**Explain this as if I am a 10 yr old: "The aim of the game is to profitably make markets. This means providing liquidity at the best prices at volumes large enough to facilitate the trading activity of other market participants. Your success will lie in identifying profitable opportunities to trade at fair prices, place your orders as quickly as possible, and keep your risk exposures below defined bounds." Explain in depth if necessary.**

Imagine you're in a big marketplace where people buy and sell things like fruits and vegetables. Some people want to buy more of something, and some people want to sell what they have.

In this game, you get to be one of the sellers in the marketplace. Your goal is to sell things at a good price to people who want to buy them. But you also want to make sure that there are enough people buying and selling, so everyone can get what they want.

To do this, you need to pay attention to what other sellers are doing and what buyers are looking for. You want to offer things for sale at a fair price that people are willing to pay. And you want to make sure you have enough of what people want to buy, so they don't have to go to other sellers.

But, just like in the real marketplace, there's a risk involved. Sometimes, you might not be able to sell everything you have, or you might not be able to sell it at the price you want. So you need to be careful and not take too many risks.

Overall, if you can sell things at a good price, have enough to sell, and manage your risks well, you'll be successful in this game.

**What is market making. Explain through example.**

Market making is the process of providing liquidity to financial markets by buying and selling securities or other financial instruments. In other words, market makers are the middlemen between buyers and sellers in financial markets, and their job is to facilitate trading by providing continuous quotes for buyers and sellers to trade against. Here's an example to illustrate how market making works:

***“****Let's say you want to buy shares of Company A, which is listed on the stock exchange. You place an order to buy 100 shares at $10 per share. At the same time, there is another investor who wants to sell 100 shares of Company A at $10 per share. Without a market maker, you and the other investor would need to find each other in the market to complete the trade. This could be difficult and time-consuming, especially if there are many other buyers and sellers in the market.*

*However, with a market maker, the process is much smoother. The market maker stands ready to buy or sell shares of Company A at all times, providing a continuous bid-ask spread for the stock. In this case, the market maker might offer to buy shares of Company A at $9.95 per share and sell shares at $10.05 per share. When you place your order to buy 100 shares at $10 per share, the market maker would sell you those shares at $10.05 per share, making a profit of $0.10 per share (the difference between the bid and ask prices).*

*In turn, if another investor wants to sell 100 shares of Company A at $10 per share, the market maker would buy those shares at $9.95 per share, making a profit of $0.05 per share (again, the difference between the bid and ask prices). By providing liquidity to the market and profiting from the bid-ask spread, the market maker helps to ensure that there is always someone available to buy or sell shares of Company A, which in turn helps to keep the market efficient and fair for all participants.****”***

**In the provided example, If I want to buy 100 shares of Company A at $10 each, and market maker is selling those 100 shares for $10.05 per share, why would I purchase?**

Good question! In the example I provided, the market maker is selling shares of Company A at a higher price than your bid price of $10 per share. This means that you would have to pay more than what you initially wanted to pay in order to buy the shares.

However, it's important to understand that the market maker's role is to provide liquidity and ensure that there are always buyers and sellers in the market. In other words, they are there to facilitate trading activity, and as a result, they need to be able to buy and sell shares quickly and efficiently.

In this case, the market maker may be selling shares of Company A for $10.05 per share because that is the price at which they are able to sell the shares to other buyers in the market. If you really want to buy the shares and there are no other sellers in the market at $10 per share, then you may choose to buy the shares at the market maker's offer price of $10.05 per share in order to ensure that you can buy the shares you want.

However, it's also important to note that you don't have to buy the shares at the market maker's offer price if you don't want to. You could choose to wait and see if another seller comes into the market who is willing to sell shares at a lower price, or you could adjust your bid price to match the market maker's offer price if you really want to buy the shares quickly. Ultimately, it's up to you to decide whether or not you want to buy the shares at the market maker's offer price, based on your own assessment of the market and your investment goals.

**What if the market maker itself doesn't hold the shares of Company A?**

If the market maker doesn't hold the shares of Company A, they may still be able to facilitate the trade by borrowing or obtaining the shares from other sources. For example, the market maker could have agreements in place with other firms or investors who hold shares of Company A, allowing them to borrow or obtain the shares when needed.

Alternatively, the market maker could use a process called "naked short selling" to facilitate the trade. Naked short selling is a controversial practice in which the market maker sells shares of Company A that they do not currently hold, with the intention of buying them back at a later time to cover the short position. This can help to provide liquidity and facilitate trading, but it can also be risky and may lead to market manipulation if done improperly.

In either case, the market maker would still be able to provide liquidity and facilitate trading in the market, even if they don't hold the shares of Company A themselves. However, it's important to note that these practices can be complex and may involve significant risk, so market makers must carefully manage their positions and adhere to regulations to ensure fair and efficient trading for all market participants.

**Explain this as if I am 10 year old with example "To attract market makers to their market, the exchange has agreed to provide incentives and services as described below. Each trade attracts a small fee paid to the exchange. In the Ready Trader Go ETF market, the aggressor in a trade pays the taker fee, which is 2bps, or 0.02% of the value of the trade. However, to incentivize market making the exchange pays the initiator of the passive order in the trade a maker fee – 1bp or 0.01% of the value of the trade."**

Imagine you have a lemonade stand, and you want to sell as much lemonade as possible. You know that your friends like your lemonade, but you want to attract more customers who don't know about your stand yet. So, you decide to offer them a special deal to encourage them to buy from you.

The exchange works in a similar way. They want to attract people who want to buy and sell things like stocks or ETFs (which are like special packages of stocks). One way they can do this is by offering special deals, or incentives, to people who want to trade on their exchange.

In this case, the exchange charges a small fee for every trade that happens on their exchange. This fee helps to pay for the services and technology that the exchange provides to make trading possible. The person who makes the trade pays a small fee, which is called the taker fee.

But, the exchange also wants to encourage people to be "market makers". A market maker is someone who is willing to buy and sell stocks on the exchange all the time, to help keep the market active and the prices stable. So, the exchange offers a special deal to market makers. If someone is a market maker and they put in an order to buy or sell a stock, and someone else comes along and takes them up on that offer, the exchange will actually pay them a small fee, which is called the maker fee.

Think of it like this: If you were a lemonade stand owner and wanted to encourage more people to come and buy your lemonade, you could offer your friends a special deal where they get a free cup of lemonade for every cup they buy. This would encourage your friends to buy more lemonade from you, and they might even tell their other friends about your lemonade stand. In the same way, the exchange is offering special deals to market makers to encourage them to trade on their exchange, which can help to keep the market active and attract even more traders in the future.

**Who is an aggressor in trading domain. Also give an example.**

In the context of trading, an "aggressor" is a term used to describe a market participant who initiates a trade by placing a new order that "crosses the spread" in the market. This means that the aggressor's order matches immediately with an existing order on the other side of the market, resulting in a trade.

To understand this better, let's take an example. Suppose there is a stock called ABC Inc. that is currently trading at $50 per share. The current market for ABC Inc. has a bid price of $49.95 and an ask price of $50.05. The bid price is the highest price a buyer is willing to pay for the stock, while the ask price is the lowest price a seller is willing to accept.

Now, let's say a market participant wants to buy 100 shares of ABC Inc. at the current market price. If they place an order to buy at the ask price of $50.05, their order will match immediately with an existing order to sell at that price. In this case, the market participant is acting as the aggressor because they initiated the trade by placing an order that crossed the spread.

On the other hand, if the market participant instead places an order to buy at a lower price, say $49.90, their order will not match immediately with an existing order in the market. Instead, their order will sit on the order book until a seller is willing to sell at that price, or until the market moves to meet their order.

So, in short, the aggressor in trading is the market participant who initiates a trade by placing an order that crosses the spread in the market.

**Define ETF formally and then explain with example.**

An Exchange Traded Fund (ETF) is a type of investment fund that is traded on stock exchanges, much like individual stocks. ETFs are made up of a basket of underlying assets, such as stocks, bonds, or commodities, and are designed to track the performance of a particular index or sector of the market.

ETFs are structured as investment companies and are subject to regulation by the Securities and Exchange Commission (SEC). They are created when an authorized participant, typically a large financial institution, assembles a portfolio of securities that match the composition of the desired index or sector, and then trades this portfolio with the ETF provider in exchange for shares of the ETF. These shares can then be bought and sold by individual investors on the stock exchange throughout the trading day.

To explain this further, let's take an example of a popular ETF called SPDR S&P 500 ETF (SPY). This ETF is designed to track the performance of the S&P 500 index, which is a benchmark index that measures the performance of the 500 largest publicly traded companies in the United States. The underlying assets of the SPY ETF consist of stocks of the companies included in the S&P 500 index, in the same proportions as the index itself.

When an investor buys shares of the SPY ETF, they are effectively buying a piece of the entire S&P 500 index, as the ETF is designed to track the performance of the index. Similarly, if an investor sells shares of the SPY ETF, they are effectively selling their exposure to the entire S&P 500 index.

ETFs offer a number of benefits to investors, such as diversification, liquidity, and transparency. They also have lower fees compared to actively managed funds, making them an attractive option for investors who want to passively invest in a particular index or sector of the market.

**Child Definition:**

**What are indexes. Give some examples and explain as if i am a 12 year old.**

Indexes are a way to measure the performance of a group of similar things, like stocks, bonds, or other assets. Think of it like a scorecard that shows how well a team is doing in a game, but instead of a team, an index tracks the performance of a group of assets.

For example, let's say you want to know how well the stock market is doing overall. One way to measure this is to look at an index like the S&P 500. The S&P 500 is an index that tracks the performance of the 500 largest publicly traded companies in the United States. When the stock prices of these companies go up, the value of the index goes up, and when they go down, the value of the index goes down.

Another example is the Dow Jones Industrial Average, which is another popular index that tracks the performance of 30 large, publicly traded companies in the United States. The Dow is calculated by adding up the stock prices of these 30 companies and dividing by a number called the "Dow divisor".

**DOUBT**

**In the example above for Dow Jones Industrial Average, are the 30 publicly traded companies fixed?**

The 30 companies included in the Dow Jones Industrial Average are not fixed forever but fixed for a considerable amount of time. The composition of the index can change over time as companies are added or removed based on certain criteria.The selection criteria for the Dow Jones Industrial Average are based on a number of factors, including the company's size, industry, and reputation. The index is intended to represent a broad cross-section of the U.S. economy, so the companies included are often large, well-established firms that are leaders in their respective industries.

Changes to the index are made periodically to reflect shifts in the economy and business landscape. For example, in 2020, three new companies were added to the index to replace three companies that were removed. These changes were made in order to better reflect the current state of the economy and to ensure that the index remains relevant and representative of the U.S. stock market.

**DOUBT**

**Does that mean it includes top 30 performing companies?**

No, the Dow Jones Industrial Average (DJIA) is not designed to track the top 30 performing companies. Instead, it aims to represent a cross-section of the U.S. economy by including 30 large and well-established companies that are leaders in their respective industries. Same goes for S&P 500.

**DOUBT**

**Then which index include only limited but top performing organizations?**

There are several indices that track limited but top-performing organizations. These indices typically focus on specific sectors or industries, rather than trying to represent the entire stock market.

For example, the NASDAQ-100 index tracks the performance of the 100 largest non-financial companies listed on the NASDAQ stock exchange, which tend to be in the technology and healthcare sectors. This index is often used as a benchmark for growth-oriented investments.

Similarly, the Russell 2000 index tracks the performance of 2,000 small-cap companies in the U.S. stock market, which are generally considered to be more volatile but potentially higher-growth than larger companies. This index is often used as a benchmark for small-cap and value-oriented investments.

Yes, that's correct ( What you are thinking ). The companies included in the NASDAQ-100 index are not fixed, but are selected based on their market capitalization, trading volume, and other criteria. The index is reconstituted annually to ensure that it continues to reflect the performance of the 100 largest non-financial companies listed on the NASDAQ stock exchange.

**DOUBT**

**On the financial dashboards why does a person only sees single price for the stock if there are multiple ask and bid prices for the same stock?**

When you view a stock on a financial dashboard or other trading platform, you will typically see a single price quoted for the stock. This price is usually referred to as the "last traded price" or "last price," and it represents the price at which the most recent trade in that stock took place.

The reason why you don't see multiple ask and bid prices on the dashboard is because these prices are constantly changing as buyers and sellers place orders in the market. The ask price represents the lowest price at which someone is willing to sell a stock, while the bid price represents the highest price at which someone is willing to buy a stock. These prices are not fixed, but can fluctuate rapidly as market conditions change.

To make it easier for investors to track the price of a stock, financial dashboards typically display the last traded price as an up-to-date snapshot of the market. This price can change frequently throughout the trading day as new trades are executed, but it provides a useful reference point for investors who want to monitor the performance of a particular stock. However, if you look at the order book for a particular stock, you can see the current bid and ask prices as well as the volume of shares available at each price level. This can give you a more detailed view of the market for that stock, and help you make more informed trading decisions.

**Pairs trading:**

Pairs trading is a type of market-neutral strategy that involves identifying two securities that have a historically strong correlation and taking a long position in one security and a short position in the other security when they diverge from their typical relationship. Here's an example of pairs trading:

Let's say you have identified two technology companies, Company A and Company B, that are in the same industry and have a historically strong correlation in their stock prices. You have noticed that over the past year, Company A has outperformed Company B and their stock prices have diverged from their typical relationship.

To implement a pairs trading strategy, you would take a long position in Company B and a short position in Company A. If the relationship between the two companies returns to its historical pattern, you could potentially profit from the convergence of their stock prices.

For example, let's say you take a long position of $10,000 in Company B and a short position of $10,000 in Company A. If Company A's stock price falls by 5% and Company B's stock price rises by 3%, you would have a net profit of $800 (3% increase in Company B - 5% decrease in Company A) on your trade.

Pairs trading can be a complex strategy that requires careful analysis and risk management, but it can be a useful tool for investors looking to generate returns in a volatile market while reducing overall market risk.