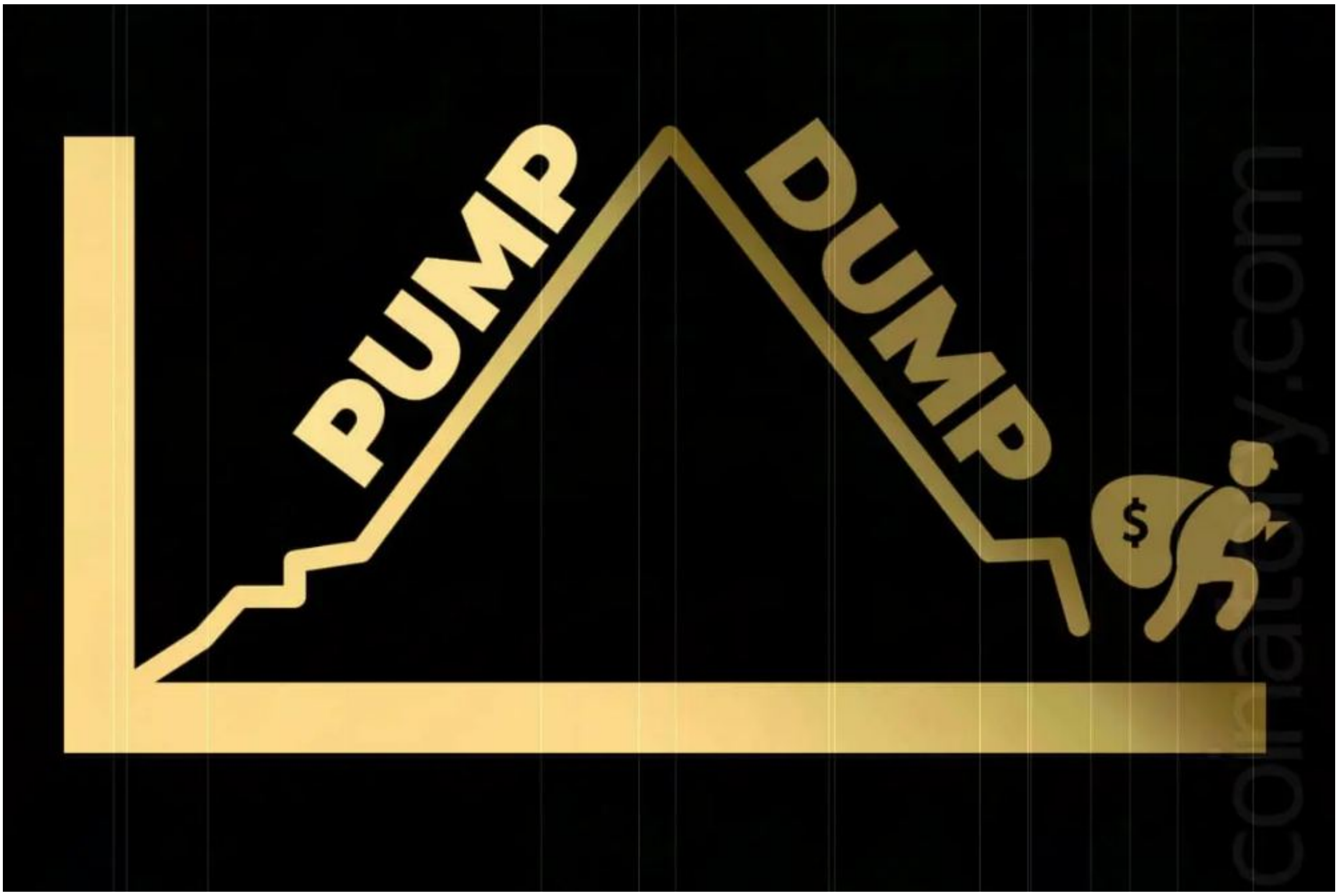
Vajiram & Ravi

What is Pump and Dump Scheme in Stock Market?

June 8, 2024 • vajiramandravi.com



About Pump and Dump Scheme:

- In the stock market, a pump and dump scheme is a type of **manipulation activity** that involves **artificially inflating the price of a stock through false** and misleading **information**, only **to sell the stock at the inflated price** and leave investors with significant losses.
- It is particularly **prevalent in the micro-cap and small-cap sectors**, **where companies** often **have limited public information and trading volumes are lower**.
- **How does pump and dump work**?

This process involves several steps:

- First, a **significant amount of stock in** a relatively s**mall or thinly traded company is acquired.** These stocks are often referred to as '**penny stocks'** because they trade at low prices and are more susceptible to price manipulation due to low trading volumes.

- Then the stock is **aggressively promoted to create a buzz** and **attract investors**. This promotion can take various forms, including sending out mass emails or newsletters with exaggerated claims about the company's prospects, as well as misleading social media posts. Promoters aim to create buzz and drive interest in the stock.
- As the promotion gains traction, **more investors buy into the stock**, **driving up its price** due to increased demand. **Sometimes, fraudsters may also engage in coordinated buying** to further boost the price. During this phase, the stock often experiences rapid and significant price increases, creating the illusion of a hot, high-potential investment.
- **Once the stock price** has been **pumped up sufficiently**, the **sell-off begins** at the inflated prices. This selling pressure **causes the stock price to plummet**, often **leaving unsuspecting investorswith significant losses** as the stock returns to its actual value or even lower.
- **Impact**:
    - **Those who bought into the hype** and purchased the stock at inflated prices typically **face substantial losses** when the stock price crashes.
    - These schemes **undermine confidence in the financial markets**, making legitimate investors wary of potential fraud.

Under the **SEBI guidelines**, **pump and dump schemes are completely banned**.

Q1: What is the Securities and Exchange Board of India (SEBI)?

The SEBI is a statutory regulatory body established by the Government of India in 1992. It was given statutory powers through the SEBI Act, 1992. It aims to regulate the securities market in India and protect the interests of investors in securities.

Source: Explained: What is pump and dump scheme in stock market and how to be safe

---