

DIRECT CONNECT

AIDED BY TECHNOLOGY, DIRECT-ACCESS BROKERS BRING CUSTOMERS CLOSER TO THE POINT OF SALE



Floor brokers communicate with institutional customers through NYSE e-Broker.

It's 9:12 a.m. and time for independent floor broker Gordon Charlop, president of W.J. Dowd Inc., to get "suited up" for his day. At his firm's booth on the perimeter of the NYSE trading floor, he clips his pager and cell phone to his belt, plugs a headset into his cell, swings the strap of his wireless handheld computer, the NYSE e-Broker™ over his shoulder and sets out into the trading crowds.

No orders yet appear on the handheld's screen, but anticipating continued customer interest in the stocks traded the day before, Charlop quickly makes his rounds to a handful of trading posts to gauge the market in those stocks, communicating with specialists and other brokers in the crowd.

By 9:17, opening price indications appear on the screens at the posts, and customer requests for "market looks" pop up on his handheld and the monitors being viewed by the sales reps in his firm's booth. Responding to each request, Charlop probes the crowd, determines who's buying and selling and the size of their interest, and sends the information directly to his customers through the handheld. The sales reps, who are communicating with Charlop through his headset, are speaking directly to the customers, discussing the market looks and confirming their investment objectives.

As the market opens at 9:30, Charlop completes two order executions. He confirms them with his customers and instantaneously provides them with a new, post-

trade look at the market in those stocks, all through his handheld computer.

This venture between the customer and the broker continues throughout the trading day.

"The goal is to bring the customer as close to the point of sale as possible with speed and accuracy of information," Charlop says. "We make sure our customers get the complete picture."

INFORMATION AND EXECUTION PROVIDERS

Charlop is one of approximately 500 individual independent floor brokers, many of whom now specialize in what has become known as "direct access."

What differentiates his firm—along with Francis P. Maglio & Co. Inc., The Griswold Co. Inc., Richard A. Rosenblatt & Co. and Polcari/Weicker and other of the business's better-known boutiques—from full-service brokers is the fact that it is a pure agent: Independents do not offer research or underwriting, and they don't commit capital or trade stocks for their own accounts.

Instead, these execution-only agents provide a direct line to the floor, real-time market snapshots and efficient executions. These no-frills service providers can charge less on commissions and add value in the form of years of experience, plus skill and knowledge of floor trading, making them an attractive option for certain institutional and corporate clients.

One of them is hedge-fund manager Gregory van Kipnis, general manager of Tiedemann/Invictus Fund at Tiedemann Investment Group. He bases his decisions on what to buy and sell on mathematical models that crunch time and price information.

Because his firm does its own research, van Kipnis has less of a need to trade with a full-service member

firm. His independent broker, W.J. Dowd, provides "pure, inexpensive execution," he says. "In effect, they charge less than a discount broker and they devote clerks and brokers to handle my specific needs, day in and day out."

Another segment of the independents' growing customer base is companies repurchasing their stock in the public market. "They have less of a need for the full-service options that a large brokerage would provide," says Joseph Cangemi, director, Francis P. Maglio & Co. Inc. "By using an independent floor broker, they know they can reduce their costs and reinvest the savings."

EVOLUTION OF A DIRECT BUSINESS

The direct-access business of independent brokers is relatively new. Once referred to as "S2 brokers," going back to the days when they earned \$2 for every 100 shares traded, independents used to earn a living executing the excess order flow that the member-firm brokerages were too busy to handle.

The business model of independent brokers expanded in the 1970s with the advent of derivatives trading. "For every option they were writing on the Chicago Board Options Exchange, they were creating an opportunity to sell or buy stock on the NYSE," explains Cangemi. He says expanding their niche services was an opportunity that these "freelance" brokers immediately seized.

The start of futures trading also created an instant arbitrage opportunity that the independents could help their customers capture. "It's the independent-floor-broker community that still responds instantly to new needs, ideas, and ways of trading," adds Richard A. Rosenblatt, president of Richard A. Rosenblatt & Co. Inc., who co-chairs the Organization of Inde-



Floor brokers Richard Rosenblatt (top) and Gordon Charlop (bottom) use e-Broker to manage orders, execute reports and deliver market information.



pendent Floor Brokers with Kenneth Polcari, managing director of Polcari/Weicker.

The most significant evolution in their business followed the Exchange rule change in 1987 that permitted members to establish communication links between their booths on the floor and their non-member customers off the floor. The independents were now able to expand their services beyond the member-firm brokerages directly to the customers themselves. Today, both full-service brokers and independents play important roles in the auction market, where money managers expect brokers to work their orders and fight for the best price.

“It’s information dissemination with a human spin from a professional who knows what an auction should look like, and it’s the subtle negotiations that create the price,” Rosenblatt explains.

Adds Cangemi: “The more efficient a money manager is, the better off the retail investor is. And one way the manager becomes more efficient is by getting closer to the point of sale.”

TECHNOLOGY-DRIVEN MODEL

Advances in trading-floor technology, such as NYSE e-Broker, are helping investors to do just that. In 1997 van Kipnis became the first customer to complete a transaction through e-Broker (with Gordon Charlop).

“Greg knew that brokers should have the ability to transmit and receive orders electronically so that we could get to the point of sale quickly, use the decision-making process of an agent to negotiate trades and immediately return that data back to the customer,” Charlop explains.

Since then, van Kipnis has been taking full advantage of electronic communications with his broker. He says the benefits are high completion rates, price improvement and fewer errors.

“We routinely get a better price than we originally targeted,” van Kipnis says. “And because we are



Joseph Cangemi works the same trading crowd with Jennifer Williams, an independent with Griswold Co. Inc.

paperless end to end, there are no misunderstandings or errors in quotes or prices.”

Floor brokers can use one of two e-Broker devices: the larger, full-function Casio Fiva, which weighs about 2.5 pounds, or the smaller Cassiopeia, which doesn’t transmit orders and reports but can send and receive market looks. Or they can opt to use their own version of the devices. All of them work off of a 2.4-gigahertz wireless network that serves as an extension of the Exchange’s BBSS (Broker Booth Support System) order-management system.

“Essentially, it’s a version of instant messaging between floor brokers and their customers,” says Lou Pastina, NYSE vice president of point-of-sale technology. “With an average of 1.2 billion shares trading on the NYSE each day, that means almost 2.5 million orders and 2.5 million quotes come in and out of this building daily, a level of activity being handled by the same number of people on the floor that were there when we traded 10 million shares a day.”

“Each of our three sales traders would need his or her own assistant if it weren’t for the technology,” Kenneth Polcari says.

Adds Warren P. Meyers, director, W.J. Dowd Inc.: “What used to take 1.5 minutes now takes 1.5 seconds. Orders come right to me, error free, and I am freed up to prioritize and make decisions based on my order flow and where I need to be.”

In 2001, e-Broker usage was up 70% over 2000 levels, to an average of 250 users per day, sending more than 50,000 messages per day and executing about 150 million shares daily, up nearly 425%, Pastina reports. This contributed to an estimated 30% reduction in paper on the floor.

NEW AND IMPROVED

Later this year, the NYSE will roll out a new, even smaller, faster and lighter version of e-Broker based on iPAQ from **Compaq Computer Corp. (CPQ)**. Robert H. McCooley, Jr., president and CEO of The Griswold Co., promises to be one of the first to subscribe. “Our customers place a high value on information,” he says. “They’ve already made their buy and sell decisions, but based on the information we provide, they can decide how to execute their order strategy.”

“Among the Exchange’s greatest assets are the intellectual skills that exist in the floor brokers and specialists,” van Kipnis says. “They’ve got the know-how to execute trades and provide liquidity. It’s important to conserve that critical resource—their minds—and free it from labor-intensive tasks by putting technology at their service, thereby creating a more productive market.” □