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ECONOMIC VIEWPOINT
By Jeffrey E. Garten

The Big Board Shouldn't Become Just Another Company

The reopening of the New York Stock Exchange on Sept. 17, after just four days of closure, epitomized the defiant spirit of global capitalism that the terrorists wanted to destroy. It also ushered in a new era for the Big Board. Before the attacks, the NYSE was considered by many to be just one of several exchanges hammered by competitive pressures. The conventional wisdom was that it should become a publicly listed company, do away with its floor traders, and become a fully automated system. But now, the world has changed, and we need to view the NYSE through a different lens.

Since the late 1990s, chronic global financial crises and the spectacular crash of technology stocks were leading to a recalibration of the balance between unfettered global capital markets and the need for more oversight, tighter regulation, and higher ethical standards. The free market had become a free-for-all. September 11 tipped the scales: In place of unbridled enthusiasm for deregulation, there is now a preoccupation with our vulnerability to disruptions and wild market swings. Public institutions need to be shored up rather than torn down.

It follows that at the heart of global markets we need organizations with the unquestioned stature and integrity that no purely commercial entity can guarantee. The NYSE stands alone among stock exchanges as a candidate for such status. It plays a far more critical role in the global market than does Nasdaq or the new electronic exchanges. After all, its listings include 90% of the nation's largest 100 companies. It is attracting nearly all of the highest-quality Asian and European global corporations, from Toyota Motor Corp. (TM) to Deutsche Bank (DB). And when there is a financial crisis, such as the 1987 stock-market crash or the 1998 Long-Term Capital Management fiasco, or September 11, it is the chairman of the NYSE who is called upon to sit with top officials from Wall Street and Washington. The Big Board has become the most visible emblem of Wall Street's global role.

HOLDING THE FLOOR. The NYSE must therefore be seen not as just another organization in the broad panoply of trading venues around the world. Instead, it should be thought of as a private institution with a public purpose, one with special national and international status.

Consequently, the concept of the NYSE as a public company that puts its shareholders' interest above all else has been overtaken by events. Why? First, the NYSE maintains spare trading capacity of more than 100% of peak loads for unpredictable crises. Second, more than one- third of its employees are involved in the exchange's self-regulatory functions. These essential costs are incompatible with what shareholders demand for quarterly profits.

In addition, the floor-based trading model should be preserved. In fact, 92% of all trades no longer touch a floor broker anyway. But as was shown during the market break of 1987, and again during the week of Sept. 17, in times of crisis floor traders and specialists can facilitate a more orderly market by buying and selling at critical junctures. No wonder sophisticated investors gravitate toward the NYSE in times of turbulence. During the week of Sept. 17, for example, the Big Board's share of large block trades, those transacted by the most sophisticated investors, jumped to 90.3%, compared with the normal 78.8%.

EMERGENCY HOME. What to do? While the NYSE has made progress toward fulfilling its public responsibilities, it should redouble efforts to be the platinum standard for both self-regulation and for the accounting and corporate-governance systems of the companies it lists. Half of its board of directors should unambiguously represent the public interest--not just those of Wall Street and Corporate America--and should be selected by an independent blue-ribbon group established by Congress.

NYSE Chairman and CEO Richard Grasso has been superb, but there's no assurance that his successors will measure up. Therefore, only the independent directors representing the public interest should be involved in picking future chairmen. To fill the post, they should reach for people who embody the standards of leaders, such as the chairmen of the Federal Reserve and the Securities & Exchange Commission. Finally, Washington ought to consider financing the physical security needs of the NYSE, including an alternative site for emergencies, not as a subsidy for New York City but in support of a vital American institution.

Of course, the NYSE must remain competitive. But it has more than held its own these past five years by maintaining market share of 83% to 85% in the trading volumes of the companies it has listed. It must also be able to afford excellent technology and talent. Acting as a private company, however, it has still been able to marshal the resources to do this, even in the expensive 1990s.

Out of crises can come important decisions. Elevating the NYSE in the landscape of our national institutions should be one of them.

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