Jane Street's F&O Trading Manipulation

Mains: GS II - *Statutory, Regulatory, and various Quasi-judicial Bodies.*

Why in the news?

Recently, Securities and Exchange Board of India (SEBI) has banned Jane Street Capital for alleged market manipulation to make major illicit gains that it took out of the country mostly in F&O trading.

What is F&O trading?

- **F&O trading -** Futures and options are *financial derivatives* that allow ***traders to speculate on the price movements*** of an underlying asset without owning it.

> ***Derivatives*** *are financial contracts whose value is linked to the value of an underlying asset. They are used for various purposes, including speculation, hedging, and getting access to additional assets or markets.*

- **Futures** – They are contracts that *legally bind holders to buy or sell* a certain asset at an agreed-upon price at some time in the future, regardless of what the price is then.
- Thus, this benefits buyers when the price has increased and sellers when it has decreased (compared to the predetermined price).
- **Options** – They are contracts that *give buyers the right (not an obligation) to purchase* an asset from a willing seller at some time in the future.
- To ensure fairness, buyers are required to *pay the seller a premium* right after signing.
- **Two types of options -** Call options and put options.
    - **Call options** – It give holders the ability *to buy the asset* at the predetermined price.
    - **Put options** - It allow the holders *to sell the asset* at the predetermined price.
- **Issues with F&O** – It is one of the *riskiest trading choices* a retail investor can make.
    - According to SEBI, *more than 9 out of 10 retail investors in India have lost money* in FY25 trading on F&Os.
- **Ways to minimize risk** - It is possible to minimize these risks by understanding ways to optimally use F&O trading.
- This can be done potentially in terms of *limiting capital expended, enhancing risk tolerance,* and more.

What is Jane Street accused of doing?

- **Jane Street** - Jane Street (JS) is a *global trading firm* based in the New York that uses data-driven, automated models to trade across global markets.
- **Issue** – On January 17, 2025 it took home a whopping Rs 735 crore in a single day by allegedly implementing algorithms that allowed them to *manipulate NIFTY and Bank NIFTY index prices*.
- They made *unlawful net profits* of more than Rs 36,500 crore, between January 2023 and March 2025.

> ***National Stock Exchange Fifty (NIFTY)*** *is an index representing the top 50 companies listed on the National Stock Exchange (NSE) of India.*

- **Impacts** – Their alleged market manipulation led to *massive losses for retail investors* while Jane Street made whopping profits.
- **Action taken by SEBI** – SEBI *prohibited Jane Street from trading* in the Indian markets.
- It *ordered banks to freeze* more than Rs 4,800 crore deposited by Jane Street in their accounts.
- While Jane Street refuted the allegation, it has deposited more than *Rs 4,800 crore in an escrow account,* in compliance with the requirements of the interim order passed by SEBI.

> *An **escrow account** is a temporary, secure holding place for funds or assets during a transaction, managed by a neutral third party, until certain conditions are met.*

How Jane Street allegedly dodged SEBI regulations?

- Jane Street relied on several factors to pull off its alleged illegal “operation” in the Indian market.
- **Created Indian Subsidiaries** – They created multiple Indian subsidiaries *to bypass “Foreign Portfolio Investors” regulation.*

> *In 2019, SEBI notified a **‘Foreign Portfolio Investors’ regulation** whereby, a foreign portfolio investor shall transact in the securities in India only on the basis of taking and giving delivery of securities purchased or sold. This rule blocks intraday trading for foreign firms.*

> ***Intraday trading** refers to buying or selling of stocks on the same day, all before the market closes.*

- Thus, Jane Street’s Indian subsidiaries were technically allowed to indulge in intraday

stock trading, *"pumping and dumping" prices for their convenience.*

- **Intra-day index manipulation -** It would *rapidly buy major banking stocks* that were components of the "Bank NIFTY" index that would artificially drive the price of the index up.
- Thousands of *retail investors would jump on this false rise*, buying call options and selling puts while Jane Street would be buying put options and selling calls.
- **Expiry day manipulation** - On contract expiry days, it would *dump its index futures and holdings*, resulting in a sudden *decline of the share price.*
- **Malicious algorithm –** Jane Street's algorithms were able to make multiple targeted trades in the derivative market within milliseconds of executing.

What lies ahead?

- Continuous monitoring and improving market intelligence can be done to strengthen market regulations.
- Creating a unified financial regulator could help to tackle jurisdictional overlaps and mismanagements.

Quick Facts



Reference

[The Indian Express|Jane Street's Alleged Trading Manipulations]



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