Wharton
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JACOBS LEVY EQUITY MANAGEMENT CENTER
for Quantitative Financial Research

“Circuit Breakers, Illiquidity, and the COVID-19 Crisis” by Claudia Moise

Discussion by Chester Spatt

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My Background

- SEC Chief Economist (2004-2007)
- Studies of trading in markets and adverse selection
- Admirer and friend of Pete Kyle and his path-breaking paper
- Penn Ph.D. (economics)

Framing the Paper

- Circuit Breakers studied in a clever context (COVID-19), one in which frequently triggered (due to volatility and withdrawal of liquidity).
- Many interesting empirical facts—commend author for drilling down this way
- A number of types of market closures—difference in scope and duration
- Good focus, important issue – Should we be closing markets temporarily? If so, when?

Contribution

- Paper highlights the dominance of reversals rather than continuations after the trading halts.
- Suggestive of a liquidity problem rather than an informational problem.
- Given the empirical result, I wonder whether halts are then helpful:
  - Given the dominance of reversals should liquidity providers hold back offering liquidity (rules affect strategies such as liquidity provision).

Motivation for Halts

- My view has evolved, should we be seeing halts as protecting against asymmetric information/ adverse selection, thereby encouraging liquidity to be offered ex ante.
- These issues would be best evaluated within a model of the impact on informed trading and liquidity provision.
- It would be useful to tie this to what the SEC hopes to accomplish with various halt policies--reduce volatility, systemic risk, asymmetric information?

The Challenge of Design

- Ex ante vs. ex post policies
- Presumably ex ante policies are desired—do we have enough data to generate these?
- In some respects, we only have small samples of extreme events (representativeness) – but few possible extreme scenarios have been observed
- Should we then weigh COVID and other unusual events strongly--what to target?
- The role of dark pools vs. lit markets – dark trading not closed

Lit Markets vs. Dark Pools

- Sometimes the paper drifts into SEC orthodoxy—such as implicit criticism of dark pools as not helping price discovery.
- My view is that is more complex—one sometimes misattributes price discovery across platforms because of issues with reporting lags and the ecosystem of wholesalers across dark and lit platforms (e.g., Ernst, Sokobin and Spatt (2023)).

Suggestions

- Use graphs or summary tables to highlight
  - various closure triggers during COVID
  - various closure triggers over time
  - key statistics for various categories
  - highlight policy conclusions
- Use theory to a greater extent -- both because the questions hinge considerably upon adverse selection/information and liquidity; the policy issues are conceptual at their core

Suggestions for the SEC

- Encourage healthy skepticism about SEC views and policies – my generic perspective
  - In this space the SEC regulations evolved with a small sample of events—How can it enhance the design?
  - Conceptual analysis (“theory”) -- detailed design
  - A number of awkward policies
  - Ex post cancellations (2010) very problematic (especially given basket trades and unpredictability of cancellations).
  - March 2020: Many ‘useless’ pandemic delayed openings—did these help avoid crashes??