

How Exchanges Compete?

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Why Compete?

Exchanges Want to Grow

- Mutually Owned Exchanges
 - Commissions for members
 - Scalping opportunity for members
 - Member's seat value
- Stockholder-Owned Exchanges
 - Profits
 - Dividends
 - Stock appreciation

Member Opportunity

Profit

How Does an Exchange Grow?

- Attract more trading in existing products
- Create new products - **Continually Innovate**

Continually Innovate

Example -- CME


- CME started in 1898
 - Butter and eggs 1898
 - Pork bellies 1960
 - Live cattle 1964
 - Currencies 1972
 - Interest rates 1976
 - Stock indexes 1982
- In Jan 2006, CME had trading in **80 futures** and 32 options products

**99% of volume is in
Products created
Since 1972**



Continually Innovate

Example -- CBOT

- CBOT started in 1865
 - Grain trading 1865
 - Soybeans 1936
 - Iced broilers 1968
 - Treasury bonds 1977
 - Dow Jones index 1997
 - In Jan 2006, CBOT had trading in **27 futures** and 17 options products
- 89% of volume is in Products created Since 1977**
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Continually Innovate

Example -- NYMEX

- NYMEX started in 1872

- Butter and cheese 1872

- Heating oil 1978 ←

- Gasoline 1981

- Crude oil 1983

- Natural gas 1990

- In Jan 2006, NYMEX had trading in **131 futures** and 23 options products

**99.7% of volume is in
Products created
Since 1978**

What Happens When An Exchange Attacks a Liquid Market?

- Traditionally – Nothing
- Futures markets as **naturally occurring monopolies** due to network effects
 - CME & CBOT attack NYMEX heating oil & gasoline in 1982 – **failure**
 - CME attacks COMEX gold in 1987 – **failure**
 - Eurex US attacks CBOT Treasuries in 2004 – **failure**
 - Euronext.liffe attacks CME's eurodollars in 2004 – **failure**
- **Monopoly rule stronger for derivatives because securities exchanges have common clearing**

Exceptions to the Monopoly Rule

- When a lower-cost, transparent, electronic exchange competes against a floor

1990s

- DTB (Eurex) steals the **Bund** from LIFFE
- NSE (India) attacks the Bombay Stock Exchange

Now

- ICE attacks NYMEX's **WTI** (19-25% share)
- CBOT attacks COMEX **gold** (12-18% share)
- CBOT attacks COMEX **silver** (5-6% share)

New York needs to be careful!