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Standding Up to Save Canadian Mining

A Monday Morning Musing from Mickey the Mercenary Geologist

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Over the past several years, I have written and spoken extensively about the dysfunctional business model employed by TMX Group Ltd (TMX), a public company listed and traded on the Toronto Stock Exchange (TSX).

In my opinion, TMX Money has significant conflicts of interest because it is the owner, manager, and regulator of the microcap to large cap Toronto Stock Exchange (TSX) and the nanocap junior TSX Venture Exchange (TSXV).

TMX Group's share price is obviously driven, as is every publicly-listed company, by net revenues and net cash flow. As the owner, manager and regulator of these stock market exchanges, it generates a significant amount of both revenues and cash flow via the collection of compliance, listing, reporting, and trading fees from the very stocks that it purports to manage and regulate.

In that regard, the TSXV allows hundreds of inactive companies with large negative working capital positions to remain on the board and trade. There is absolutely no reason for this except to generate additional revenues from listing and compliance fees.

All this said, today's missive is focused on a trading issue that has been an increasing problem over the past several years. The issue has only recently come to the forefront as the junior resource industry emerges from a long bear market and specific gold stocks have started to run up.

The problem is naked short selling, which is the arguably illegal practice of selling a stock short without first borrowing shares or ensuring that the shares can be borrowed as is required for short sales.

In 2012, the Investment Industry Regulatory Organization of Canada (IIROC) and the regulator of this regulator, the Canadian Securities Association (CSA), removed a 142-year old trading rule known as the "tick test". The tick test restricted short selling to positive or neutral transactions and expressly prohibited shorting on negative trades, i.e., on the downtick.

This in industry parlance is known as the "uptick rule".

Since this long-standing rule was changed in 2012, naked short selling combined with trading by high-frequency and algorithmic computer programs has wreaked havoc on the junior resource sector

With characteristic shortsightedness, the oft-ineffectual IIROC ruled the expanded short selling rule would not only be applied to the main listings of the TSX Venture Exchange but equally across all Canadian trading venues. This relaxation of regulations resulted in an explosive growth of alternative trading platforms, which according to TMX, now number 14. Most of them are so-called "dark" exchanges that are opaque to the regular market.

Since then, the Canadian equities market has evolved into a plethora of trading locations and spawned a burgeoning dynamic where high-frequency, algorithmic trading dominates daily volumes.

Predatory short sellers have been able to exploit the lack of an uptick rule and this has proven to be especially detrimental to the largely illiquid nanocap juniors. In addition, the multiple trading platforms have severely reduced the main Venture Exchange's ability to effect any change because its trades now constitute only about 50% of total daily volumes.

In mid-November of 2019, an advocacy group called **Save Canadian Mining (SCM)** was formed by junior company entrepreneur Terry Lynch. It called on the CSA and IIROC to reinstitute the tick test and/or ban short-selling of stocks with less than $250 million market capitalization. This is the lobbying organization's initial press release: **Junior Mining Sector Responds to Predatory Short Selling; Launches "Save Canadian Mining"**.

According to the release, SCM has the support of many prominent voices in the exploration, mining, and investment community including: Brady Fletcher, Managing Director of the TSX Venture Exchange; Eric Sprott of Sprott Mining; Garry Clark, Executive Director of the Ontario Prospectors Association; and Chris Hodgson, President of the Ontario Mining Association.

It has also attracted yours truly along with other newsletter writers and analysts, numerous junior CEOs, media organizations, and investor relations firms.

My anecdotal evidence from trading junior resource stocks over the past eight years indicates:

- Naked short selling of illiquid, nanocap junior stocks is rampant and is accelerating.
- Algorithmic small volume trading is at times apparent with minute-by-minute small transactions by anomalous sellers, presumably via on-line, no-fee trading houses.
- Very small volume, end-of-day sales on the downtick are also indicative of short sellers manipulating the stock. They harm investor perception of a company's market, trading patterns, and future outlook.
- In some instances, these small trades are executed from both sides by the same entity or by associated firms using different market makers and/or brokerage accounts.
- Trades occur on several different platforms. The retail speculator can see trades on only a couple of these. While individual brokers may have access to two or three, their back-office traders and

market makers may be executing orders on many more. Regardless, a significant amount of trading volume occurs with complete opacity.

- 90% of the naked algorithmic short selling is estimated to originate from offshore. Four specific locations have been mentioned by my sources: China, Philippines, Singapore, and Slovakia. It seems likely that other domiciles are in play.

- Front-running, presumably by high-frequency traders, is common and occurs particularly when trades are entered as limit orders for a significant number of shares.

- Very large trades and insider crosses are generally executed via dark pools that few brokers or traders have access to or can get pertinent information about. They appear only at end-of-day recaps of trading volume. This exacerbates an underlying lack of trust in the honesty and transparency of junior markets by retail investors.

Over the past nine months, I have observed repeated naked short attacks on three microcap to nanocap juniors in which I hold positions. In each instance, the attacks were eventually repelled by market makers that the companies hired or by high net worth investors who entered large multiple bids at premiums to the shorts' small bids and recent trades. Their actions resulted in short squeezes and the attacks ceased after two or three attempts.

So long story short, these bad actors can be busted. A concerted effort backed by significant financial resources is necessary. My list of general requirements includes:

- A dedicated and committed management that understands what is happening and is motivated to do something about it;

- Constant monitoring by the company of trading patterns from pre-market open to market close;

- In some cases, the retaining of dedicated market makers to manage the company's trades;

- Independent shareholders who can bring buying pressure on the naked sellers, move the stock up, and force short squeezes.

Folks, the bandwagon is growing and we are beginning to see progress on this critical issue. It is the group's position that reinstatement of the uptick rule and/or banning of short selling stocks with a market cap of less than $250 million is required to return to a healthy nanocap venture capital market. That will allow small, diligent retail investors to once again play on a fair and level field and to profit from smart and timely trading.

If you are in agreement with this platform or would like to learn more before signing on, here's the website link again: **Save Canadian Mining**.

For more information on the TSX Venture Exchange's progress on this and other junior equity issues, see its **2019 Roundtable** from last March that features comments and recommendations from 19 participants representing a cross-section of our business.

Ciao for now,

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The **Mercenary Geologist Michael S. "Mickey" Fulp** is a Certified Professional Geologist with a B.Sc. in Earth Sciences with honor from the University of Tulsa, and M.Sc. in Geology from the University of New Mexico. Mickey has 40 years of experience as an exploration geologist and analyst searching for economic deposits of base and precious metals, industrial minerals, uranium, coal, oil and gas, and water in North and South America, Europe, and Asia.

Mickey worked for junior explorers, major mining companies, private companies, and investors as a consulting economic geologist for over 20 years, specializing in geological mapping, property evaluation, and business development. In addition to Mickey's professional credentials and experience, he is high-altitude proficient, and is bilingual in English and Spanish. From 2003 to 2006, he made four outcrop ore discoveries in Peru, Nevada, Chile, and British Columbia.

Mickey is well-known and highly respected throughout the mining and exploration community due to his ongoing work as an analyst, writer, and speaker.

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