

(Excerpts from Ch 7 Virtually, Viral Computerization)

Deciphering Who's Who and What

Have you heard of Savvis, Equinix, or Blade? Savvis is a telecommunications company that provides co-location and cloud computing data-center services. Savvis hosts half of the top financial private and public exchanges in the U.S. through its data center in Weehawken, N.J., including the “dark pools” for investment firms such as Barclays, Credit Suisse, and UBS.² (Dark pools is a term used for trades that are concealed from the public, mostly large transactions between institutions.)

Sitting in these data centers are banks of computers trading with computers, splitting and bundling large blocks of orders. These transactions route through IT firms that scrub electronic transmissions sent on to the global exchanges. Tech companies like Savvis or Blade compete for the exchanges’ electronic business, from the hardware infrastructure to actual high-frequency trading.

Not all computer systems on the Dark Side are high-frequency traders; not all are created equal, or have the same purpose. The electronic systems are simply the backbone of the world’s global financial system. How those transactions are sliced, diced, and funneled to market makers depends on the creativity of the new batch of financial engineers.

The Dark Side’s massive network encompasses many layers of different technology companies managing the flow of transactions. Identifying an infrastructure provider versus a financial institution has become a daunting task. No solid line delineates which firms and institutions are traders, market makers, or simply providers of hardware systems. Therefore, how do we know which firms could potentially create an economic systemic risk?

Search, Hunt, Kill Algos

“Guerilla,” “Sniper,” “Scout,” “Raider,” and “Search, Hunt, Kill.” Those are the names of some of the Algos. Really! Traders have been pounding the table for years, screaming about Algos deliberately attacking stocks. It has been no secret that hedge funds and the large financial institutions like Goldman Sachs, Credit Suisse, Citi, and UBS run algorithmic programs with warfare titles. Ask the CEOs of the companies that have been innocent targets. Listen to AIG’s past CEO Hank Greenberg’s testimony in the Congressional hearings about short-sellers’ damage to AIG.

It’s been no surprise to the government, either. The Commodities Futures Trading Commission warned of aggressive Algos before a special panel investigating the flash crash. Its Technology Advisory Committee acknowledged that “some algorithmic programs were geared to take advantage of market circumstances, but also to instigate certain market conditions in order to then initiate their own program of buying or selling.”⁹

Algos do what they are programmed to do. If nothing is in their way, they continue as instructed until another force blocks their mission. Rogue traders know the common strategies, the target points, and resistance points. They also know how to trigger Algos in thinly-traded environments, where there is little resistance.

As the environment becomes harder to interpret, more fund managers buckle and rely on algorithmic packages that match one of the major indices, leaving computers to drive the market. At least their clients can’t complain if the fund matches the

index. Selling out for mediocrity is easier than trying to stand out in this crowd.