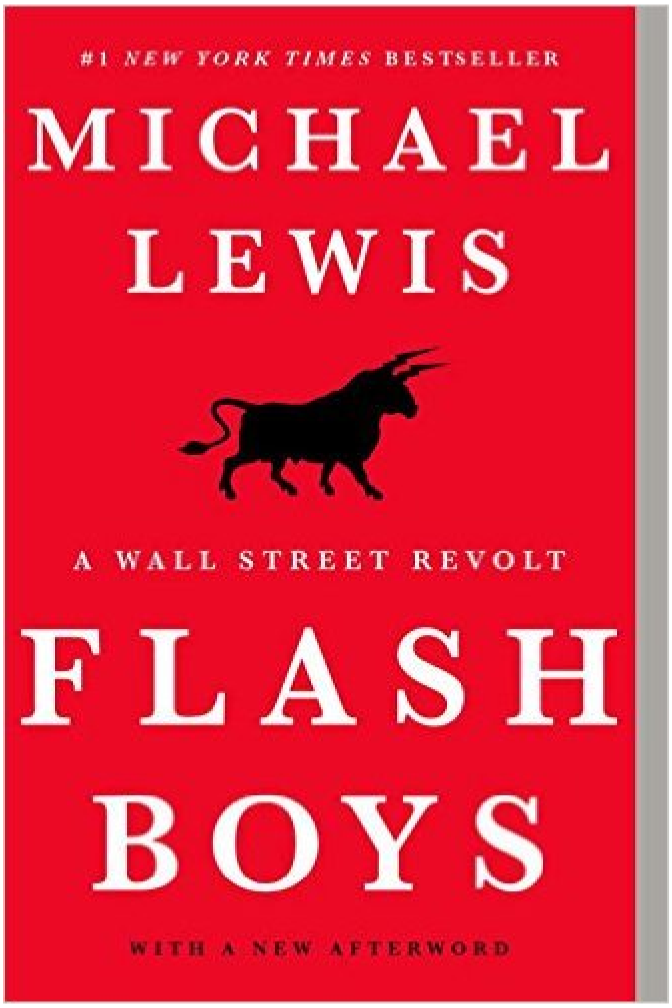
Flash Boys: A Wall Street Revolt



Synopsis

#1 New York Times Bestseller â • With a new Afterword"Guaranteed to make blood boil." â •Janet Maslin, New York TimesIn Michael Lewis's game-changing bestseller, a small group of Wall Street iconoclasts realize that the U.S. stock market has been rigged for the benefit of insiders. They band togetherâ •some of them walking away from seven-figure salariesâ •to investigate, expose, and reform the insidious new ways that Wall Street generates profits. If you have any contact with the market, even a retirement account, this story is happening to you.

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Customer Reviews

I retired from the hedge fund world and I can tell you that this book is mostly on target. For those who deny that HFT (high-frequency trading) is a rigged game, either they are un-informed or disingenuous.It wasn't always like this. There was a time, when a bid was a bid, and an ask was an ask. If you liked the ask, you could hit the buy button and have a buy order confirmed instantly. Likewise, if you liked the bid, you could hit it and have a sale order confirmed instantly. That instant used to be measured in seconds or less. Then came along the HFT algo. All of a sudden, a bid is no longer a firm bid, and an ask is no longer a firm ask. You can hit the bid, but instead of selling instantly, you now become the ask price, and the bid just got lowered by a penny or more, and the market is moving away from you. Most of the time, the price move is a head fake - an illusion, trying to get you to trade at a price with "scalping" built-in against you. If you are willing to stick around, the precise price you want will return and you can have your trade. But other times when execution really matters, it was all real, the price you were willing to trade at just got shifted permanently right before your eyes and somebody "front-run" you.I decided to retire, partly out of disgust, partly out of my lack of financial ambition. I learned a while ago, if the first million can’t make you happy, that you have to accumulate more, you will never be content. If you have to play the rigged game to add more riches to your money pile that most human beings will never see in their lifetime, I feel sorry for you. Life is too short for me to play that game.Addendum: This book was written for the lay person, so was my review. Sorry for not bandying about the jargons as some would expect, my bad. As much as I tried, I seem to have failed to write in plain English and draw the analogy to a functioning market. That’s where Michael Lewis’ book excelled, hence my recommendation. Granted, true free market doesn’t exist in the financial world (no matter where you look, New York/London/Chicago/Tokyo). Only the naive will expect any market to give all participants the same level of positioning to engage in any transaction. My favorite analogy is my local farmers’ market. When I show up to buy strawberries, some farmers/dealers have way more information on the supply and demand, and have inventory to reflect their view. They will rightfully make a profit when I buy the basket of strawberries from any of them. What I don’t want to see is some jerk get in the way and buy up all the strawberries just before I hand my money to the seller, then turn around and sell the strawberries to me as if he had been the seller all along. The price quoted at my farmer’s stand should be the price I can buy strawberries at, not a new price some jerk just jacked up to after seeing my intention to transact. I hope the description above clears any doubt about what this book is really about. It’s not about someone having some legitimate edge after doing extensive research, or illegitimate edge resulting from inside information. It is about the financial market must be well functioning and free of unnecessary intermediation. That said, still two thumbs up on the book! For those who deny the unfairness of HFT front-running, either you haven’t seen it (which should disqualify you from commenting on this topic) or you are so jaded that you can’t see its harm (which begs questions about your integrity). As for myself, still happily retired after a short stint in the world of finance, thank you very much! I never learned much and never enjoyed rattling off the jargons.

Michael LewisÃ¢Â Â™ new book Ã¢Â ÂœFlash Boys: A Wall Street Revolt,Ã¢Â Â• hit the top of The New York Times bestseller list a week after its release. As you would expect, the book is skilfully assembled and quite sensational. When I first started to read it, I too was convinced that Lewis was on to a big story, an important narrative about the seamy underside of Wall Street.But the more I read and, more important, the more I checked his story with my colleagues on the operations side of the financial markets, the more it becomes apparent that Lewis has missed the real story Ã¢Â Â“ and perhaps deliberately. The headline of Ã¢Â ÂœFlash BoysÃ¢Â Â• is about

Wall Street traders using fast technology and unfair tactics to trade ahead of retail investors Ã¢Â Â“ and they do Ã¢Â Â“ but Lewis misses the real issues, namely: 1) a lack of transparency and 2) deliberate complexity.It is important to distinguish between issues related to the Ã¢Â Âœflash crashÃ¢Â Â• of May 2010, when the deliberately fragmented ghetto that is the US equity markets almost melted down and the daily business of HFT. The former is discussed in an important 2011 paper by Ananth Madhavan of BlackRock, Inc. Unfortunately, as the title of his book confirms, Lewis combines the two issues together into an often confusing narrative that is almost impossible for laymen to understand.The abusive aspect of HFT which Lewis rightly identifies is not so much about the speed of the trading but rather always being first in line. If you think of the current market price of a stock, a couple of years ago, the trader using HFT used to sit just above and below the current market price, and sought to execute quickly when the market price either went up or down. The fact of computers and fast network connections enables this HFT activity, but it is not really the key part of the strategy. Instead the key is to always be first in line.The important part of the story that Lewis misstates is that there is no conspiracy, no illegal activities. All of the strategies used in HFT are not only legal, but they are the result of extensive rule making and public hearings by Congress, the Securities and Exchange Commission, FINRA and the major exchanges. So while Lewis is right to say that these strategies Ã¢Â ÂœscrewÃ¢Â Â• retail customers in a practical sense, the fact is that the activity has been entirely blessed by Congress, regulators and the major exchanges.In the first aptly named chapter, Ã¢Â ÂœHidden in Plain Sight,Ã¢Â Â• Lewis describes groups of traders attempting to conceal their activities, great stuff if your chief objective is to sell books. But the reality is that the top three HFT firms Ã¢Â Â“ Goldman Sachs, Morgan Stanley and Credit Suisse Ã¢Â Â“ have been very visibly investing in trading technology for decades. These investments in computers and fast network connections not only give them an advantage over other firms, but afford these firms bragging rights on the Street. If you are an equity trader, you donÃ¢Â Â™t want to work at a Ã¢Â Âœflow shopÃ¢Â Â• like Merrill Lynch.Part of the reason that the Big Media is making such a fuss over Ã¢Â ÂœFlash TradersÃ¢Â Â• is that they have no idea how the equity markets actually work in the brave new world of Reg NMS Ã¢Â Â“ 600 pages of unintelligible rules and definitions. Lewis notes that as the size of equity trades after 2000 Ã¢Â Âœhad plummeted, the markets had fragmented and the gap in time between the public view of the markets and the view of high frequency traders had widened.Ã¢Â Â• This passage and others give readers the false impression that the speed of the HFT is the key point, but this is incorrect.Going back to the point about being first in line, letÃ¢Â Â™s take an example. The BATS order type known as Ã¢Â Âœdisplay-price slidingÃ¢Â Â• allows an investor to essentially position themselves in the center of the equity market for a given stock. This means that when the market price changes, instead of the HFT Ã¢Â Âœmarket orderÃ¢Â Â• being canceled as per the National Best Bid and Offer (NBBO) rule, it simply Ã¢Â ÂœslidesÃ¢Â Â• to follow the market. Most investors and advisors donÃ¢Â Â™t even know that such an order type exists.For example, when Lewis talks about the fact that Virtu Financial had made money almost every day for five years, the reader is given the impression that the speed of the trading gave Virtu and other HFT shops the advantage. But the reality is that the high frequency trader not only executes before the retail customer, as Lewis describes, but is always first in line. This structural duplicity is programed into the system, but is perfectly kosher under Reg NMS.Indeed, the real scandal is that all of this has been entirely blessed by the SEC, FINRA and the major exchanges and is described in the voluminous public documentation for permitted order types. But suffice to say, virtually nobody in the Big Media or at most Wall Street firms understand any of this or knows, for example, that there are over 100 different order types allowed by the SEC and FINRA under current law and regulations.The crime of HFT is that Congress, the SEC and other regulators have allowed a handful of Wall Street firms to assemble a set of opaque market rules that few people understand. You could probably put all of the Wall Street operations people who really understand HFT in a large conference room. Outside of the small community of traders and operations people who make HFT work, almost nobody else on Wall Street really understand the nuances of the business. And virtually nobody at the SEC has a clue how this works in practice.We should thank Michael Lewis for using his celebrity and considerable writing skills to draw attention to this issue of HFT, but Ã¢Â ÂœFlash BoysÃ¢Â Â• incorrectly demonizes individual traders and firms. Lewis Ã¢Â ÂœPuts a Face on HFT,Ã¢Â Â• but in doing so misses the real point of the problem. Instead of drawing an accurate picture of HFT, namely corruption and stupidity in Washington, admittedly a banal and boring tale, Lewis chose instead to create a sensational and interesting fictional narrative that will obviously sell more books.Ã¢Â ÂœFlash BoysÃ¢Â Â• is a book written for Hollywood instead of the history books or policy makers. Just as the hyper-popular Ã¢Â ÂœWolf of Wall StreetÃ¢Â Â• was not an accurate portrayal of fraudster Tom Prousalis, as his daughter Christina testifies, the story line in Ã¢Â ÂœFlash BoysÃ¢Â Â• is more fictional dramatization than fact. The true perpetrators in Michael LewisÃ¢Â Â™ tale of Wall Street greed and corruption are, in order of complicity, the US Congress, the SEC, FINRA and major exchanges, and last but not least the community of Buy and Sell Side Advisors, who genuinely do not understand how HFT really works. That covers just about everybody.As illustrator Walt KellyÃ¢Â Â™s Pogo said famously: Ã¢Â ÂœWe have met the enemy and he is us.Ã¢Â Â•This review was published in Zero Hedge in April 2014: [...]

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