



ELSEVIER

Available online at [www.sciencedirect.com](http://www.sciencedirect.com)

SCIENCE @ DIRECT®

Journal of Financial Economics 69 (2003) 375–397

JOURNAL OF  
Financial  
ECONOMICS

[www.elsevier.com/locate/econbase](http://www.elsevier.com/locate/econbase)

# An examination of own account trading by dual traders in futures markets<sup>☆</sup>

Sugato Chakravarty<sup>a,\*</sup>, Kai Li<sup>b</sup>

<sup>a</sup> *Purdue University, West Lafayette, IN 47907, USA*

<sup>b</sup> *University of British Columbia, Vancouver, Canada V6T 1Z2*

Received 19 January 2001; received in revised form 9 April 2002; accepted 21 March 2003

---

## Abstract

Using proprietary audit trail transaction data compiled by the Commodity Futures Trading Commission, we investigate at the individual trader level (1) the *timing* and (2) the *determinants* of dual traders' personal trades. Our analysis reveals an absence of any trade timing by dual traders in relation to the execution of their customers' orders. Further examination employing correlation statistics and time series regressions provides strong support for the proposition that dual traders supply liquidity and actively manage inventory. Even after simultaneously controlling for factors representing information, liquidity supply, and inventory control, within a multivariate regression framework, liquidity supply and inventory control remain as the determinants of dual traders' personal trades. Overall, the emergent profile of a dual trader is that of an uninformed trader performing complimentary tasks.

© 2003 Elsevier B.V. All rights reserved.

*Keywords:* Dual trading; Front-running; Informed trader; Inventory; Liquidity; G20; G28

---

---

<sup>☆</sup>We thank two anonymous referees for their detailed and insightful comments, Steve Mann for providing the data, and Peter Locke for clarifying institutional details. We also thank Doron Avramov, Murray Carlson, David Denis, Gerry Garvey, Rob Heinkel, Alexander Kempf, Alan Kraus, John McConnell, N.R. Prabhala, Asani Sarkar, Avaniidhar Subrahmanyam (Subra), Raman Uppal, and seminar participants at Purdue University, York University, and the Chicago Board of Trade 13th Annual European Futures Research Symposium in Scotland for various comments and suggestions on the present, and earlier, versions of the paper. Marta Sue Foth and Yang Wu prepared the tables, Joshua Slive provided valuable editorial help, and Longkai Zhao provided excellent research assistance during the revision of the paper. We also thank the Futures Industry Institute for providing us with the daily settlement price data. Chakravarty acknowledges financial support from the Purdue Research Foundation and Li acknowledges financial support from the Social Sciences and Humanities Research Council of Canada and the Bureau of Asset Management at UBC. The usual disclaimer applies.

\*Corresponding author. Tel.: 1-765-494-6427; fax: +1-765-494-0869.

*E-mail addresses:* [sugato@purdue.edu](mailto:sugato@purdue.edu) (S. Chakravarty), [kai.li@commerce.ubc.ca](mailto:kai.li@commerce.ubc.ca) (K. Li).

0304-405X/03/\$ - see front matter © 2003 Elsevier B.V. All rights reserved.

doi:10.1016/S0304-405X(03)00117-X

## 1. Introduction

Dual trading is an age-old custom in futures markets whereby some floor traders are allowed to trade both for themselves and for their customers. The Chicago Mercantile Exchange Rulebook defines dual trading as:

The term “dual trading” shall mean trading or placing an order for one’s own account, an account in which one has a direct or indirect financial interest or an account which one controls, in any contract month in which such person previously executed, received or processed a customer order on the Exchange floor during the same Regular Trading Hours session.

This seemingly innocuous practice has attracted the attention of researchers and regulators alike, in light of ongoing Congressional debate on imposing personal trading restrictions on dual traders. An excerpt from Bloomberg news wire release, July 22, 1999, titled “Regulators to Decide Personal Trading by Futures Brokers” reads, in part, as follows:

U.S. regulators are gearing up to decide soon whether to limit a common trading practice on futures exchanges in Chicago that some critics say raises the potential for brokers to cheat their customers. . . . . “We will lose some of our brokers, who say they need to supplement their income by trading for themselves as well as their customers [If these trading limits are imposed],” said Jim Sutter, who manages Cargill Inc.’s oilseeds and grain futures trading on the Exchange.

The supporters of the ban on dual trading argue that floor traders are in a position to front run their customers’ orders. An FBI sting operation at the Chicago Board of Trade (CBOT) and the Chicago Mercantile Exchange (CME) in late 1988 and early 1989 concluded that brokers (including dual traders) were cheating customers. This operation led to dozens of arrests and a 1992 government ban on dual trading in major futures contracts. Interestingly, Congress banned the practice of dual trading but then left the door open by telling regulators they could decide on when to enforce the ban. Opponents of the ban claim (see Grossman, 1989) that some brokers affected by the ban might exit the market, resulting in illiquid markets and higher trading costs for investors.

The debate ultimately boils down to whether dual traders should be allowed to enjoy the privilege of own account trading along with their normal brokering activities. We contribute to this debate by investigating two related questions not addressed by the extant empirical literature. Specifically, we examine (1) the *timing* of a dual trader’s personal trades in relation to the execution of a customer’s orders and (2) the *determinants* of his personal trading decision. Existing research suggests the possible candidates driving dual traders’ personal trading are information, liquidity supply, and inventory control.<sup>1</sup>

---

<sup>1</sup>See, for example, Grossman (1989), Roell (1990), Fishman and Longstaff (1992), Smith and Whaley (1994), Chakravarty (1994), Chang et al. (1994), Sarkar (1995), Chang and Locke (1996), Manaster and Mann (1996), and Locke et al. (1999).

متن کامل مقاله

دریافت فوری ←

**ISI**Articles

مرجع مقالات تخصصی ایران

- ✓ امکان دانلود نسخه تمام متن مقالات انگلیسی
- ✓ امکان دانلود نسخه ترجمه شده مقالات
- ✓ پذیرش سفارش ترجمه تخصصی
- ✓ امکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
- ✓ امکان دانلود رایگان ۲ صفحه اول هر مقاله
- ✓ امکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
- ✓ دانلود فوری مقاله پس از پرداخت آنلاین
- ✓ پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات