TESTIMONY OF

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BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
SUBCOMMITTEE ON SECURITIES, INSURANCE, AND INVESTMENT

UNITED STATES SENATE

ON

"HIGH FREQUENCY TRADING'S IMPACT ON THE ECONOMY"

JUNE 18, 2014

Introduction

Chairman Warner, Ranking Member Johanns, and distinguished Members of the Senate Subcommittee on Securities, Insurance, and Investment, thank you for the opportunity to testify today on behalf of T. Rowe Price[1] regarding the impact of high frequency trading ("**HFT**") on the economy. My name is Andrew (Andy) M. Brooks. I am Vice President and Head of U.S. Equity Trading of T. Rowe Price Associates, Inc. I joined the firm in 1980 as an equity trader and assumed my current role in 1992. This is my 34th year on the T. Rowe Price trading desk.

T. Rowe Price, founded in 1937, is a Baltimore-based global adviser with $711.4 billion in assets under management as of March 31, 2014 and serving more than 10 million individual and institutional investor accounts.

We welcome the opportunity for discussion regarding the industry and market practices.

Since I last testified before this Committee in September 2012, we have seen considerable turnover in Congress, this Committee, and at the U.S. Securities and Exchange Commission ("**SEC**", or the "**Commission**"); however, there has been little change in addressing the issues discussed twenty-one months ago, although we do applaud the SEC's efforts in implementing limit up and limit down controls and developing the Consolidated Audit Trail. Additionally, we are encouraged by Chair Mary Jo White's recent comments suggesting a heightened focus on improving market structure and we appreciate this Committee's continued interest in improving our markets. However, order routing practices, payment for order flow, maker/taker pricing, market data arbitrage, and the myopic quest for speed are all issues that remain unaddressed. In addition, we have grown increasingly concerned about the growth of dark pools and the challenges of the direct "fast" feed operating alongside the "slow" Securities Information Processor ("**SIP**") feed. We recognize that change in Washington is constant, but would like to emphasize the fact that the fundamental market structure issues we face as an industry are ever evolving and are incapable of being resolved without regulatory intervention.

Although this hearing is focused on HFT, we believe HFT is merely symptomatic of larger market structure problems. We are cautious not to lump all electronic trading into the class of HFT and further, we do not believe that all HFT is detrimental to the market. We are supportive of genuine market making; however, we acknowledge that there are predatory strategies in the marketplace that have been enabled by our overly complex and fragmented trading markets. Those parties utilizing such strategies are exploiting market

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[1] T. Rowe Price Associates, Inc., a wholly-owned subsidiary of T. Rowe Price Group, Inc., together with its advisory affiliates (collectively, "**T. Rowe Price**"), had $711.4 billion of assets under management as of March 31, 2014. T. Rowe Price has a diverse, global client base, including institutional separate accounts; T. Rowe Price sponsored and sub-advised mutual funds, and high net worth individuals. The T. Rowe Price group of advisers includes T. Rowe Price Associates, Inc., T. Rowe Price International Ltd, T. Rowe Price Hong Kong Limited, T. Rowe Price Singapore Ltd., T. Rowe Price (Canada), Inc., and T. Rowe Price Advisory Services, Inc.

structure issues to their benefit and to the overall market's and individual investor's detriment.

We question whether the functional roles of an exchange and a broker-dealer have become blurred over the years creating inherent conflicts of interest that may warrant regulatory action. It seems clear that since the exchanges have migrated to "for-profit" models, a conflict has arisen between the pursuit of volume (and the resulting revenue) and the obligation to assure an orderly marketplace for all investors. The fact that 11 exchanges and over 50 dark pools operate on a given day seems to create a model that is susceptible to manipulative behaviors. If a market participant's sole function is to interposition themselves between buyers and sellers we question the value of such a role and believe that it puts an unneeded strain on the system. It begs the question as to whether investors were better served when exchanges functioned more akin to a public utility. Should exchanges with de minimus market share enjoy the regulatory protection that is offered by their status as exchanges, or should they be ignored?

Additionally, innovations in technology and competition, including HFT, have increased market complexity and fragmentation and have diluted an investor's ability to gauge best execution. For example, in the race for increased market share, exchanges and alternative trading venues continue to offer various types of orders to compete for investor order flow. Many of these order types facilitate strategies that can benefit certain market participants at the expense of long-term investors and, while seemingly appropriate, often such order types are used in connection with predatory trading strategies. We are supportive of incremental efforts, such as a recent initiative by the New York Stock Exchange to eliminate 12 order types from their offerings.

We also believe that increased intraday volatility over the past few years is symptomatic of an overly complex market. Though commission rates and spreads have been reduced, intraday volatility continues to be alarmingly high. It was refreshing to see a recent report from RBC Capital Markets[2] examining the impact of intraday volatility and exposing the high costs to investors. Most academics only look at close to close market volatility.

Increased market complexity results in a lack of investor confidence. Our firm is particularly focused on the interests of long-term investors although we appreciate the role other types of investors can have in creating a dynamic marketplace. A recent Gallup poll noted that American household ownership of stocks continues to trend well below historic norms[3]. One can never be sure what drives investor behavior, but it seems clear to us that we need to do a better job of earning investor's confidence in the market. Those investors who have stayed on the sidelines in recent years, for whatever reason, have missed out on significant equity returns. We worry that the erosion of investor

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[2] Bain, S., Mudassir, S., Hadiaris, J., & Liscombe, M. (2014). RBC Capital Markets, "The Impact of Intraday Volatility On Investor Costs: Insights into the Evolution of Market Structure", RBC Capital Markets

[3] U.S. Stock Ownership Stays at Record Low. (n.d.). U.S. Stock Ownership Stays at Record Low. Retrieved June 17, 2014, from http://www.gallup.com/poll/162353/stock-ownership-stays-record-low.aspx

confidence can undermine our capital markets, which are so important to the economy, job growth, and global competitiveness. Re-affirming a strongly rooted commitment to fairness and stability of the market's infrastructure is critically important.

Over the past two decades the markets have benefited from innovations in technology and competition. Generally, markets open at 9:30am, close at 4:00pm, and trades settle efficiently and seamlessly. The markets function in an orderly fashion, but if one were designing a market from scratch we doubt that we would end up with the overly complex structure we have today.

Vibrant and robust markets function best when there are varied investment opinions, styles and approaches. However, given the myriad of ways to engage in the markets, we feel that investors would benefit from an increased focus on market structure, particularly features that enable predatory and manipulative practices. We applaud looking into an enhanced oversight of HFT and other high frequency strategies and conflicts of interest in our current market structure. Disruptive HFT strategies are akin to a tax loophole that has been exploited and needs to be closed. Market participants utilizing such strategies are essentially making a riskless bet on the market, like a gambler who places a bet on a race that's already been run and for which he knows the outcome.

Suggestions

In the spirit of advancing the interests of all investors we might make the following suggestions:

A good first step might be to experiment with a number of pilot programs to examine different structural and rule modifications. We envision a pilot program where all payments for order flow, maker-taker fees, and other inducements for order flow routing are eliminated. We also envision a pilot that incorporates wider minimum spreads and some version of a "trade at" rule, which we believe would lead to genuine price improvement. These programs should include a spectrum of stocks across market caps and average trading volumes, among other factors. Additionally, we would advocate for a pilot program that would mandate minimum trade sizes for "dark pools". "Dark pools" were originally constructed to encourage larger trading interests and it seems perverse that many venues on the "lit" markets or exchanges have a larger average trade size than "dark pools".

HFT and market structure issues were recently brought into the public spotlight by Michael Lewis and his book Flash Boys[4]. Sometimes it takes a storyteller like Mr. Lewis to bring the attention needed to an issue, and we hope that all parties involved will come together and seize this opportunity to improve our markets. Again, we would advocate for pilot programs to test and ultimately implement measured yet significant changes. At the end of the day we are here because of our firm commitment to all investors to ensure that the capital markets perform the functions for which they were designed-capital

[4] Lewis, M. (2014). Flash boys: a Wall Street revolt. New York: W.W. Norton & Company, Inc..

formation for companies and investment opportunities for both institutions and individuals.

On behalf of T. Rowe Price, our clients, and shareholders, I want to thank the Committee for the opportunity to share our views on how we can, together, make our markets as good as they can be.