Trading Spike Seen Just Before ADP Report

By STEPHEN L. BERNARD

Data from two independent sources show that trading in select currencies and future contracts surged in the seconds before last Wednesday’s unexpectedly strong private-sector jobs report from payrolls processor Automatic Data Processing Inc., raising suspicions that someone obtained the report ahead of its official release.

Analysis of exchange-rate prices from foreign-exchange platform EBS revealed a disproportionately large 0.12-yen spike in the dollar versus the yen in the last tick period before the clock hit 8:15 a.m., the report's official release time. The tick data, provided by CQG, are broken up into small, intraminute periods as per the feed from EBS.

Meanwhile, on CME Group Inc.'s Chicago Mercantile Exchange, an extraordinarily large flow of orders was processed immediately before the report's release in E-mini S&P 500 Futures, a contract that charts the stock index of the same name.

Anybody who placed those orders stood to make large gains in the subsequent minutes as first high-speed trading platforms and then regular investors put through big buy orders after ADP reported an increase of 297,000 in private-sector jobs, nearly triple the consensus estimate for a 100,000 gain.

The news offered a more upbeat view of the economy and the corporate earnings outlook than some had expected. It also raised the prospect of an increase in U.S. interest rates that would widen the differential with Japanese rates and boost the dollar versus the yen.
Noting the anomaly in the CME data, some high-speed trading users of algorithmic news feeds, which turn indicators such as the ADP report into electronically executable information, told Dow Jones Newswires that they thought someone had obtained the report early. These people declined to be identified.

ADP says that it followed strict procedures to ensure the data are protected before that release time. "We maintain stringent security controls and procedures designed to ensure the confidentiality of the report prior to its release to the public every month. We are not aware of any deviation from our established controls and procedures prior to the release of the latest report at 8:15 a.m. on Wednesday, January 5, 2011," ADP said in an emailed statement in response to questions on the matter.

The Securities and Exchange Commission declined to comment on whether it had received any complaints about trading last Wednesday. The Commodity Futures Trading Commission didn't immediately return calls seeking comment.

Still, within the millisecond-sensitive context of the modern high-frequency trading environment, the tick data analyzed by Dow Jones Newswires are striking.

Out of the 3,666 E-mini S&P 500 contracts traded in the minute before the ADP release, 3,212, or 87.6%, were completed at exactly 8:14:56, four seconds before the official release, according to the CME. And then in the last three seconds of that minute, only 196 contracts were traded.

In that one pre-release second, more contracts were traded than in the full minute before the ADP data were released in any of three previous months, when an average of just 1,071 contracts were traded in the 60-second period.

"As part of our normal surveillance process, we routinely monitor activity in our markets. To the extent that CME Group's Market Regulation Department identifies activity that merits further inquiry, an appropriate review is conducted, but as a matter of policy we do not comment on whether or not we are investigating specific activity in our markets," a CME Group spokesman said in an emailed statement.

In the unregulated spot foreign-exchange market, unusual moves were also detected in both volumes and prices in the moments preceding the ADP report, indicating that a large buyer of dollars was active at that time.

The dollar jumped to 83.38 yen from 83.26 yen in the final price level that EBS registered just before 8:15 a.m. Eastern time, according to CQG. The same data stream shows that the move for that tick was larger than any single other move in the minute following the release of the ADP data. A pickup in the frequency of ticks transmitted by EBS to CQG compared with earlier that day also suggests that volume spiked at that time. CQG said that both its data and times stamps are synched to the millisecond with those of EBS.

Any trader making a bet that the dollar would strengthen would have turned a big profit as it rose 0.28% in the following minute after the numbers were made public and had gained 0.73% after 15 minutes had passed.

The traditionally more heavily traded euro-dollar cross didn't see nearly as much activity at this time. However, dollar-yen would be a more natural market for investors to exploit inside...
knowledge of the employment data as it is especially sensitive to interest-rate differentials. Concerns about the euro zone's sovereign debt crisis and ambiguity over how investor risk appetites play out in that market left people less certain of how the euro would respond to the strong employment data.

"If I had information on interest rate differential, I could clearly use the FX market," said Bernard Donefer, adjunct associate professor at New York University's Stern School of Business, using industry parlance for foreign exchange. He also cited S&P 500 or 500 Mini contracts in the futures market as prime candidates for such activity because of their liquidity and the ability to place leveraged bets in those markets.

Similar anomalies weren't detected in the trading patterns for other securities at this time, which could back up the thesis that one person or a group of people acted upon early access to the information in selected markets.

In times past, such changes in second-by-second price data would have been unimportant and would have perhaps suggested that ADP's numbers were simply released a little early to the broader market. But in the world of high-speed trading, all the participants in the information chain—from data providers such as ADP, to news-release wires, to newswires, to the high-frequency traders themselves—use atomic clocks that are fully synchronized with each other.

In such an environment, obtaining information early offers a huge advantage.

"Anyone could benefit from this type of trading," said Ciamac Moallemi, professor at Columbia Business School. With a just a 10-second advantage, anyone could beat a high-frequency machine to the trade, Prof. Moallemi said. And with just a 100-millisecond advance, a high-frequency trader could win.

What is more, Prof. Moallemi said, high-frequency trading tends to amplify the effect of an initial trade based on early information, as computers pick up on the momentum it creates, triggering additional trades.