

Direct Edge Looks to Beat BATS at its Own Game

By Nina Mehta

May 1, 2008

Direct Edge, the second-largest ECN, has revamped its technology and pricing in its effort to win the business of high-frequency trading firms--the segment of automated traders that made BATS Trading the top gun in ECN volume.

"The Direct Edge critical mass was not built on high-frequency, black-box order flow," said William O'Brien, chief executive officer of the ECN. "But now, that's a segment we're targeting aggressively." Direct Edge's matched market share in its two markets, EDGX and EDGA, was 3.9 percent last month, up from 3.4 percent in March. BATS's matched market share is more than twice that.

Direct Edge yesterday overhauled the pricing on EDGX, its platform with traditional maker-taker fees. The new pricing, which applies to all NMS securities, charges subscribers 26 cents per 100 shares to remove liquidity from its book, while those adding liquidity get a 25-cent rebate. EDGX accounts for about two-thirds of Direct Edge's matched market share, with EDGA providing the rest. EDGA's pricing did not change.

Direct Edge also added a new rebate tier for liquidity providers on EDGX, designed for high-frequency trading firms. Those adding a daily average of 40 million shares on a monthly basis will now get a rebate of 29 cents per 100 shares for that liquidity. That higher tier gives those firms the benefits of inverted pricing since the take fee they pay is lower than their rebate.

Direct Edge's pricing changes yesterday went into effect along with those of Nasdaq, NYSE Arca and the ISE Stock Exchange. The ISE now offers the industry's highest rebate tier of 35 cents per 100 shares.

To draw volume from high-frequency traders, Direct Edge acknowledged, the ECN needed to improve its infrastructure and technology. Previously, it wasn't considered fast enough for some of those latency-sensitive trading firms.

O'Brien noted that Direct Edge recently re-architected its real-time market data feed, which now operates with sub-millisecond latency. The ECN also improved the capacity of its matching engines and increased the efficiency of its network processes by streamlining the system's consumption of market data, the exec said.

BATS Trading declined to comment on Direct Edge's recent moves.

BATS's core liquidity-providing constituency is high-frequency automated trading firms. It was founded by a former CEO of Tradebot Systems, a high-frequency firm, who brought over a group of 13 people to run BATS. BATS's 11 current owners also include GETCO and Lime Brokerage, two other high-frequency players.