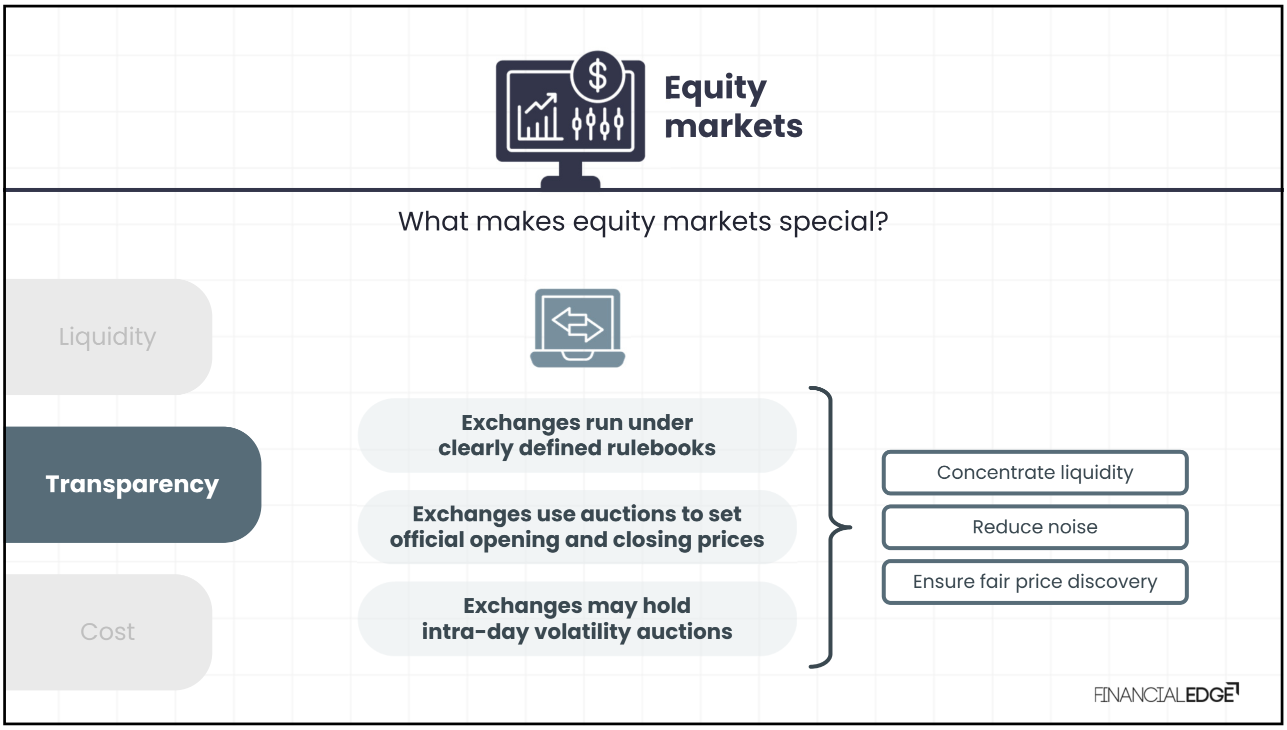
Equity markets
What makes equity markets special?
Liquidity
Transparency
Cost
Exchanges run under clearly defined rulebooks
Exchanges use auctions to set official opening and closing prices
Exchanges may hold intra-day volatility auctions
Concentrate liquidity
Reduce noise
Ensure fair price discovery
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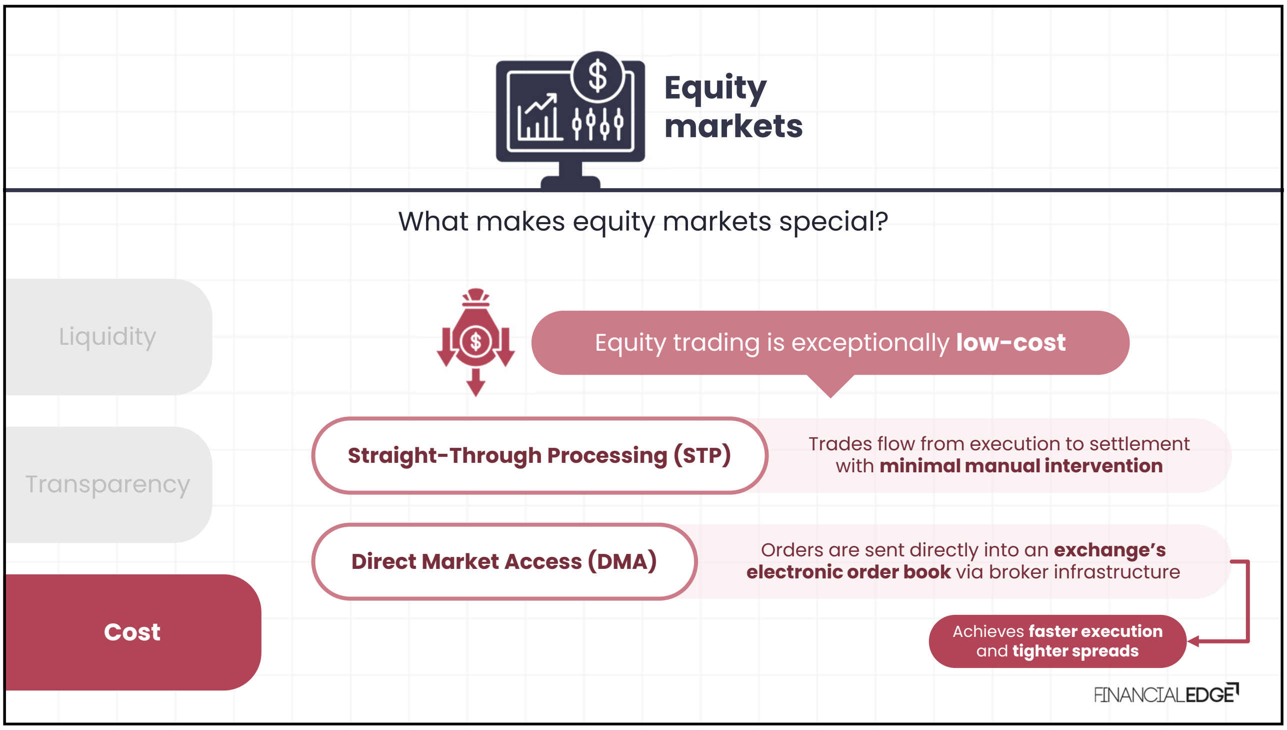
Equity markets
What makes equity markets special?
Liquidity
Transparency
Cost
Equity trading is exceptionally low-cost
Straight-Through Processing (STP)
Trades flow from execution to settlement with minimal manual intervention
Direct Market Access (DMA)
Orders are sent directly into an exchange's electronic order book via broker infrastructure
Achieves faster execution and tighter spreads
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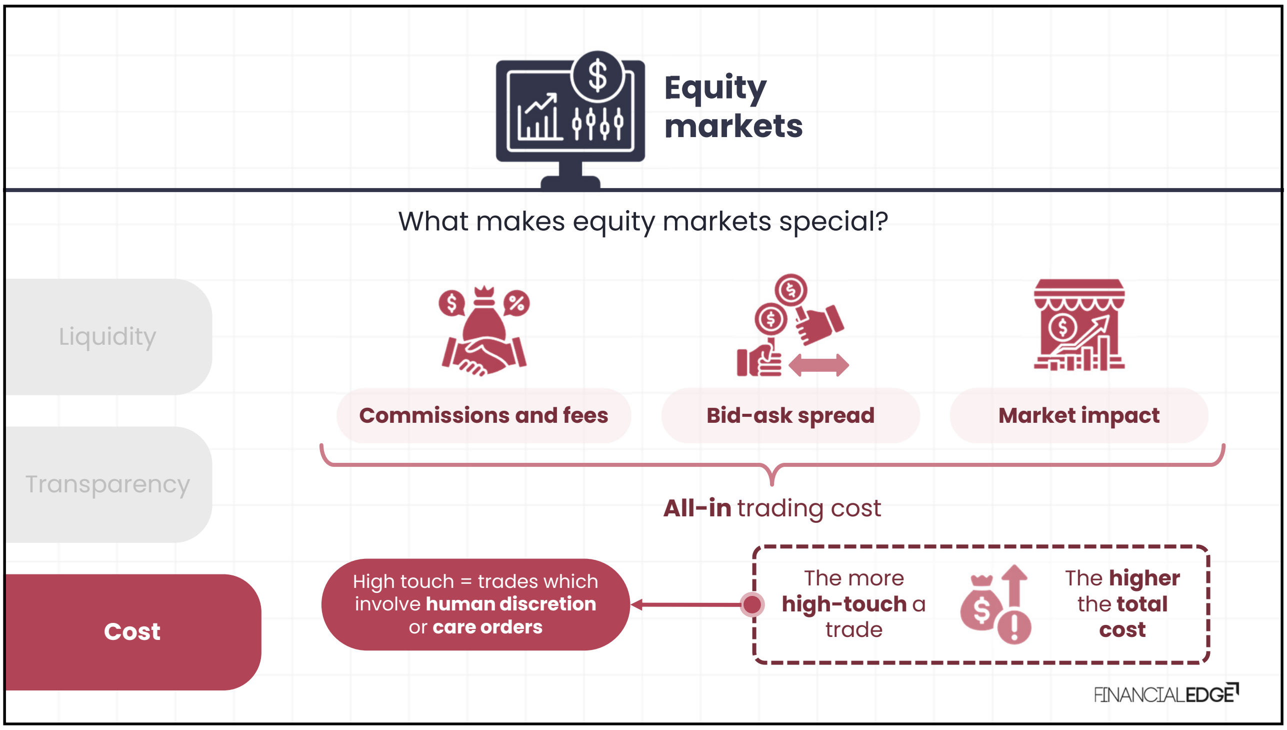
Equity markets
What makes equity markets special?
Liquidity
Transparency
Cost
Commissions and fees
Bid-ask spread
Market impact
All-in trading cost
High touch = trades which involve human discretion or care orders
The more high-touch a trade
The higher the total cost
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# Equity Order Types

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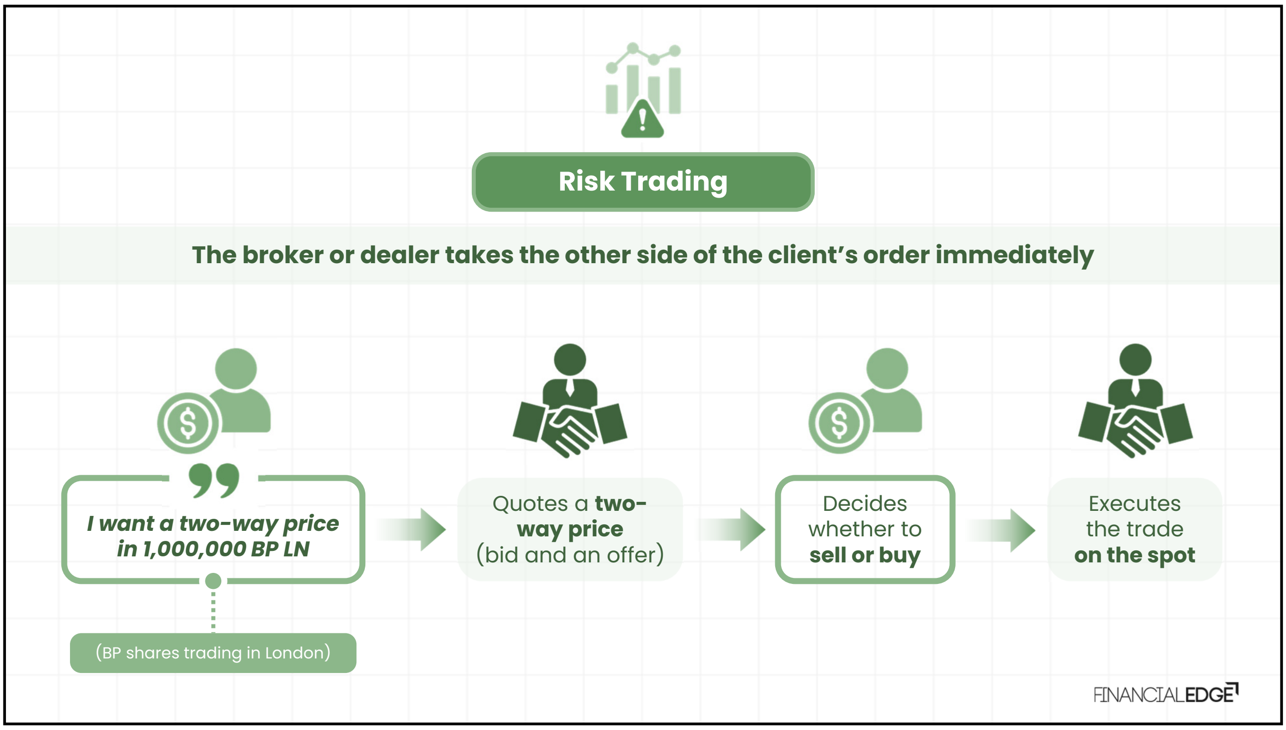

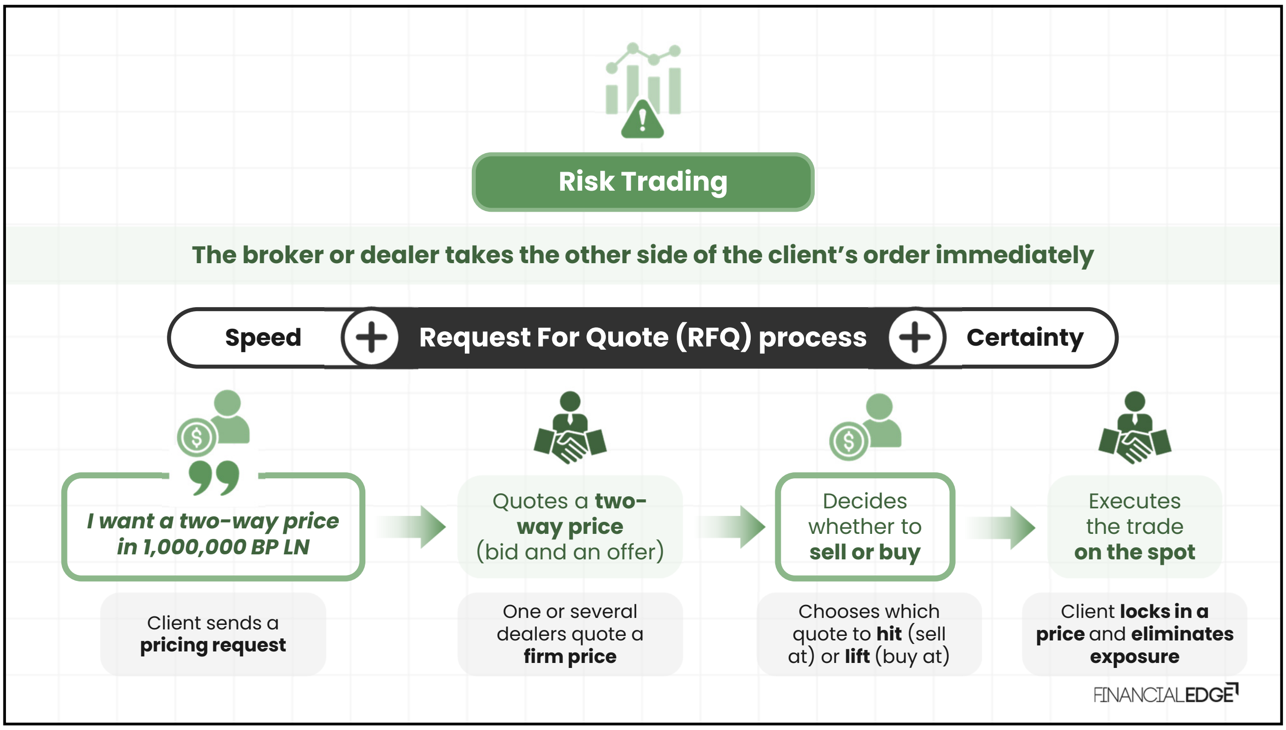
Risk Trading
The broker or dealer takes the other side of the client's order immediately
Speed
Request For Quote (RFQ) process
Certainty
I want a two-way price in 1,000,000 BP LN
Client sends a pricing request
Quotes a two-way price (bid and an offer)
One or several dealers quote a firm price
Decides whether to sell or buy
Chooses which quote to hit (sell at) or lift (buy at)
Executes the trade on the spot
Client locks in a price and eliminates exposure
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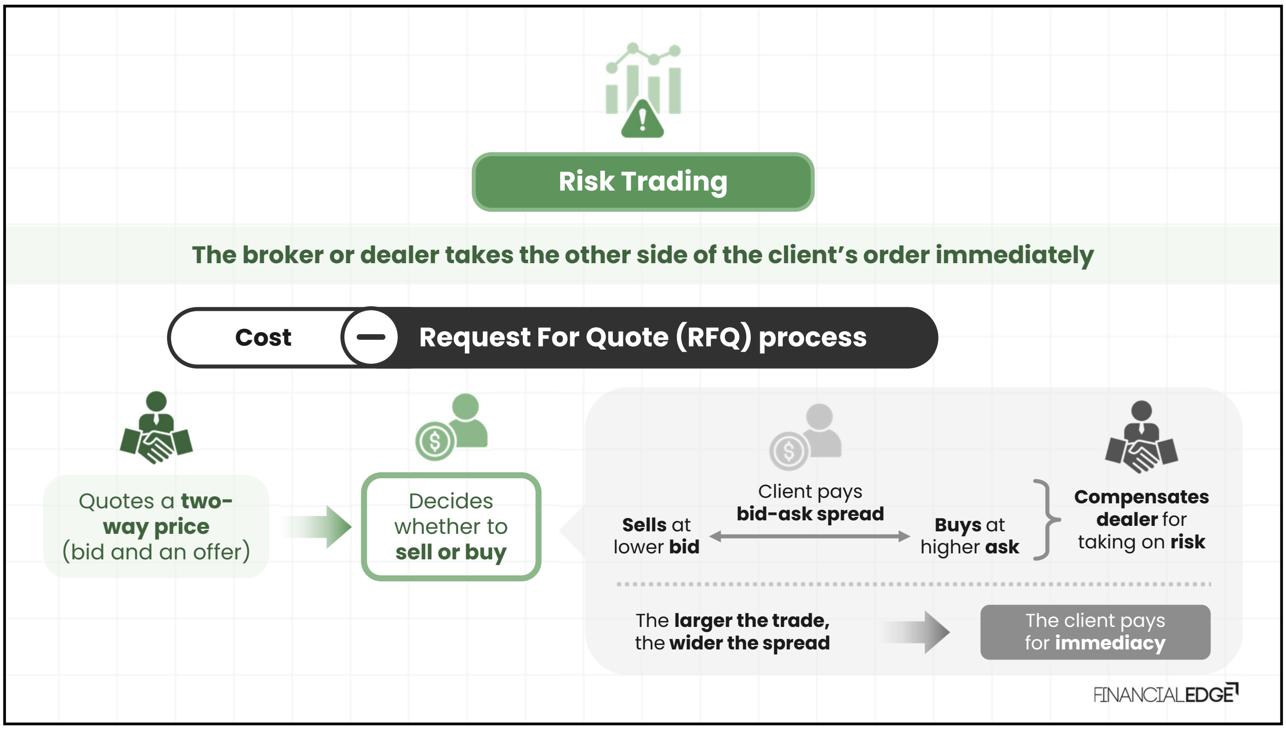
Risk Trading
The broker or dealer takes the other side of the client's order immediately
Cost
Request For Quote (RFQ) process
Quotes a two-way price (bid and an offer)
Decides whether to sell or buy
Client pays bid-ask spread
Sells at lower bid
Buys at higher ask
Compensates dealer for taking on risk
The larger the trade, the wider the spread
The client pays for immediacy
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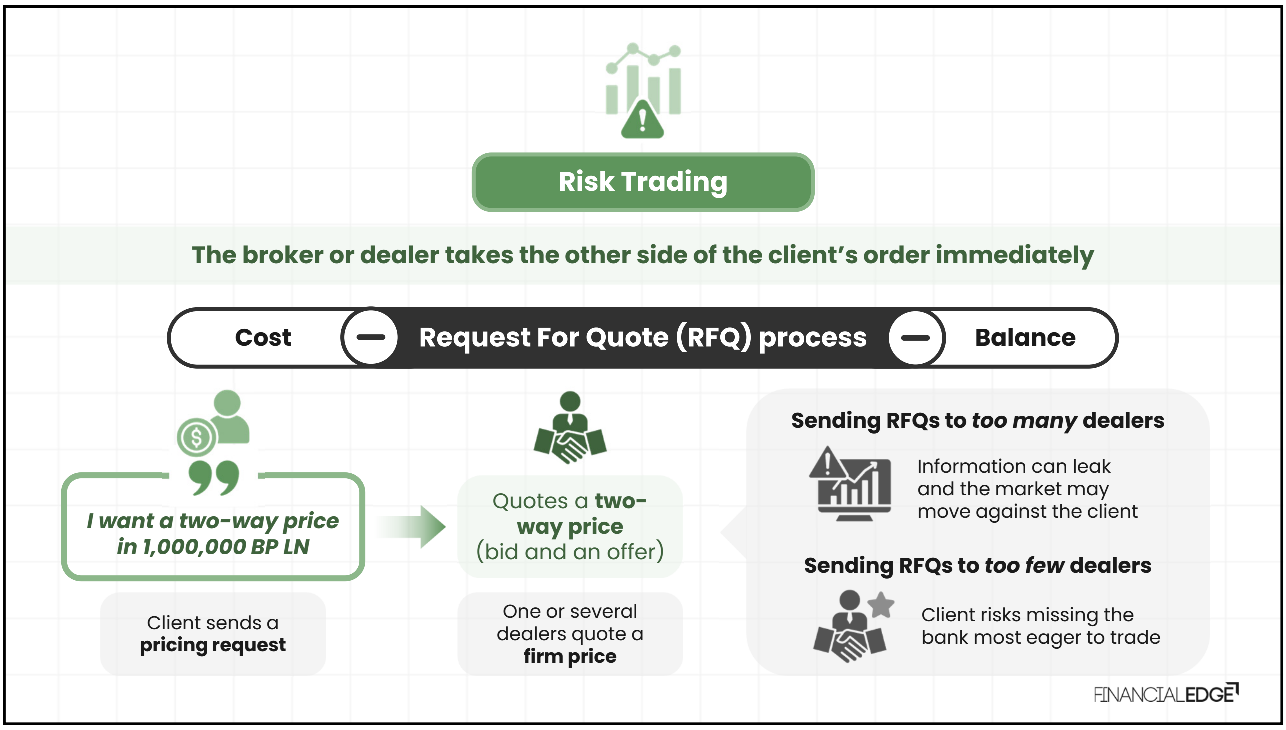
Risk Trading
The broker or dealer takes the other side of the client's order immediately
Cost
Request For Quote (RFQ) process
Balance
I want a two-way price in 1,000,000 BP LN
Client sends a pricing request
Quotes a two-way price (bid and an offer)
One or several dealers quote a firm price
Sending RFQs to too many dealers
Information can leak and the market may move against the client
Sending RFQs to too few dealers
Client risks missing the bank most eager to trade
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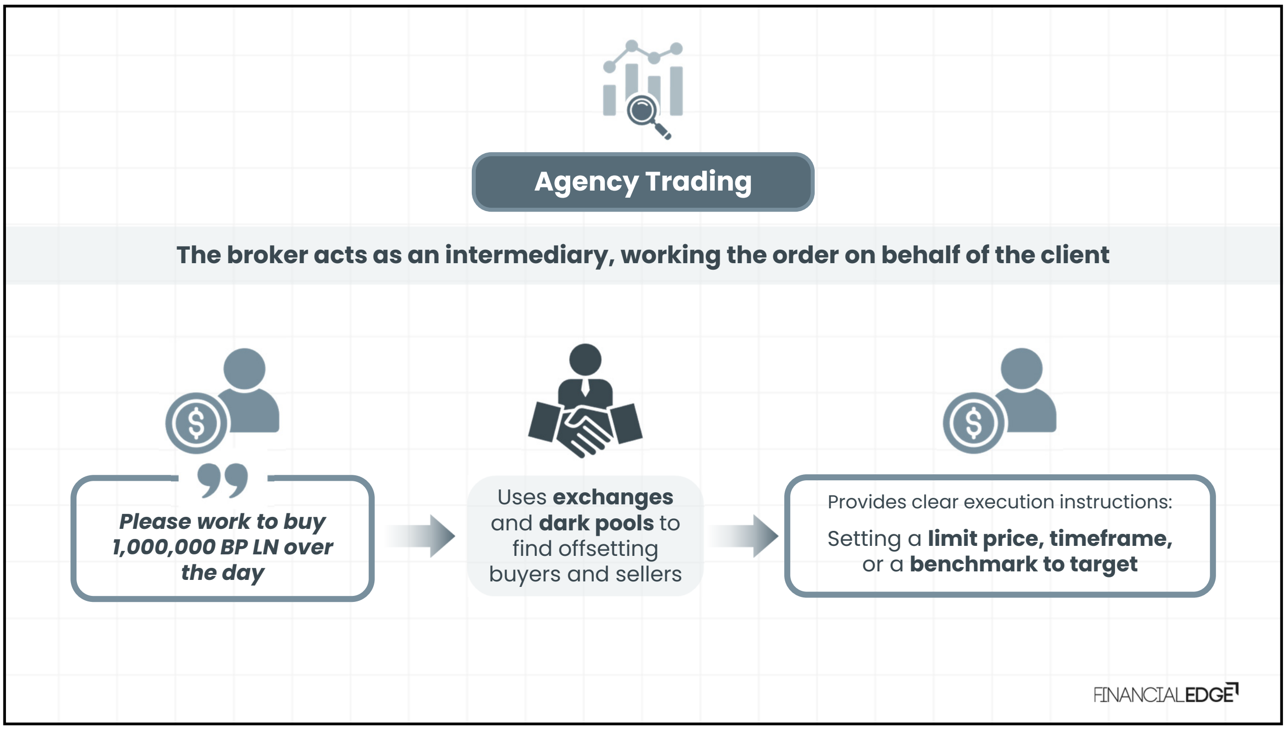
Agency Trading
The broker acts as an intermediary, working the order on behalf of the client
Please work to buy 1,000,000 BP LN over the day
Uses exchanges and dark pools to find offsetting buyers and sellers
Provides clear execution instructions:
Setting a limit price, timeframe, or a benchmark to target
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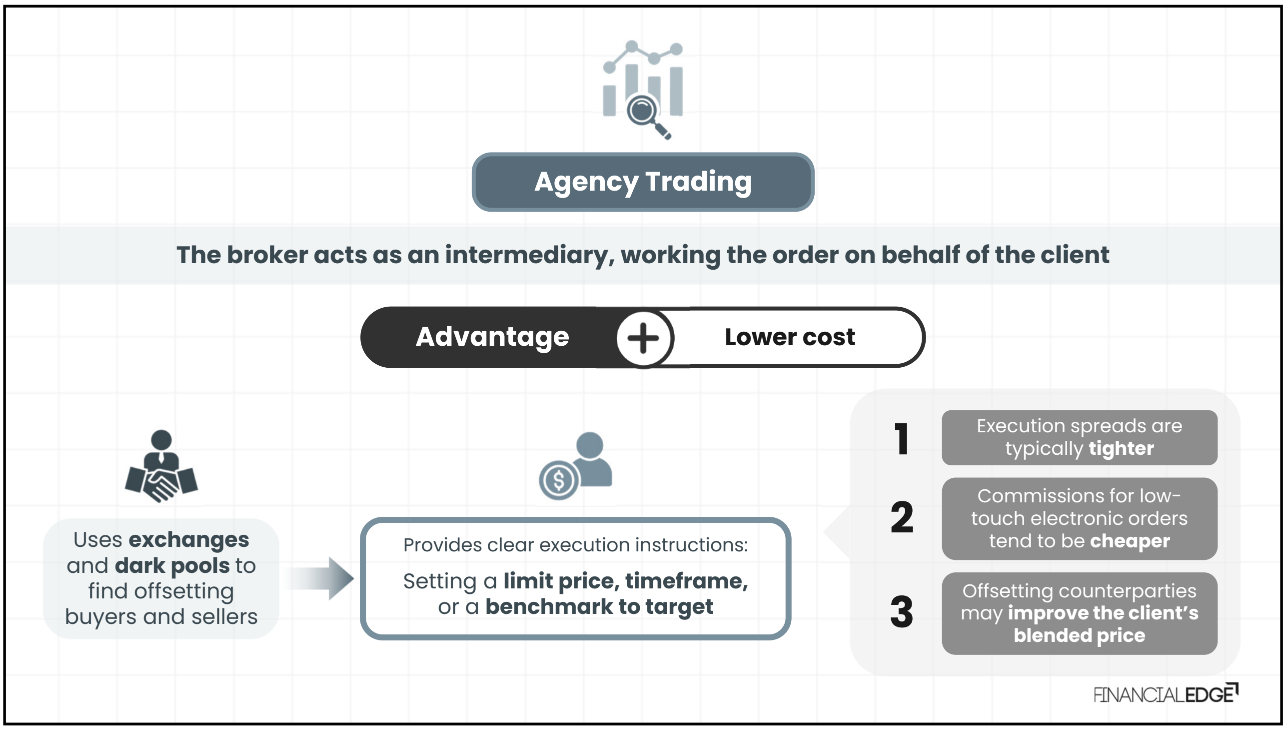
Agency Trading
The broker acts as an intermediary, working the order on behalf of the client
Advantage
Lower cost
Uses exchanges and dark pools to find offsetting buyers and sellers
Provides clear execution instructions:
Setting a limit price, timeframe, or a benchmark to target
1
Execution spreads are typically tighter
2
Commissions for low-touch electronic orders tend to be cheaper
3
Offsetting counterparties may improve the client's blended price
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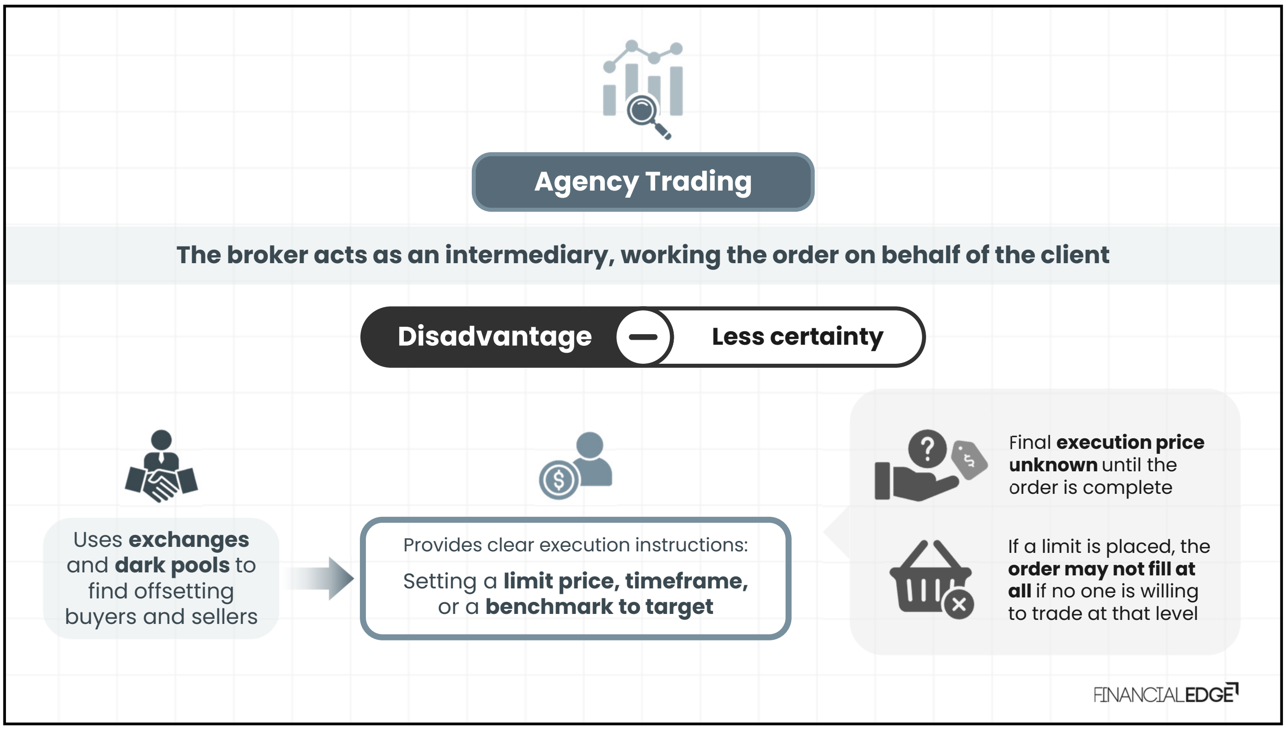
Agency Trading
The broker acts as an intermediary, working the order on behalf of the client
Disadvantage
Less certainty
Uses exchanges and dark pools to find offsetting buyers and sellers
Provides clear execution instructions:
Setting a limit price, timeframe, or a benchmark to target
Final execution price unknown until the order is complete
If a limit is placed, the order may not fill at all if no one is willing to trade at that level
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# Equity Order Book

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## How equity trades are executed

**How orders reach the market** ◀ It depends on ▶ **How prices form through buyer-seller interaction**

### **Off-book risk** trading

Investor trades through brokers or dealers who **take risk** and **quote prices directly**

↳ **Negotiated bilaterally** between the two parties

### **Electronic order-book** trading

Investor **sends their orders electronically** into the market

↳ Orders are **matched automatically** against other participants through the **order book**

**Order-book:** the real-time system that **pairs buyers and sellers**, and is **visible to exchange members**

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## **Electronic order-book** trading

The order book lists **all current limit orders** to **buy and sell a stock**

**Each order shows a:**

**Price** & **Size**

Traders can see the **full depth of the market**

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## **Electronic order-book** trading

Top line = inside market, or **'touch price'**
Difference between them is the **bid-ask spread**

| Bid side | | Offer (ask) side | |
|---|---|---|---|
| **13000** | **182.8** | **183.1** | **1450** |
| 8800 | 182.8 | 183.1 | 1450 |
| 4200 | 182.8 | 183.2 | 2200 |
| 14088 | 182.7 | 183.2 | 188 |
| 3535 | 182.6 | 183.3 | 4200 |
| 6174 | 182.5 | 183.4 | 6100 |
| 180 | 182.5 | 183.5 | 10000 |
| 10000 | 182.3 | 183.5 | 3150 |
| 10000 | 182.1 | 183.5 | 5580 |
| 860 | 182 | 183.5 | 860 |
| 12040 | 182 | 183.6 | 7714 |
| 6660 | 182 | 183.8 | 8462 |

**Bid prices**

The prices where **buyers** are willing to buy (bid)

**Best bid:** highest price a buyer is currently quoting

**Ask prices**

The prices where **sellers** are willing to sell (ask)

**Best offer:** lowest price a seller is currently quoting

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## **Electronic order-book** trading

Top line = inside market, or **'touch price'**
Difference between them is the **bid-ask spread**

**Highest bid**

**182.8**

Traders can **sell shares** immediately at **182.8**

| Bid side | | Offer (ask) side | |
|---|---|---|---|
| **13000** | **182.8** | **183.1** | **1450** |
| 8800 | 182.8 | 183.1 | 1450 |
| 4200 | 182.8 | 183.2 | 2200 |
| 14088 | 182.7 | 183.2 | 188 |
| 3535 | 182.6 | 183.3 | 4200 |
| 6174 | 182.5 | 183.4 | 6100 |
| 180 | 182.5 | 183.5 | 10000 |
| 10000 | 182.3 | 183.5 | 3150 |
| 10000 | 182.1 | 183.5 | 5580 |
| 860 | 182 | 183.5 | 860 |
| 12040 | 182 | 183.6 | 7714 |
| 6660 | 182 | 183.8 | 8462 |

**Lowest offer**

**183.1**

Traders can **buy shares** immediately at **183.1**

## **Electronic order-book** trading

Below the top prices = **many other orders** representing deeper layers of **liquidity**

The **more depth** there is, the **less the price will move** when a large trade hits the market

| Bid side | | Offer (ask) side | |
|---|---|---|---|
| **13000** | **182.8** | **183.1** | **1450** |
| 8800 | 182.8 | 183.1 | 1450 |
| 4200 | 182.8 | 183.2 | 2200 |
| 14088 | 182.7 | 183.2 | 188 |
| 3535 | 182.6 | 183.3 | 4200 |
| 6174 | 182.5 | 183.4 | 6100 |
| 180 | 182.5 | 183.5 | 10000 |
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| 860 | 182 | 183.5 | 860 |
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| 6660 | 182 | 183.8 | 8462 |

# Equity Order Book Example

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***Please sell 20,000 shares at market***

**Market order**
"execute immediately at the best price available"

Prioritizes **speed** and **certainty** over price control

**Order execution**

1. **8,800 @ 182.8** fully executed
   ↳ Remaining: **11,200 shares**
2. **4,200 @ 182.8** fully executed
   ↳ Remaining: **7,000 shares**
3. **7,000 @ 182.7** partially executed

**= 20,000 shares @ 182.765**

(volume-weighted average price)

**Bid side**

| | 13000 | 182.8 |
|---|---|---|
| 1 | ~~8800~~ | ~~182.8~~ |
| 2 | ~~4200~~ | ~~182.8~~ |
| 3 | ~~14000~~ 7088 | 182.7 |
| | 3535 | 182.6 |
| | 6174 | 182.5 |
| | 180 | 182.5 |
| | 10000 | 182.3 |
| | 10000 | 182.1 |
| | 860 | 182 |
| | 12040 | 182 |
| | 6660 | 182 |

**Offer (ask) side**

| 183.1 | 1450 |
|---|---|
| 183.1 | 1450 |
| 183.2 | 2200 |
| 183.2 | 188 |
| 183.3 | 4200 |
| 183.4 | 6100 |
| 183.5 | 10000 |
| 183.5 | 3150 |
| 183.5 | 5580 |
| 183.5 | 860 |
| 183.6 | 7714 |
| 183.8 | 8462 |

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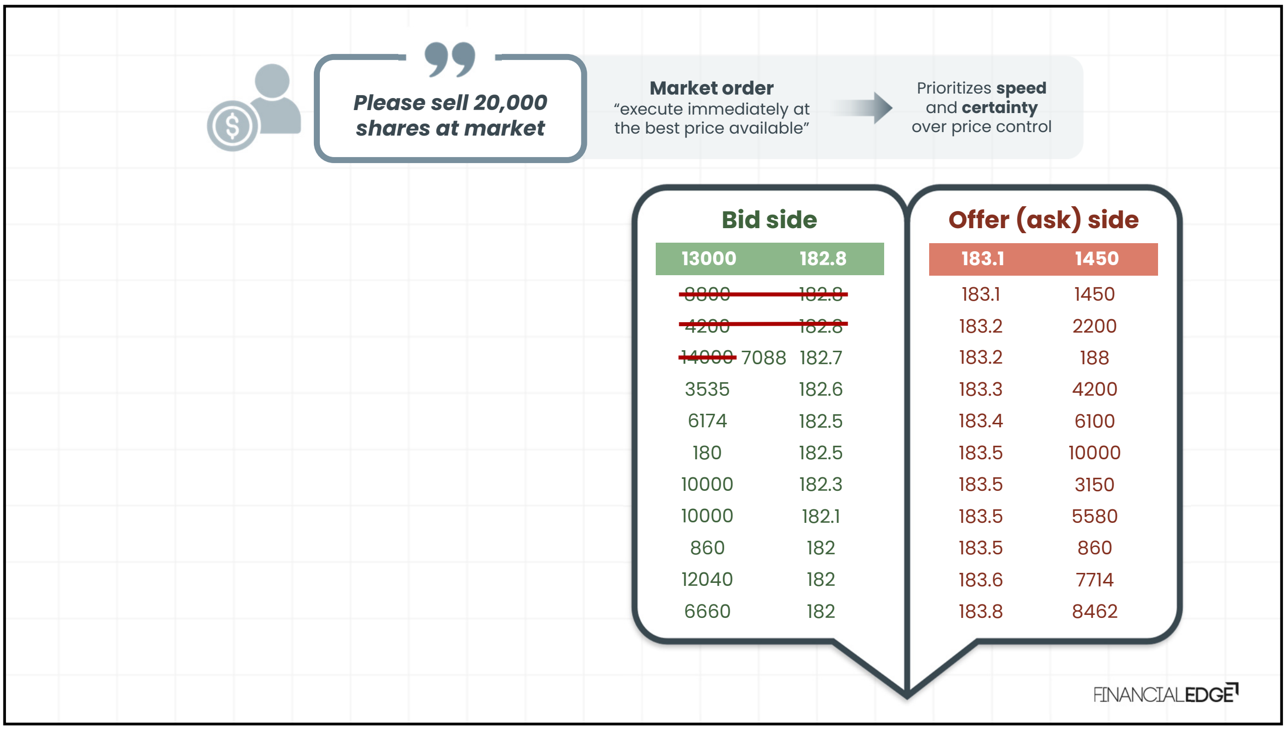
Please sell 20,000 shares at market
Market order
"execute immediately at the best price available"
Prioritizes **speed** and **certainty** over price control
Bid side

| 13000 | 182.8 |
|---|---|
| ~~8800~~ | ~~182.8~~ |
| ~~4200~~ | ~~182.8~~ |
| ~~14000~~ 7088 | 182.7 |
| 3535 | 182.6 |
| 6174 | 182.5 |
| 180 | 182.5 |
| 10000 | 182.3 |
| 10000 | 182.1 |
| 860 | 182 |
| 12040 | 182 |
| 6660 | 182 |

Offer (ask) side

| 183.1 | 1450 |
|---|---|
| 183.1 | 1450 |
| 183.2 | 2200 |
| 183.2 | 188 |
| 183.3 | 4200 |
| 183.4 | 6100 |
| 183.5 | 10000 |
| 183.5 | 3150 |
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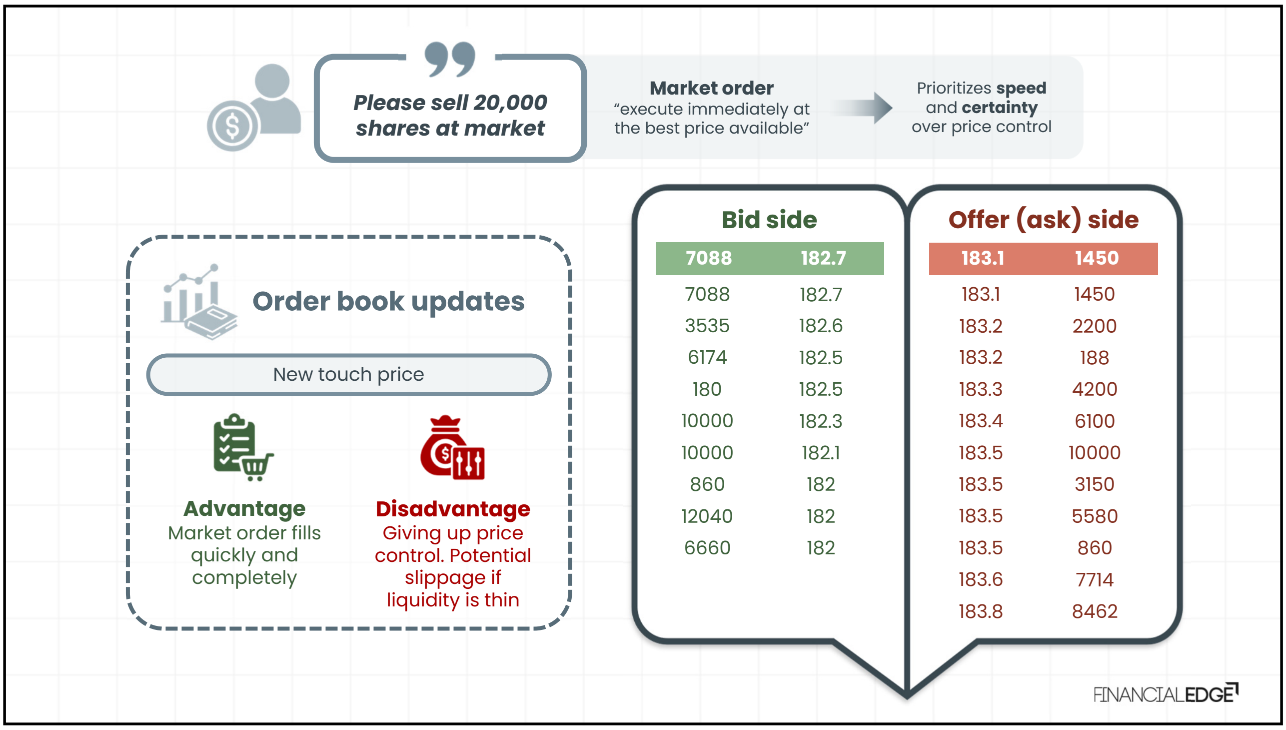
Please sell 20,000 shares at market
Market order
"execute immediately at the best price available"
Prioritizes **speed** and **certainty** over price control
Order book updates
New touch price
**Advantage**
Market order fills quickly and completely
**Disadvantage**
Giving up price control. Potential slippage if liquidity is thin
Bid side

| 7088 | 182.7 |
|---|---|
| 7088 | 182.7 |
| 3535 | 182.6 |
| 6174 | 182.5 |
| 180 | 182.5 |
| 10000 | 182.3 |
| 10000 | 182.1 |
| 860 | 182 |
| 12040 | 182 |
| 6660 | 182 |

Offer (ask) side

| 183.1 | 1450 |
|---|---|
| 183.1 | 1450 |
| 183.2 | 2200 |
| 183.2 | 188 |
| 183.3 | 4200 |
| 183.4 | 6100 |
| 183.5 | 10000 |
| 183.5 | 3150 |
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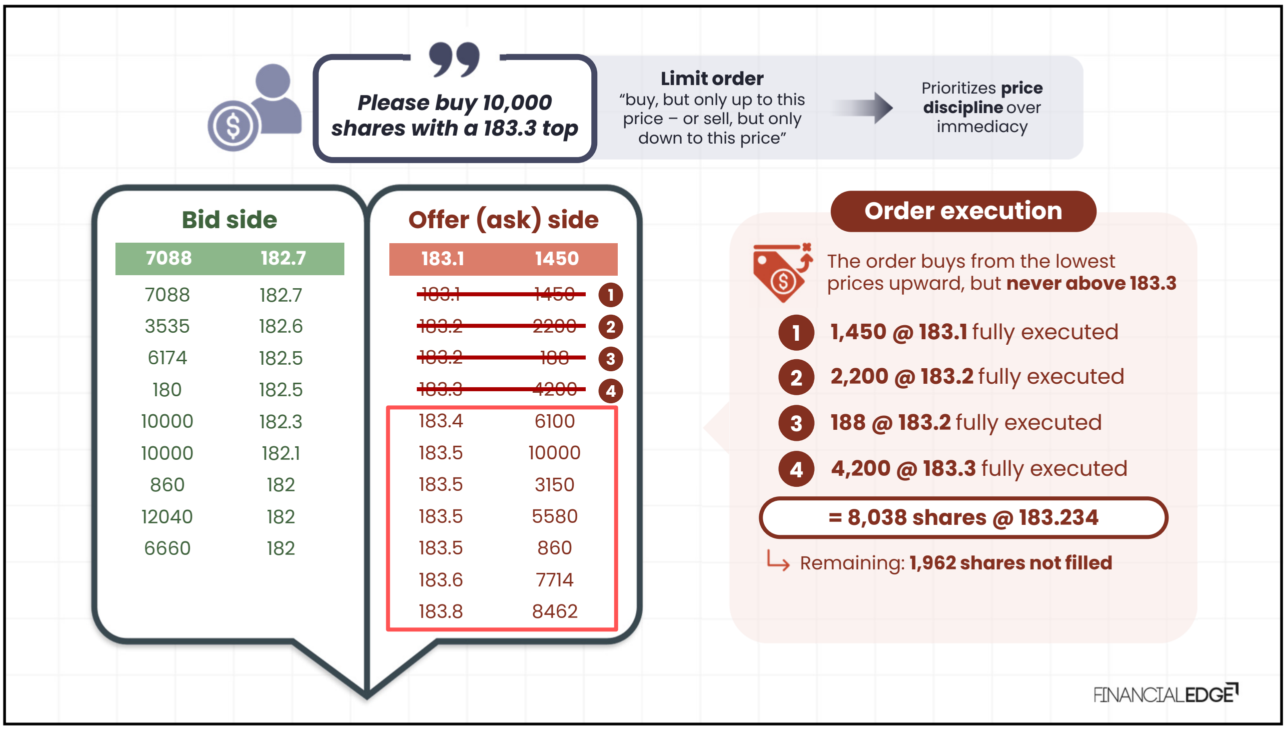
Please buy 10,000 shares with a 183.3 top
Limit order
"buy, but only up to this price – or sell, but only down to this price"
Prioritizes price discipline over immediacy
Bid side
7088 182.7
7088 182.7
3535 182.6
6174 182.5
180 182.5
10000 182.3
10000 182.1
860 182
12040 182
6660 182
Offer (ask) side
183.1 1450
~~183.1 1450~~ 1
~~183.2 2200~~ 2
~~183.2 188~~ 3
~~183.3 4200~~ 4
183.4 6100
183.5 10000
183.5 3150
183.5 5580
183.5 860
183.6 7714
183.8 8462
Order execution
The order buys from the lowest prices upward, but never above 183.3
1 1,450 @ 183.1 fully executed
2 2,200 @ 183.2 fully executed
3 188 @ 183.2 fully executed
4 4,200 @ 183.3 fully executed
= 8,038 shares @ 183.234
Remaining: 1,962 shares not filled
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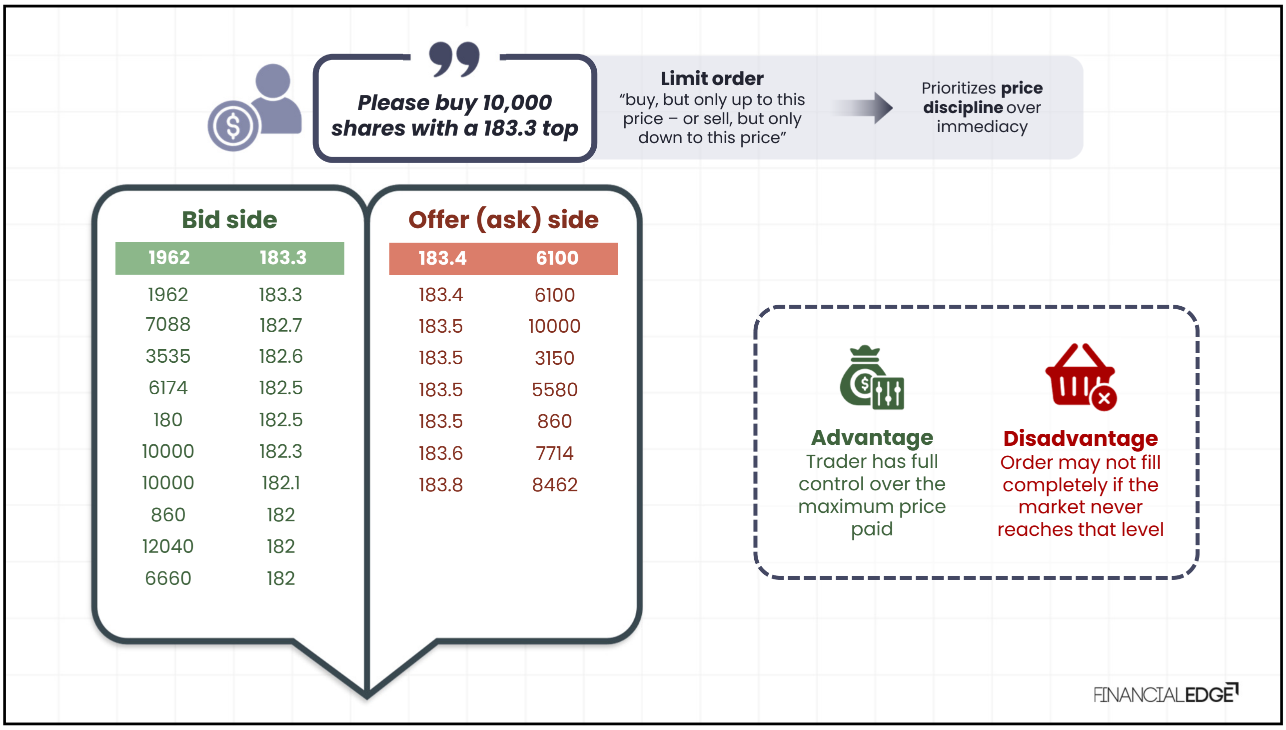
Please buy 10,000 shares with a 183.3 top
Limit order
"buy, but only up to this price – or sell, but only down to this price"
Prioritizes price discipline over immediacy
Bid side
1962 183.3
1962 183.3
7088 182.7
3535 182.6
6174 182.5
180 182.5
10000 182.3
10000 182.1
860 182
12040 182
6660 182
Offer (ask) side
183.4 6100
183.4 6100
183.5 10000
183.5 3150
183.5 5580
183.5 860
183.6 7714
183.8 8462
Advantage
Trader has full control over the maximum price paid
Disadvantage
Order may not fill completely if the market never reaches that level
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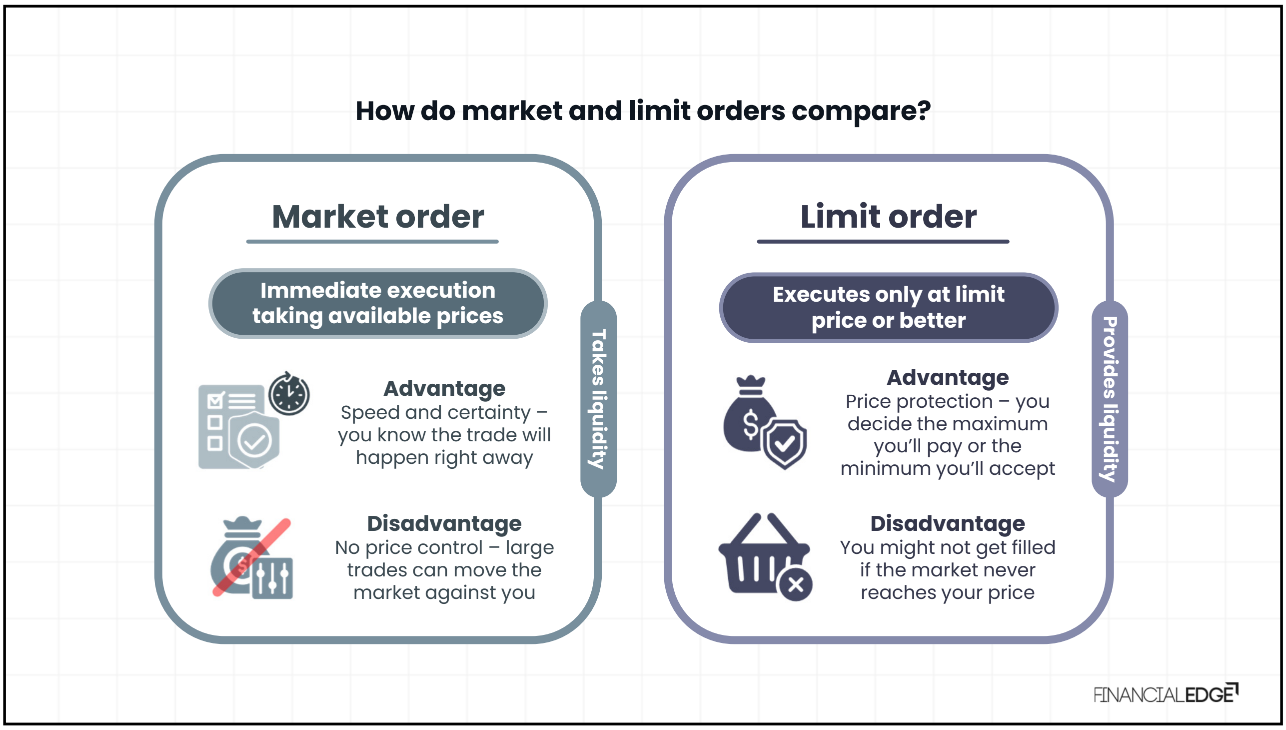
How do market and limit orders compare?
Market order
Immediate execution taking available prices
Advantage
Speed and certainty – you know the trade will happen right away
Disadvantage
No price control – large trades can move the market against you
Takes liquidity
Limit order
Executes only at limit price or better
Advantage
Price protection – you decide the maximum you'll pay or the minimum you'll accept
Disadvantage
You might not get filled if the market never reaches your price
Provides liquidity
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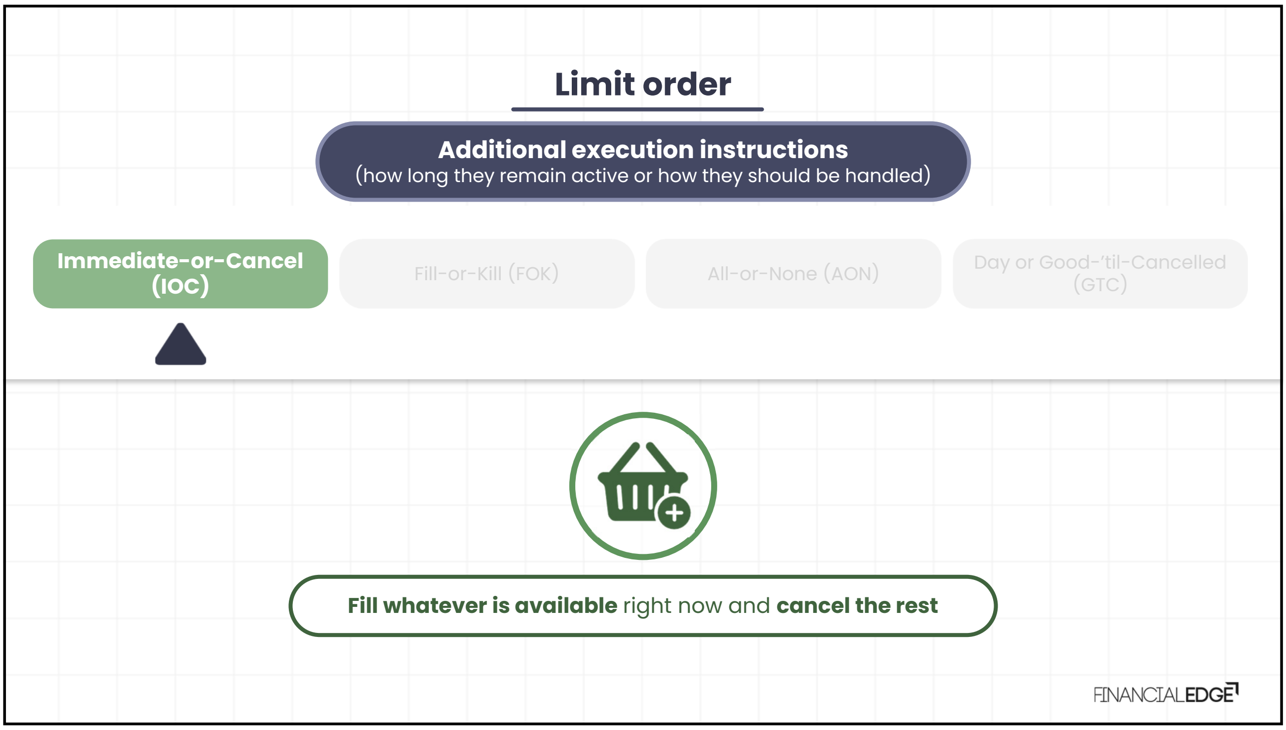
Limit order
Additional execution instructions
(how long they remain active or how they should be handled)
Immediate-or-Cancel (IOC)
Fill-or-Kill (FOK)
All-or-None (AON)
Day or Good-'til-Cancelled (GTC)
Fill whatever is available right now and cancel the rest
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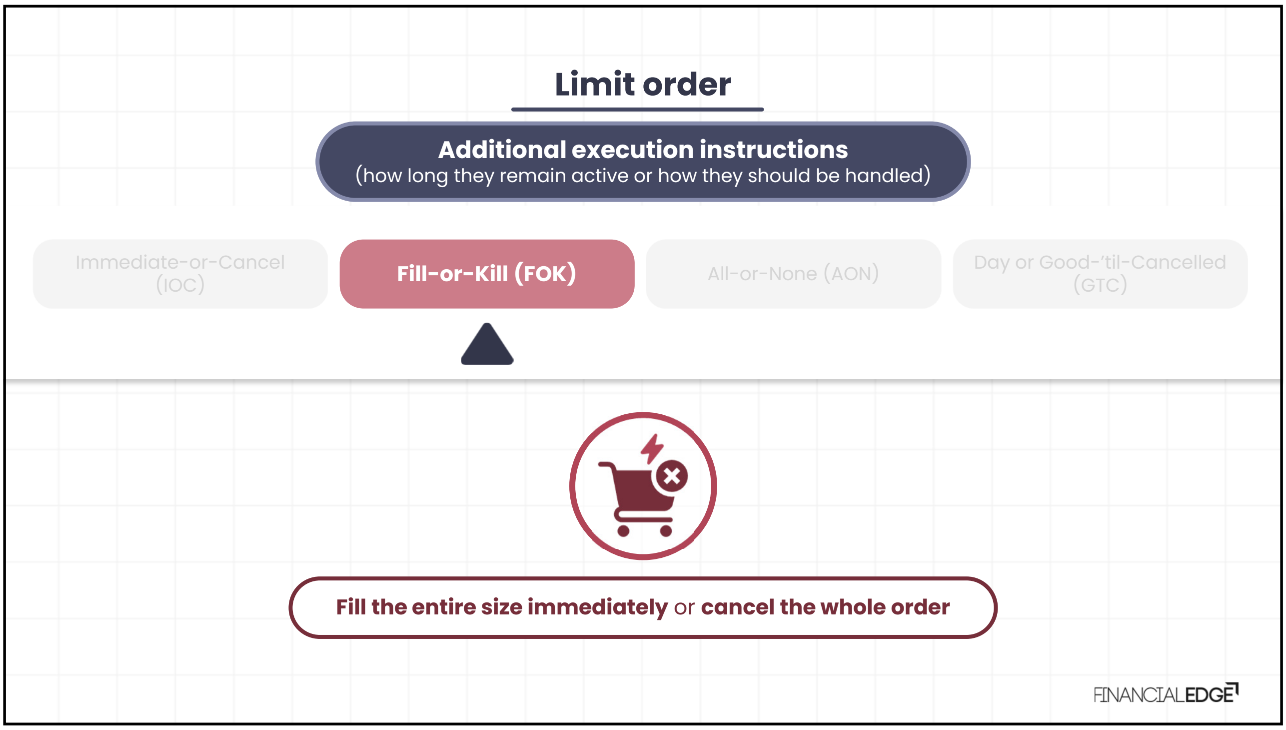
Limit order
Additional execution instructions
(how long they remain active or how they should be handled)
Immediate-or-Cancel (IOC)
Fill-or-Kill (FOK)
All-or-None (AON)
Day or Good-'til-Cancelled (GTC)
Fill the entire size immediately or cancel the whole order
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Limit order
Additional execution instructions
(how long they remain active or how they should be handled)
Immediate-or-Cancel (IOC)
Fill-or-Kill (FOK)
All-or-None (AON)
Day or Good-'til-Cancelled (GTC)
Fill the full size in one go, even if that means waiting
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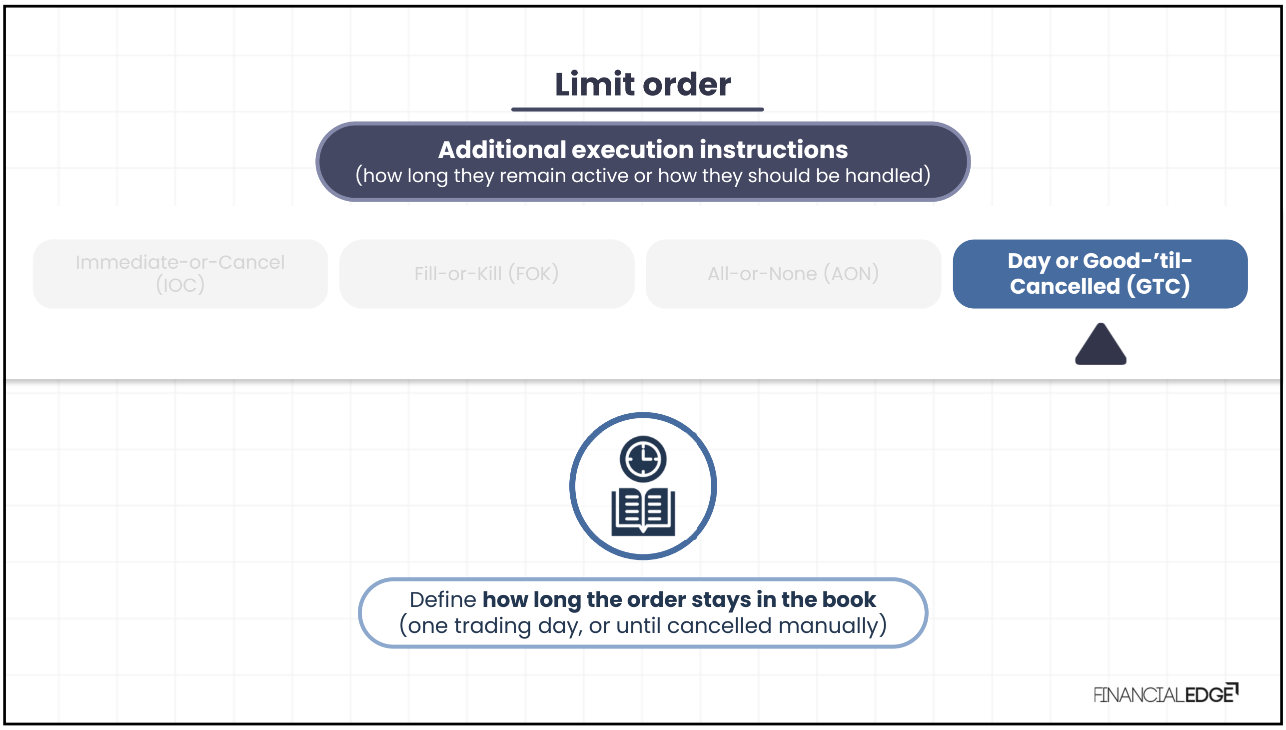
Limit order
Additional execution instructions
(how long they remain active or how they should be handled)
Immediate-or-Cancel (IOC)
Fill-or-Kill (FOK)
All-or-None (AON)
Day or Good-'til-Cancelled (GTC)
Define how long the order stays in the book
(one trading day, or until cancelled manually)
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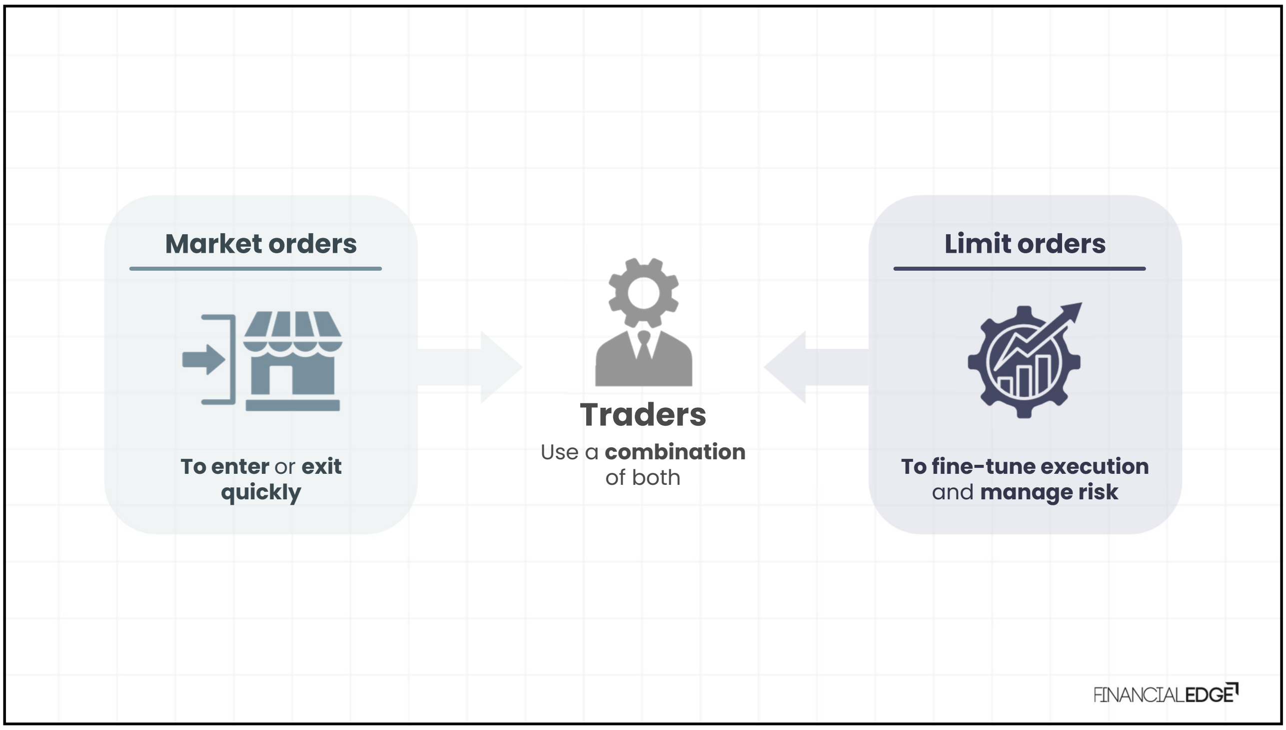
Market orders
To enter or exit quickly
Traders
Use a combination of both
Limit orders
To fine-tune execution and manage risk
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