

Market Turmoil “Flash Crash”

On Thursday May 6th, the stock market took a dive of epic proportions. On this day between 2:30 and 3:00 p.m. the market dropped about 999 points. At approximately 1 p.m. the market Dow Jones Industrial Average (DJIA) was at 10,797 and at 2:46 p.m. it was at 9870. That move alone is well over 900 points down. This “Flash Crash”, as it’s called by many, was triggered largely by electronic trading exchanges. Unrest in Greece, which is still ongoing, caused this large increase in stock selling. When you have more sellers than buyers, or an over-supply, this will cause the price to drop. Some stocks such as Procter & Gamble trade on multiple exchanges. Its primary listing is on the New York Stock Exchange (NYSE), but it also trades in other markets such as the NASDAQ. When an extremely large number of sell orders hit the NYSE it can divert some to other markets to fill the order. Some other exchanges, that aren’t primary, have fewer bids for the stock (buyers), so the price of the stock plunges in a way to match up buyers and sellers. In a crude sort of way the price drops until people start to buy because it deemed cheap or a good deal.

These so called “Flash Crashes” are more common today as compared to even 10 years ago as so much of our trading is now electronic. Preset electronic parameters may actually worsen a situation as buy orders can be withheld if a stock price drops. These can be preprogrammed functions to automatically execute or not, in this case. This results in more sellers than buyers and ultimately having the stock plunge if this happens in a short period of time.

To try and combat this problem U.S. exchanges are implementing a tool called trading “Curbs” or “Circuit Breakers”. These sorts of things already exist but are being refined all the time. The goal is to put the brakes on a Flash Crash before it happens. Big companies will have a pause in trading if their stock price moves more than 10% in a five minute period. This pause would allow the exchanges time to find a match of buyers and sellers and keep liquidity in the security reasonable. Initially, this pilot program will run through the remainder of 2010. Things of this magnitude need to be addressed to keep confidence in domestic equity markets.

In general we have found that confidence is shaky, and investors are unhappy about two main things. The first is low stock prices and the second is historically low interest rates. We here at Superior National Bank & Trust do believe rates will rise and the stock market will rebound. When, is the million dollar question!!! We are advising our customers to be patient. Even though interest rates are historically low it is still a positive return on your money. Investors must remember that when they go after higher than market yields they are increasing their risk to intolerable levels. To understand your current risk levels or to review your account, simply call or stop in to see any of our three Trust Officers (Barb Luke, Greg Seppanen, or myself Chris Gariepy). If you currently have your account elsewhere, we invite you in to visit with us and see how we can be of service to you.

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July 9, 2010