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How a short-seller may have caused an accidental sell-off for two Canadian companies

Both Element Fleet Management and ECN Capital saw their share prices plunge after an early morning tweet from short-selling firm Muddy Waters claiming it had identified a new unnamed Canadian target



THE CANADIAN PRESS/Darryl Dyck

Shares of two Canadian companies were taken on a dramatic ride Wednesday in what appears to have been a mistaken reaction to a social media posting from a U.S. short-seller.

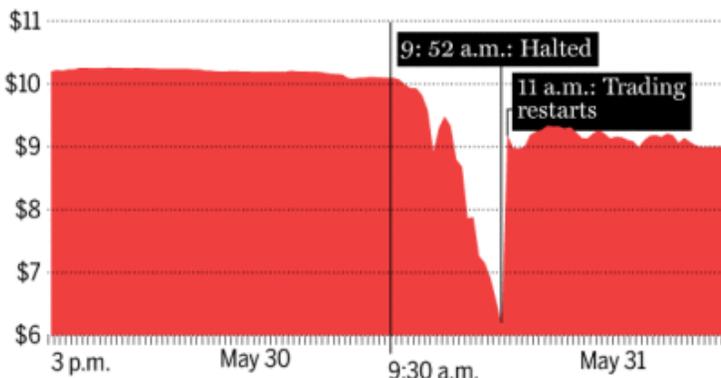
Both Element Fleet Management Corp. and ECN Capital Corp., which was spun out of Element last year, saw their share prices plunge after an early morning tweet from short-selling firm Muddy Waters claiming it had identified a new, but unnamed, Canadian target.

While that target was later revealed to be Vancouver-based miner Asanko Gold Inc., the uncertainty seemed to trigger a sell-off in the shares of Element, which plunged as much as 40 per cent, and ECN, which also lost significant ground.

ELEMENT FLEET MANAGEMENT

(EFN/TSX)

Intraday, every minute



SOURCE: BLOOMBERG NEWS

NATIONAL POST

Though both rebounded in part, observers said the rapid and dramatic response to a Twitter conversation illustrates the skittishness of investors and the vulnerability of Canadian companies to even the spectre of a short-selling campaign.

"There's no recourse. People can just put out whatever they want on the Internet," said Ken Lester, an adjunct professor at McGill University's Faculty of Management and president of Lester Asset Management Inc.

He said he was concerned by the market activity as both a finance professor and an investment professional, whose firm owns shares in Element.

"Element is one of our largest positions," Lester said, adding that the firm is "kind of a prime target" for what happened, given the general skittishness about Canadian financial services firms in the wake of problems faced by mortgage lender Home Capital Group. In April, the Ontario Securities Commission accused Home Capital of misleading disclosure related to an investigation into fraudulent mortgage documentation in 2014 and 2015. A run on the bank's deposits followed, and the share price is down nearly 60 per cent. Short-seller Marc Cohodes, who has a longstanding position in Home Capital, has been active on Twitter about his views on the depth of the firm's problems.

This month, he also publicly discussed his short position in Badger Daylighting Ltd.

On Wednesday, it was another short seller, Carson Block's Muddy Waters, which appeared to trigger the market action. An early morning tweet announced the U.S. short selling firm best known for its role in the collapse of Canada's Sino-Forest Corp. was about to release "a new short that we think is on its way to Zero."

The subsequent plunge in Element's stock price between 9:30 and 10 a.m. triggered a single stock circuit breaker at the Investment Industry Regulatory Organization of Canada, which subsequently halted trading.

Element put out a statement at 10:36 a.m. at the request of the regulator that said the company was "not aware of any material, undisclosed information... that would account for the recent decrease in the market price and level of trading volume."

Trading resumed and the shares ended the day at \$8.56, down 15 per cent. ECN closed down 2.3 per cent at \$3.69.

Through a spokesperson, Element's chief executive Steve Hudson declined a request for an interview.

According to IIROC, the regulator monitors trading and can make inquiries or investigate when unusual activity is detected. Matters can also be referred to other regulators if warranted.

In a television interview, Block said he doesn't understand why investors would guess which firm he might be targeting instead of waiting for Muddy Waters to issue a report.

"For investors to jump the gun, there's nothing I can say to that," Block said on BNN.

"To sell a company ... without hearing what we or another activist short, our position is, I don't get it." **Anthony Scilipoti**, chief executive of **Veritas Investment Research**, Canada's largest independent equity research firm, said stock trading on rumours and speculation is not new, though it is taking place in more public fashion thanks to social media.

But he said the impact on stocks is being fuelled by frothy markets and resulting investor skittishness.

"It think it's tied to the fact that we've had such run up," **Scilipoti** said. "There's a lot of jitters. Investors have low conviction."

That's not to say that **Veritas** doesn't see risks among the companies targeted by short-sellers.

The firm's watchlist includes Home Capital and Badger Daylighting. Element has been on the list for about a year, he said.

When a company makes it to the watchlist related to perceived risks about the business model, a tax issue, or corporate governance, the likelihood of something going wrong may be considered low. But the impact of a negative event "will be very material," **Scilipoti** said.