HMRC - STSM124040 - Market Makers

In the UK a principal broker dealer may also apply to the London Stock Exchange (LSE) to register as a market maker in particular shares. The market maker has to register on a share by share basis and for larger companies there may be several market makers competing with each other for business.

The role of a market maker is to ensure that there is always “a market” in which investors can buy and sells shares in the companies for which they are a market maker for.

The principal obligation of a market maker is to publicly quote a two-way price per share for each share they are registered as a market maker for. In the UK this is done using a computerised screen based Stock Exchange Automated Quotation System (SEAQ). (SeeSTSM122020).

For example, a share might be priced at:

240p - 244p

The lower price (240p) is called the bid price and is the price at which the market maker will buy the share from other brokers. The higher price (244p) is the offer price, the price at which the market maker will sell the shares to other brokers.

The difference between the bid and offer prices is called the ‘spread’ and this is the basis of the market maker’s profits.

Having made an investment decision a broker will undertake the deal with the market maker over the telephone. Market makers are obliged to deal whenever requested by other brokers and cannot refuse a transaction.

In return for accepting the obligations of acting as a market maker firms gain the following privileges:

Only market makers are allowed to input prices on SEAQ

They are exempt from SD/SDRT on purchases

They are able to borrow securities to cover short term positions through the stock exchange money brokers

They have access to the inter-dealer broker network which allows them to buy and sell large volumes of securities anonymously

Market makers may also use the SETS system (STSM122020) to place orders to buy shares.

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