

Front running is the practice of entering into a trade based on advance knowledge of pending orders, typically to capitalize on the price movement those orders may cause.

## **Key Points**

1. Often considered unethical or illegal, especially when done by market makers or brokers

2. Can affect market liquidity and fairness

3. Different from legitimate anticipatory trading based on public information

# **Types of Front Running**





• Trading ahead of a known client order

#### 2. Electronic Front Running:

 Using high-speed systems to detect and act on order flow information

#### 3. Insider Trading (a form of front running):

• Trading based on non-public material information

## How Front Running Works



1. Obtain information about pending large orders



2. Enter a position in the same direction before the large order is executed



3. Exit the position after the large order moves the market

## Impact on Markets

- 1. Can lead to worse execution prices for large orders
  - 2. May reduce market liquidity
  - 3. Erodes trust in market fairness

## **Detection and Prevention**



#### 1. Regulatory surveillance:

Monitoring trading patterns for suspicious activity

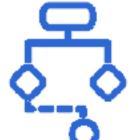


#### 2. Time-stamping of orders:

To track the sequence of trade executions



3. Ethical guidelines and compliance training for market professionals



4. Use of algorithmic trading to disguise large orders

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### Legal and Ethical Considerations

- Front running is illegal when done by brokers with client order information
  - It's a grey area for traders using publicly available information
- Ethical traders should avoid any practices that unfairly disadvantage other market participants

### **Tips for Traders**

- Be aware of potential front running when placing large orders
- Consider using algorithms or splitting large orders to minimize impact
- Report any suspicious trading activity to regulatory authorities