FINANCIAL TIMES
FRIDAY OCTOBER 10 2003

MAURICE GREENBERG

Shake up the NYSE specialist system or drop it

The first job of chief executives is to provide value for their shareholders. But no matter how profitable a company is, its investors will not share fully in the rewards of equity ownership if the market where they buy and sell their stock is not fair, efficient and transparent.

The New York Stock Exchange is the world's largest and most successful equities market. But it relies on a specialist system for executing trades that does not, in my opinion, always work in the best interests of investors, especially investors in large-capitalisation stocks.

Each company listed on the NYSE has one specialist firm whose job is to maintain a fair and orderly market in the company's stock. In theory, the specialist does this by matching buyers and sellers and, when buyers and sellers are unable to agree on price, it provides liquidity and reduces volatility by committing its own money to buy shares of stock. If companies believe that their specialists fail to perform this role as required under NYSE rules, they have an obligation to their shareholders to speak out. If that does not work, we should consider changing the structure of the system.

I have been critical of the specialist system for some time – before, during and after my tenure on the NYSE board of directors. Concerns about this system led to the creation of a board subcommittee on the role of the specialist, which I chaired. This subcommittee recommended that the NYSE's listed companies committee should regularly conduct an audit to make certain that the specialist trading system is operating fairly and efficiently.

When evaluating the effectiveness of the specialists in maintaining efficient and orderly markets, a number of concerns need to be dealt with.

> If the specialist cannot effectively perform his role, then we need to look for alternatives including the electronic matching of buyers and sellers, with no human intervention

First, a specialist should have no opinion as to the future direction of a stock. The specialist's job is to buy shares when investors are selling and sell shares when investors are buying. By making a ready market he reduces unnecessary violent swings in prices that are detrimental to the interests of both buyers and sellers and undermine the confidence of the investing public.

Second, the capital requirements for the specialists should be sufficient to enable them to maintain their effectiveness as market makers. For example, when AIG first listed on the New York Stock Exchange in 1984, our market capitalisation was approximately $5bn. Today our market cap is approximately $160bn and we have more than 2.6bn shares outstanding. In order to make an efficient and orderly market in AIG stock today, the specialist must have capital commensurate with the size and the activity of the stock in which he is making a market. Furthermore, he must be prepared to use it. However, I believe that specialists have not consistently been committing the capital required to maintain orderly markets in large-cap stocks. If the specialist cannot effectively perform his role, we need to look for alternatives including electronic matching of buyers and sellers, with no human intervention.

Last, the vertical integration of specialist firms into investment banks that underwrite, trade and invest in these same stocks requires careful scrutiny. There are serious potentia l conflicts when one company is engaged as a specialist in a stock while the same firm is underwriting, trading or investing in that same ompany's securities. The Chinese wall must be unbreachable and the separation clearly evident to market participants.

Every chief executive has a duty to his company's shareholders to make certain the specialist is making a fair and efficient market in the company's securities. If a CEO believes the specialist is not doing his job according to the applicable laws and regulations, he must speak out to the specialist as well as to the management of the stock exchange, which has the ultimate responsibility for assuring orderly markets.

Since AIG listed on the NYSE in 1984, I have not hesitated to try to ensure that AIG shareholders have a level playing field. I have regularly contacted our previous and present specialist firms, as well as Goldman Sachs, the owner of our present specialist firm. In addition, I have contacted the chairmen of the NYSE, both Richard Grasso and his predecessors. I shall continue to do so while John Reed is chairman and after his successor is named. The specialist system must be made to work as it was intended to, or we must find an alternative system that will operate in the best interests of shareholders in the 21st century.

The writer is chairman and chief executive of AIG