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News Release

SECURITIES MARKET ISSUES FOR 1989: MARKET LIQUIDITY, LARGE TRADER INFORMATION, AND HOLDING COMPANY RISK ASSESSMENT

Remarks of

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I. Introduction

It is a great pleasure to speak to the Women's Economic Round Table. As you may be aware, women occupy many of the top positions at the Securities and Exchange Commission. Two of our four major operating divisions are headed by women, and my executive assistant, Linda Fienberg, is the de facto chief operating officer of the Commission.

Since the dramatic events in October 1987 much of my energy has been devoted to monitoring the health of our securities markets. The October 1987 market break stimulated comprehensive analyses of various aspects of our securities markets, and, as the Chairman of the government agency most directly charged with responsibility for regulating those markets, I have directed that there be regular review of their performance.

Following October 1987, many changes were implemented. Looking beyond the significant reforms already instituted and those the markets continue to pursue, there are many areas where changes still should be considered. Three areas of particular importance are: (1) market liquidity; (2) the need for more current information regarding large securities trades; and (3) the Commission's ability to obtain early warning of the potential financial risks to broker-dealers arising from activities of their unregulated affiliates.

II. The Market Break and Subsequent Reforms

One of the central lessons of the October 1987 market break was that institutional trading strategies can have extreme effects on market volatility. The acceptance of modern finance and diversification theories, the growth in size of institutional portfolios, and lowered trading costs have led to the increasing use of portfolio trading strategies by institutions. In October 1987 simultaneous decisions by institutions pursuing common short-term trading strategies produced a "rush to the exit" that overwhelmed the capacity of our markets. While there has been much debate about the causes of the market break, it seems clear now that deficiencies in operational systems, information transmission, liquidity, and clearance and settlement procedures affected the speed and size of the decline.

Since the market break, many reforms have been instituted by the markets.

Automation

Automation improvements by the exchanges, the National Association of Securities Dealers (NASD), private vendors, broker-dealers, and investment companies have greatly expanded the operational capacities of our markets. In future periods of market stress, the flow of orders should be handled much more efficiently. Customers should be able to reach their brokers and orders should be executed more quickly.

Market Makers

Measures to improve market makers' performance have been implemented. The NASD has imposed new market making commitment requirements with respect to its Small Order Execution System that will increase the efficiency of its markets. Improvements in securities exchanges' "reallocation" procedures have helped to strengthen the exchange specialist system. The exchanges have increased specialist capital requirements and, recently, the Commission has proposed that specialists be required to comply with its net capital rule, from which they are currently exempt. 1/ Specialists and other market makers have been encouraged to review and strengthen their lines of credit with banks.

Communications

Communication, coordination, and contingency planning have been increased. Dedicated telephone lines have been installed between the major markets, and personal lines of communication have been established. Communication between various regulatory agencies has been enhanced at both the staff and agency head level, and the President's Working Group on

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1/ Securities Exchange Act Release No. 26402 (December 28, 1988).