

Working Paper: Algorithmic Trading and High Frequency Trading In the Israeli Capital Market – Review and Initial Findings

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Abstract

In recent years, algorithmic trading has become increasingly prevalent in the Tel Aviv Stock Exchange. Algorithmic trading is significant in terms of encouraging liquidity and market development, as well as various regulatory issues.

The study describes the characteristics of algorithmic trading, reviews its contribution to the capital market both in Israel and abroad and examines its share and contribution to liquidity in the forward and financial instruments market (MAOF). The study found that the share of algorithmic players in the contract volume in the MAOF market peaked in 2011, reaching approximately 40%, while in 2013, it reached 25%. On the other hand, their share of the orders was double, and even higher in orders entered in the first level. In other markets, their share was smaller, and is most evident in the corporate bond market and ETN market. In addition, the study showed that algorithmic research has important advantages in terms of efficiency, liquidity, correct pricing, fairness and stability. The study also found that algorithmic traders contribute to liquidity in the MAOF market according to the CRT index. Their contribution is even greater in cases of low liquidity, and somewhat in crisis periods.

The study found that algorithmic trading in Israel is still a long way from that in large Western markets: its scope is more limited, it has developed late in relation to other capital markets in the world, and traders end the day with larger positions in relation to their daily activity volume. The study expects this area to continue expanding and improving in Israel, and also expects current algo traders to be joined by both foreign players and additional local players.

The study maintains that any future regulation should preserve the advantages of algorithmic trading, minimize potential risks and respond to the need to follow up on developments in this area.

Read the full text in Hebrew