ASIC
Australian Securities & Investments Commission

Pump and dump of micro-cap securities

Report 732 | July 2022

About this report

This report summarises our review of a series of pump and dump events that occurred in listed equity markets over 2020–21. These events had a high impact on the traded prices of micro-cap securities.

This report also sets out good practices to help market participants detect, prevent and respond to pump and dump activity.

Contents

'We observed a spike in disruptive trading in the listed securities of smaller capitalised companies during 2020–21. We quickly intervened, disrupted the misconduct and are taking action to hold these individuals to account.'

Danielle Press | ASIC Commissioner

About ASIC regulatory documents

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Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations. Examples in this report are purely for illustration; they are not exhaustive and are not intended to impose or imply particular rules or requirements.

Overview

ASIC observed an increase in unusual price moves of micro-cap securities in 2020–21. We reviewed this activity, assessed market impact and intervened to disrupt trading and social-media-led campaigns influencing share prices.

Our observations

Some short-term traders targeted and exacerbated high volatility in micro-cap securities

We analysed market activity, investor behaviour and social media from January 2019 to July 2021 (the review period) and observed:

- a marked increase in anomalous price moves in the market
- elevated interest in small and micro-cap securities
- significant increases in day trading.

The anomalous price moves were most prevalent in less-liquid securities capitalised between $7 and $20 million and priced below 37c.

Pump and dump events drove some price moves

We found the anomalous price moves were sometimes driven by pump and dump events in the form of momentum ignition and organised campaigns on social media.

Momentum ignition: Trading accounts targeting volatile micro-cap securities tended to trade through large online retail brokers. We also identified a small number of aggressive day-trading accounts targeting company disclosures by micro-caps, which amplified intraday price movements. In many cases, it appeared that individual traders accounted for 30% of a targeted security's turnover.

Social media campaigns: We saw a marked uptick in 2021 of social media platforms being used to promote coordinated trading in illiquid securities. Social media commentary of micro-cap securities did not show a balanced or temperate view of investment risks being offered. Rather, online commentary was overwhelmingly positive and tended to express strong support for the securities discussed.

Retail investors were affected

Momentum ignition, coupled with high volatility, may have led to losses of $6.3 million per month for retail investors over the review period.

We also found that 81% of accounts that participated in organised social media pumps realised a financial loss or zero benefit.

Our response

We worked closely with the listing market, the Australian Securities Exchange (ASX), and market participants to identify and disrupt pump and dump activity. Market operators paused trading and market participants closed suspected client accounts. ASIC issued warnings on social media forums and has instigated action against perpetrators.

We also published Information Sheet 269 *Discussing financial products and services online*, which outlines how financial services laws apply to online commentary of shares and share trading.

Our expectations of market participants

Market participants are the gatekeepers to Australian markets. They should take note of the findings of our review and implement the good-practice expectations outlined on page 9.

Changes in investor behaviour

We profiled trading across the market and catalogued accounts by size and behaviour. Our review identified increased investor interest in short-term trading.

A combination of COVID-19 pandemic stay-at-home orders, low market prices and a hunt for yield triggered intense retail interest in Australian equity markets. **We observed a surge in retail participation across all capitalisation segments of the Australian equity market from pre-pandemic levels**.

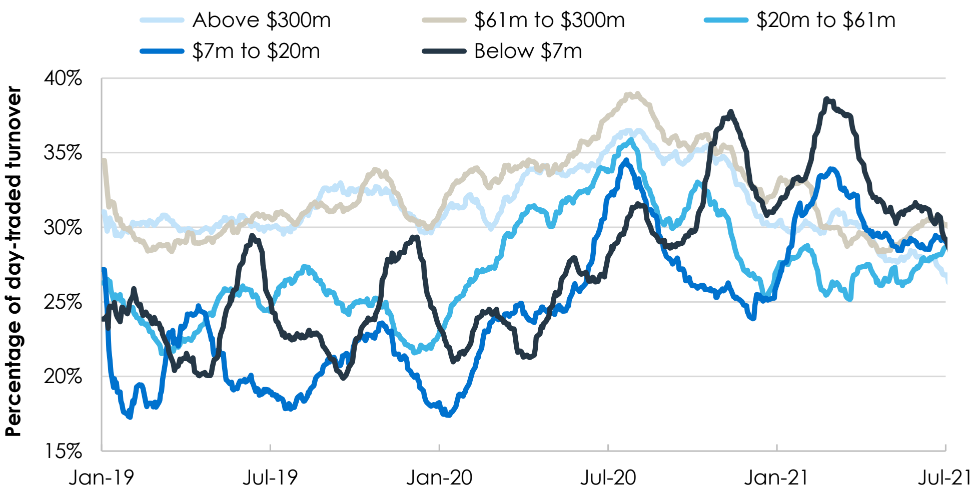
This elevated retail interest pivoted to micro-cap securities over the latter half of 2020. **By the end of 2021, retail activity at the smaller, and more speculative end of the market, had increased three-fold** (see Table 1).

Table 1: Average number of retail accounts active in the listed equity markets across five equal-sized partitions of market capitalisation

Capitalisation range of listed securities	2019	2020	2021
Above $300m	21,244	39,063	39,742
$61m to $300m	11,140	19,454	19,748
$20m to $61m	7,115	13,800	13,951
$7m to $20m	6,583	11,919	17,246
Below $7m	11,776	22,422	29,005

We also saw an increase in day trading, which peaked at 39% across the broader market in July 2020 (see Figure 1). Speculative trading of micro-cap securities lagged this trend by four months eventually reaching 38% in February 2021. Levels remained elevated against historical norms throughout 2021.

Figure 1: Our estimate of day trading in listed equity markets over the period January 2019 to July 2021



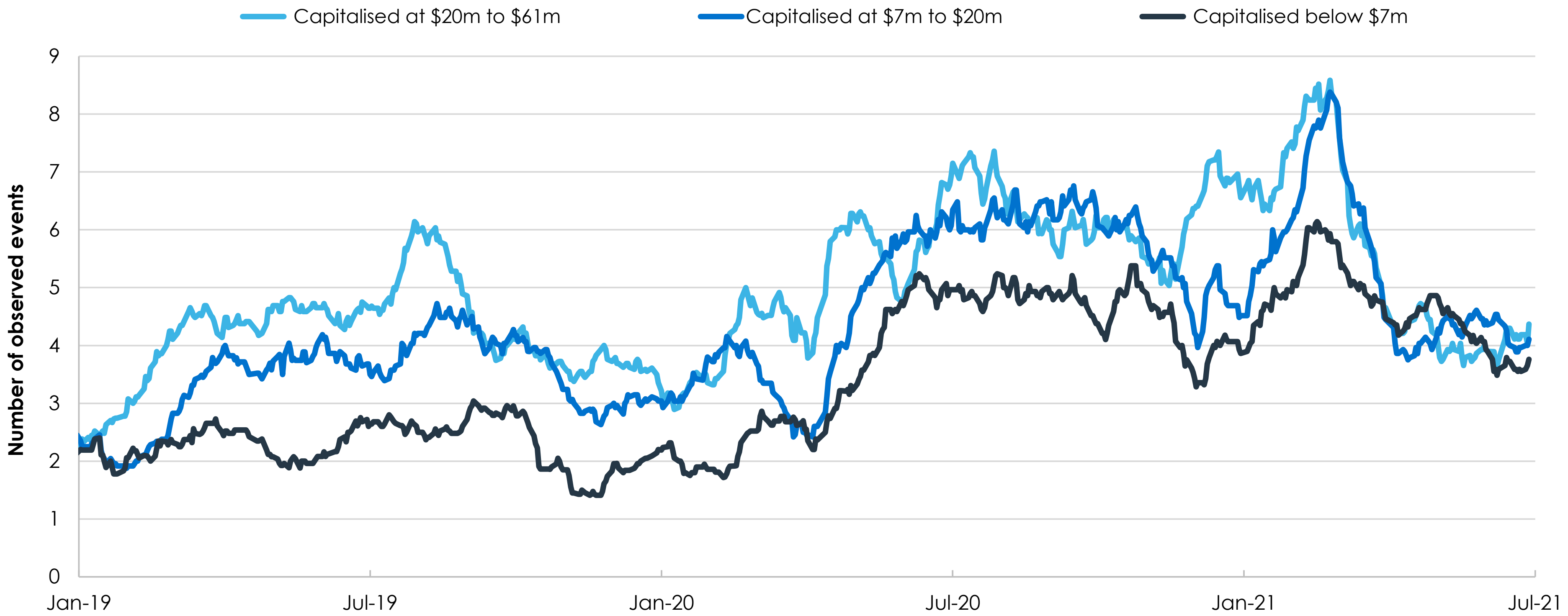
We believe that some retail day traders were alert to many of the speculative forces behind pumped securities. Day traders actively targeted micro-cap securities that had high levels of investor interest, increased volumes and extended trading ranges. Market orderbooks for pump and dump events, promoted over social media, were overwhelmingly populated by retail day traders before market open.

Driving factors: Pump and dump events

We analysed the activity of trading accounts in relation to price moves and reviewed social media. We found that two of the driving factors behind some of the observed anomalous price moves in micro-cap securities were pump and dump events in the form of **momentum ignition** and **organised social media campaigns**.

The estimated number of potential pump and dump events we observed over the review period trended upwards over 2020 and peaked in early 2021 (see Figure 2).

Figure 2: Estimated number of potential pump and dump events in the listed equity market per day between January 2019 and July 2021



Note: Our estimate is constrained to the lower three quintiles of market capitalisation.

Momentum ignition

We analysed trading to determine which accounts day traded micro-cap securities when their market prices traded over anomalously large price ranges. We also analysed how that trading occurred.

We identified a number of individual accounts that tended to appear in the trading schedule when markets were unusually volatile. Overwhelmingly these traded through larger retail brokers offering electronic online access.

A number of institutional and high-frequency trading accounts were also consistently present, however these accounts did not appear to target or drive the potential pump and dump events collected through our analysis. Therefore, our analysis focused on other account activity.

Some of the individual accounts that we identified regularly traded the same securities at the same time. These accounts tended to submit resting orders onto the orderbook, purposefully targeting the larger spreads of low-value securities with unusually large investor interest.

A smaller ring of aggressive traders were suspected of initiating concurrent purchases and sales to entice interest from other investors.

A small number of individual professional traders regularly targeted micro-cap securities through aggressive, high-impact, short-term and non-algorithmic day-trading strategies. In many cases, it appeared that individual traders accounted for 30% of a targeted security's turnover and gave a false impression of true market demand. These traders ran high-risk strategies that accommodated large profit-and-loss swings.

They appeared to test and then leverage positive sentiment to encourage third-party trading to promote excessive price swings.

We observed traders submitting orders to move market prices, one-sided layering of the orderbook and the timely removal of priority bids to avoid trading.

All identified accounts submitted orders manually to the market using automated order processing systems. We did not identify algorithmic traders regularly engaged in momentum ignition over the review period.

Where ASIC identifies concerning conduct or contraventions of the law, we may take enforcement or other action to change behaviour and improve market integrity. We may seek punitive actions such as imprisonment or financial penalties. We may pursue a negotiated outcome that discourages further access to financial services. Our regulatory tools scale to the nature of the harm identified.

What is momentum ignition?

Momentum ignition is the practice of aggressive purchasing by one or several accounts to have a significant impact on price and encourage other traders to participate in the buying activity. This activity further impacts the price of the underlying security.

This type of trading strategy can result in allegations of market manipulation when participants facilitate high-impact strategies in low liquidity securities that increase volatility, reduce market integrity and harm investors.

Social media campaigns

We analysed social media commentary about Australian equities and market activity. We connected social media pseudonyms to trading accounts and identified market sales that profited from surging markets.

We found that promoters, across a range of platforms, encouraged their followers to engage in coordinated purchases and sales of low liquidity securities susceptible to market impact. Followers were motivated by the potential for trading profits in manipulated markets.

We observed multiple instances of coordinated retail order flow into the pre-open markets of targeted securities on the announced days. The organisers would announce over social media a security to be traded. Coordinated demand would push up the pre-open and traded price of targeted securities before a surge of selling liquidated traded positions. Promoters pre-positioned themselves before the announcement and sold early, into the demand, for a profit.

Approximately 81% of all participating day-trading accounts lost money or broke even in these events. Market operators paused trading in some securities, and we identified follower accounts seeking to profit from market distortions.

Our analysis of the conduct of promoters of social media pumps suggested that they may have been engaged in market manipulation.

In response, we issued warnings on social media forums and instigated action against perpetrators. We have also taken steps to discourage the use of social media to promote potential misconduct (see list on right).

To discourage pump and dump events on social media, we are:

- **Monitoring social media for potential misconduct and tracking potential organisers**
- **Proactively engaging with market participants to identify offending clients and reporting potential abuses to the social media platforms**
- **Engaging directly with participating audiences over social media platforms**
- **Enforcing orderly markets by working with ASX to halt trading in targeted securities**

How investors were affected

Momentum ignition and pump and dump trading activity undermine the capacity of markets to efficiently price risk and allocate capital. Such activity lowers the quality of investor outcomes and can damage confidence in markets.

Excessive volatility can create financial harm when investors enter risk positions at inflated price points. Alternatively, more astute investors may utilise rapid price rises to exit positions.

We found that investors (or accounts that did not day trade) could benefit from volatility but relative financial outcomes were sensitive to size. Smaller accounts appeared to handle greater price volatility poorly.

We tested the financial harm imposed on the smallest of these investor accounts (that is, accounts that traded less than $100,000 per day) over the trading events identified in our analysis. Greater volatility led to a much wider range of financial outcomes. In potentially pumped markets, 16% of all retail investors exiting intraday risk received a financial outcome that was $800 less than the equivalent end-of-day outcome. Across all other trading days the comparable rate was only 5%. **We estimated that retail investors exiting risk, over potentially pumped events, incurred a loss of $6.3 million per month.**

Table 2: Percentage of retail accounts that lost or made a benefit by trading against intra-day – rather than end-of-day – price levels

Retail marginal outcome	Normal market	In potential pumps
Lost more than $800	5%	16%
Lost more than $400	8%	27%
Made more than $400	12%	23%
Made more than $800	6%	16%

The largest losses across potential pump and dump events were suffered by accounts that only partially exited their intra-day positions. Disciplined day traders were more adept at managing short-term financial risk and amongst this cohort volatility did not favour size. The smallest day traders appeared to perform better as volatility increased.

Many of the securities pumped by social media specifically targeted low-capitalised micro-cap securities exhibiting limited liquidity. Normal trading in these securities was small and so trading over the pumps was essentially limited to the day traders themselves. Financial transfers were largely limited to profit and loss movements between the participating day traders.

Minimal long-term investor participation was noted over these organised pumps and so, given the small sizes and limited liquidity involved, the potential for wider financial contagion was constrained.

Our expectations of market participants

Market participants, such as brokers, play an important gate-keeping role in detecting and preventing pump and dump activity.

We found that some market participants failed to critically analyse, and report, potential misconduct of high-impact clients. We expect market participants to vet all client orders (either manually or using automated systems) and to follow the good-practice expectations outlined below.

Good-practice expectations for market participants:

Remain aware of indicators of potential pump and dump trading (see indicators on right)

Consider the circumstances of all orders against obligations in the Corporations Act and market integrity rules

Ensure monitoring and surveillance controls remain fit for purpose

Immediately stop and deter suspicious activity. Reject client instructions that may create a false market in a security and close disruptive client accounts

Report any suspicious activity through ASIC's regulatory portal or by email to markets@asic.gov.au

Indicators of pump and dump trading

- High impact day trading by clients, in micro-cap securities, responsible for a material portion of market turnover
- Day-trading clients that habitually remove market bids following the liquidation of trading positions
- Day-trading clients that layer a single side of the market orderbook with multiple orders while transacting in the opposite direction
- Clients placing multiple orders at the same price and then selectively removing the priority order
- Clients chasing the extremities of anomalous price moves in micro-cap securities with limited liquidity
- Any sudden or unusual surge in trading interest that cannot be explained by recent company disclosures, financial news or market events
- Excessive or unusual social media commentary highlighting micro-cap securities with limited liquidity or constrained price elasticity
- Market transactions, in illiquid securities, between related parties.

Key terms

anomalous price move	A movement in the share price that cannot be explained by fundamental factors or expected volatility
Corporations Act	*Corporations Act 2001*, including regulations made for the purposes of that Act
day trading	The purchase and sale of securities within a single trading session
high-impact trading	Trading that creates a material move in the quoted price of a listed security
market capitalisation	The total dollar value of a listed company, determined by its current market price
market integrity rules	Rules made by ASIC, under s798G of the Corporations Act, for trading on domestic licensed markets
micro-cap securities	Generally recognised as the collection of listed securities with a market capitalisation below US$300 million, although the actual range will vary. For example, the *MSCI Australia Micro Cap Index©* contains a basket of securities ranging from A$3 million to A$600 million. This report refers to securities with market capitalisations below A$61 million as 'micro-cap'
momentum ignition	The practice of aggressive purchasing by one or several accounts that has a significant impact on price, and that encourages other traders to participate in the buying activity
pump and dump	The practice of buying shares in a company and then organising a program that seeks to increase (or 'pump') the share price. This is done over social media and online forums to create a sense of excitement in a stock or spread false news about the company's prospects. The shares are then sold (or 'dumped') for a profit. Other shareholders suffer as the share price falls
review period	January 2019 to July 2021
small-cap securities	Generally recognised as the collection of listed securities with a market capitalisation between US$300 million and US$2 billion, although the actual range will vary. For example, the *MSCI Australia Small Cap Index©* contains a basket of securities ranging from A$40 million to A$8 billion