Game stop for stock markets?

The specter of the power of financial democracy is creeping, perhaps for the first time, into the deepest heart of finance. To use the same terms that have characterized the political verbiage in recent years, one could say that financial populism has exploded on Wall Street. In recent days a myriad of small online investors have decided to deliberately challenge the big professionals. Those who seek, on the basis of extremely accurate analysis, securities that they consider overvalued, with the intention of "shorting" them, i.e. selling them short without actually owning them, and then buying them back at a lower price and monetizing the profit. A practice in which some hedge funds are masters. Their role has often been to give the coup de grace to companies in difficulty, angering a large number of people who worked in those companies and who found themselves unemployed. This phenomenon was particularly in vogue some 20 years ago. The 2008 financial crisis wiped out certain exaggerations of short selling, of speculating on the downside. But the children of that generation, who suffered hard times, are now the millennials: they are the first post-war generation to earn less than their parents. They are in debt before they even enter the job market: the cost of a college degree in the United States is enormous. And they're angry, but extremely digitized.

In recent weeks, *GameStop*, a chain of stores for video games on floppy disk, overtaken by digital alternatives (in 2019 it closed a thousand stores) and therefore at risk of bankruptcy, has seen its stock gain as much as 1'600%, defying the logic of financial common sense. Basically, a hedge fund, *Citron Research*, had placed a bearish bet on the company's stock, publicly announcing its move. It hoped to be emulated, convinced that the stock would depreciate further. But small investors on the web, organized on digital Reddit platforms such as WSB (WallStreetBets), decided to go against nature and buy the stock en masse, not only through shares, but also through derivatives (call options). The hedge fund was forced to cover itself, i.e. to buy back the securities it had borrowed, causing its prices to explode. Small traders inflicted losses of billions on the bearish fund. *"Now Wall Street's bets,"* we read in a post on WSB, "*have cost Wall Street billions, and millennials have celebrated by paying for medical care and repaying student loan debt.*"

And in another comment: *"Same. I even studied accounting and finance in order to understand what the fuck was happening so I could avoid the same pain my parents experienced. What I learned and the types of people I met in that finance program disgusted me. Forget republican/democrat, left/right... the bankers play both sides and have almost always come out on top".* And then, *"Occupy Wall Street was a misguided, but earnest airing of grievances. This time we're actually hitting them where it hurts. KEEP HODLING."*

This organized attack, which also targeted other stocks, was made possible thanks to trading tools created especially for small investors. The Robinhood platform, at the heart of the *GameStop* operation, deliberately aims to democratize finance by even allowing to "play" with options for free (it does not charge commissions). In practice it encourages leverage in the markets. If we consider that the WallStreetBets community gathers six million investors, their ability to move at least small or medium capitalization stocks is enormous. Robin Hood used to steal from the rich to give to the poor. But last week the platform suspended trading in the targeted securities, inflicting losses on those who had bought them, hence on small investors. The case has become political. Alexandria Ocasio-Cortez, the youngest woman elected to Congress, intervened defending the millennials: *"Gotta admit it's something to see Wall Streeters with a long history of trating our economy as a casino complain about a message board of posters also treating the market as a casino. Anyways tax the rich."*

The platforms have since reopened trading to stocks targeted by social. While financial market monitoring institutions keep watch. It is difficult for politics to intervene. After the attack on Capitol Hill, the risk of exasperating the disgruntled may have incalculable consequences.

This episode, which could also be the beginning of a saga, has already inflicted on the markets a change of pace that could characterize the entire 2021. The stock market phase that the technicians call momentum, the one in which any news contributes to feed the markets, has been interrupted. At the base of these trends there are parameters, therefore algorithms, which feed themselves. Their strength depends precisely on the fact that a good portion of the financial community uses similar models. Once they were above all the data related to the single Stock to create the movement (relationship price/earnings, cash flow/indebtedness, price/book value etc.). Now to these have been added those relative to the market: for example, the yield of dividends in relation to that of bonds and volatility. In practice, the promise of central banks, reiterated by both the Federal Reserve and the European Central Bank, to inflate their balance sheets, inflates the stock markets. For some time now, there has been talk of a bubble in the markets. Technical indicators have reached levels that signal overpriced stock markets. In these cases, central banks, unable to reduce liquidity, issue a few warnings. But the spread of the coronavirus in January has not allowed these verbal interventions: the risk that a stock market crash will discourage already worried consumers is too high.

The case of China is different, where growth has restarted and the coronavirus is under control. It is no coincidence that the People Bank of China on January 27 withdrew the equivalent of 12 billion usd from the market, causing the interbank rate (overnight repo rate) to suddenly rise from 2.5% to 2.8%, the highest level since the end of 2019; the stock market that day lost 2%. Added to this was the comment by an advisor to the Chinese central institution that the risks of a financial bubble increase, if monetary policy is not adjusted as soon as possible. It is a scenario that in some respects is reminiscent of 2017, when the Chinese central bank began to curb monetary expansion, later followed by the Federal Reserve: the financial markets in 2018 suffered the consequences.

The month of January started very well. However, it closed negatively for the stock markets that represent the economies most in difficulty: -2% Eurostoxx50, -3% Italy, -4% Spain. In the United States the S&P returned to negative territory (-1.1%), while the Nasdaq remained positive, despite eroding much of its new year's earnings (+1.4%). The Russel 2000, the American index of small and medium capitalization, where stocks such as *GameStop* are found, closes at +5%. While China maintains a +2.6% (CSI300) and Hong Kong recovers, in 2021, 3.8%.

Is the party winding down in the markets? Is the bubble bursting? Probably not. Or at least not yet. Liquidity remains plentiful. Joe Biden's intervention plans include pouring money directly into people's pockets, and some of it will end up in the stock market. But the markets will be less directional. In the USA, the retail investor population, which previously did not exceed 15% of stock exchange volumes, now exceeds 20% and is showing that it can concentrate on a few actions. But by doing so, they are able to upset the supports calibrated by the big investors, thus shaking the markets. If millennials do not exaggerate, in this market phase, they can also help the FED, because they allow to correct market exasperations, thus allowing the central bank not to intervene directly. The European Union, after its historic decision to share aid to the weakest, is looking with concern at what is happening in Italy. But everything will depend on the speed with which the expansion of the coronavirus is contained, hence on vaccines. Slowdowns will have repercussions on growth. Positive news on the containment of the virus will bring back to the markets the savings parked in the banks. February is still a difficult month for the stock markets. Perhaps a tactical buying opportunity in a market that will need to be actively addressed.

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