



## **Models, Morals, and Management in a Wall Street Trading Room**

### **Taking the floor**

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#### **Editorial RiskNet**

The recent financial crisis has shown that international financial markets are not only an essential and important instrument of economic growth processes and a multiplier for wealth gains, but can also produce and reinforce crisis-like developments in the economy and society. In order to understand this Janus-faced form of the financial markets and to regulate it meaningfully, one must immerse oneself deeply in the functioning of the financial markets. This also includes looking at the actors' fingers, understanding their methods and models, and understanding the organisation and subculture of the financial markets.

The discussion on the regulation and reform of the financial markets has shown that a healthy and robust financial system depends on which governance, and above all culture, is implemented and lived. Based on intensive research in a Wall Street trading room for financial derivatives, author Daniel Beunza has examined how the culture of financial organizations must change in order to remain robust in times of crisis.

In his book "Taking the Floor: Models, Morals, and Management in a Wall Street Trading Room", Daniel Beunza also analysed how the comprehensive use of financial and risk models and technologies has had a far-reaching and disturbing impact on Wall Street in recent decades. How have quantitative models changed the financial markets? How have models changed the moral behaviour of market participants?

Many people still think of screens with price tickers on them when they talk about "stock market trading" and of the stock market floor with screaming traders. But for many years no one has been screaming on the floor. People still work on the stock markets, but they are neither the masters of the financial market nor do they have a privileged insight into the markets. Today, stock trading takes place in a black box, more precisely in high-security buildings in New Jersey and Chicago, London and so on. Only "insiders" know what is going on in this black box. The fact is that about forty percent of the stock exchange transactions carried out on Deutsche Börse's electronic trading platform are attributable to so-called flash traders.

Robotic stock trading, for example, is a specific type of high frequency trading (HFT) in which securities are bought and sold within milliseconds. Seconds trading is based on order information that they receive for a few fractions of a second earlier than others. "Frontrunning" is what stock exchange experts call this. This temporal difference is sufficient for the scalar or

vector calculators to be able to send their own orders to the market the decisive millisecond earlier.

Among other things, HFT has made financial markets more sensitive and susceptible to weak signals. Flash traders can, for example, move the markets with fictitious orders. Algorithms are optimized so that they can react to an event within milli- or nanoseconds. As a consequence, high-frequency trading can lead to destabilization of the markets through a domino effect.

The reader of "Taking the Floor" accompanies the author behind the scenes and into the trading room. Here the author points out the increasing risk that quantitative models can lead to the risk being detached from morality. It is algorithms that make decisions. And an algorithm can neither distinguish between "right" and "wrong" nor between "good" and "evil". An algorithm is quasi "unscrupulously conscientious". Trading algorithms cannot verify decisions with regard to their moral content.

Beunza opens the black box of a Wall Street trading room and presents the reader with a surprising picture of morality and governance. The book thus primarily provides incentives for the establishment and further development of a sustainable governance structure and a living risk culture. From the perspective of risk management, the author shows that such technology and model-driven trading has massively increased potential systemic risks.

Original link:

<https://www.risknet.de/wissen/rezensionen/taking-the-floor/>