In this article

HTZ
HERTZ GLOBAL HOL
1.57 USD
▲ +0.03 +1.79%

TSLA
TESLA INC
1,654.79 USD
▲ +33.79 +2.08%

WLL
WHITING PETROLEU
0.93 USD
▼ -0.03 -2.66%

CL1
WTI Crude
42.23 USD/bbl.
▼ -0.01 -0.02%

0850607D
SC LOWY FINANCIAL HK LTD
Private Company

BMH: Bankruptcy

Here's a story you could tell about the last few months in the stock market, and the next few months. A deadly pandemic occurred and shut down much of the world. Investors worried that all the companies would go out of business, due to a combination of economic losses and financial panic: The companies wouldn't have any revenue, their creditors would refuse to fund them, and they'd go bankrupt. But then things turned out not to be so bad. A financial panic was averted by quick and comprehensive government action, companies actually had a pretty easy time getting credit to stay afloat, and the bankruptcies were averted. The economy will reopen, revenue will bounce back, everything will go back to being how it was before. Financial conditions kept companies afloat until the economy could recover, and now it will recover and they'll be fine.

I do not especially mean to endorse this story but it does seem to fit the stock market, which went down a lot and then up again a lot. (The S&P 500 index peaked in February, then fell 34% by March 23, then rose 44%; as of yesterday's close it was up a bit year-to-date.) And if this is your story, it is *the* story for almost every company: The most important fact for any given company is not its particular business model or execution, but the pandemic. There are some exceptions, some companies that weren't really affected by the pandemic, or even benefited from it; this is not the story of Zoom or Slack. But the companies most obviously harmed by the economic shutdown—cruise lines, airlines, non-essential retailers, WeWork—are the ones that went down the most and will have the sharpest recoveries, so if this is your thesis you should buy them indiscriminately. "Everything will be back to normal soon" is an argument for buying the stocks that went down the most.

There is however an important exception. The bankruptcies were not *all* averted. Quite a few of them actually happened, and more might be coming. Some companies had no revenue for a while and ran into trouble with their debt, and their creditors, instead of saying "wow the Fed is buying everything, we will cheerfully extend these companies credit at record-low interest rates until their revenue recovers," said "yeah we don't think these companies are good for it," called in their loans and put the companies into default. *Economically* the same story may end up being more or less true: Maybe in a few months these companies will be back to normal, their revenue will recover, they will be profitable again. But normally the way corporate bankruptcy works is that when a company goes bankrupt it is then owned by its creditors. The company may keep operating, it may return to profitability, but those profits will go to the (former) creditors. The shareholders who owned it before the bankruptcy don't own it anymore; the return of profits doesn't do them any good.

If (1) your basic thesis of investing is the one I laid out above —roughly, everyone panicked about the pandemic but it will work out fine, so the hardest-hit stocks are the best buys— and (2) you have, uh, never invested before and don't know much about stocks, then you might especially focus on buying the stocks of the bankrupt companies. Hertz sure went down a lot, but now the rental-car business will recover, so that stock is a great buy!

> Car renter Hertz Global Holdings Inc., oil driller Whiting Petroleum Corp. and retailer J.C. Penney Co. are among companies that have seen their shares more than double in recent trading sessions despite being in Chapter 11 bankruptcy, a process that allows companies to keep operating while working out a plan to repay creditors.
>
> "I have always thought people have a psychological urge to buy stocks at a low price," said Kirk Ruddy, a former bankruptcy claims trader. Retail investors may be buying big names they recognize without realizing how rare it is for shareholders to get anything back in bankruptcy, he said.
>
> "If you look at the markets in general, people don't know where to put their money. They are like 'Hey, I'm going

> to try that $1 stock,"' said Ruddy, who now works in sales for SC Lowy Financial HK Ltd.

Now, I should say, you could have this thesis for real. Corporate bankruptcy doesn't *always* wipe out the shareholders. If everything really is going to get back to normal soon, then there could be enough money to satisfy creditors and leave shareholders with something, and clearly some professional investors think that might be true about some of these bankrupt names. "On Tuesday, J.C. Penney shareholders will press a federal judge to appoint a court-approved committee to represent them in the bankruptcy case," suggesting that they have a case for some recovery. "Whiting Petroleum does have a plan on file which calls for a payout to current stockholders in the form of new shares." Analysts have pointed to improvements in air travel and used-car prices to conclude that there's some chance of Hertz shareholders recovering. Maybe all the companies and their creditors will show up in bankruptcy court and say "never mind, things are fine now, everything will go back to how it was," and the stocks will rally. It has happened occasionally in the past—Bill Ackman made a fortune holding General Growth Properties stock through bankruptcy—and these are strange and unprecedented times.

On the other hand, "debt securities tied to the companies continue to trade below par, implying a less-than-full recovery for creditors who are ranked well ahead of shareholders." J.C. Penney's credit default swap auction just assigned a 1.4% recovery to its bonds, which is not encouraging for the stock. And it is … possible … that many of the thousands of brand-new investors on Robinhood have not carefully analyzed the capital structures to find the fulcrum securities?

So there is a widespread view that the rally in bankrupt stocks is an effect of the boredom markets hypothesis[1]:

> But the rally could also be fueled by amateur traders, bored in lockdown and looking for a quick buck, using platforms such as Robinhood. The number of Robinhood users holding both Hertz and Whiting Petroleum shares surged after the companies filed for bankruptcy, according to Robintrack, a website unaffiliated with the stock trading platform that uses data to show trends.

And a CreditSights "analyst said that the stock price [of Hertz] doesn't 'make any sense whatsoever but as long as everyone out there is having fun trading, they won't begrudge them that.'"

We have talked a few times about the boredom markets hypothesis, the idea that a lot of individual investors buy stocks mainly because it's fun, and that the more fun stocks are, and *the less fun everything else is*, the more they'll buy stocks. In a pandemic, when people can't really leave their house and sports are canceled, there is a lot less fun to be had elsewhere, so trading stocks seems relatively more fun, so people buy more stocks.

When we first discussed the BMH, I noted that, in the specific case of a pandemic, it is essentially countercyclical:

> The worse the economy is, the more bored investors will be. If stocks sell off because the coronavirus crisis is longer and worse than expected, there will be even fewer entertainment options and more people will turn, in desperation, to buying stocks on their phones. If someone finds a magic cure for the virus tomorrow, stocks will rally and all the new retail investors will happily sell into the rally at the top and go back to their other, more entertaining, entertainments.

For individual stocks the effect is less obvious. The normal model of retail traders, not that long ago, was that stocks that go up are more fun than stocks that go down. Tesla Inc., the long-time favorite of day traders looking for entertainment, got more volatile the more it went up: It went up rapidly, which looked fun, which attracted more buyers. Stocks that go down are no fun, so day traders looking for entertainment dump them and move on to more fun things. The standard pre-pandemic view of the BMH—of retail traders' entertainment preferences—was that it was procyclical and volatility-increasing: Stocks that go up are more fun so they go up more, stocks that go down are less fun so they go down more.

But in the pandemic that seems to have reversed; the retail traders who have flocked to Robinhood since all other entertainment has shut down seem to particularly enjoy stocks that have gone down a lot. "Hey, I'm going to try that $1 stock": A near-bankrupt, or actually bankrupt, company, one that is particularly beaten down and unloved in the pandemic, might feel like more of a fun gamble, and a compelling story arc of trial and redemption, than one that is doing fine. (One that's doing great might also be fun, though, and individual investors are piling in to big tech stocks; the BMH might be good for the best stocks, good for the worst stocks, and neutral or bad for the boring ones in the middle.)

You could have a model of bored retail traders as the ultimate value investors: When no one else ascribes any value to a company's stock *because it is literally bankrupt*, they will buy it for the lulz.

That sounds pejorative and it probably shouldn't be. I don't know what to tell you about Hertz, but in general, jumping in to buy beaten-down stocks at the lows seems like a pretty good plan? Here's a Bloomberg article from Friday titled " Dumb Money Is Looking a Lot Smarter in Never-Ending Stock Rally":

> "Young investors have been putting money in the market, and in the short run, that seems to be good timing," said Mike Skillman, chief executive officer of Cadence Capital Management. "The evidence in history for folks that day-trade their own accounts on average is not very good, so we'll see how that plays out over a full cycle, but in the short term, that looks like a pretty good decision."
>
> That's been particularly true in the exchange-traded fund universe. The US Global Jets exchange-traded fund has swelled to over $1 billion in assets and soared nearly 58% in the past months as "bored" millennials pile in. The United States Oil Fund LP -- another favorite among retail traders -- has returned over 34% in that time frame.

And here's Myles Udland:

> Right now, it appears that there is a new class of investors exerting some not-insignificant level of influence on stock prices. And it appears this class of investor all learned the same rule about what makes a good investor and have acted on that basis.
>
> And that rule is buy low, sell high.

Well, it's "buy low" anyway. If the retail traders all get out before the top I will be impressed.

BMH: Call options

If you are bored and looking for some action, buying call options is preferable to buying stocks. A call option is just more action per dollar; it is a leveraged, volatile, exciting way to speculate on a stock. So it makes perfect sense that fun-seeking retail traders buy lots of call options, and that options speculation by bored retail traders would increase in a pandemic. And here you go:

> Speculative excess has surged to the highest in at least 20 years among U.S. options traders -- and that's a negative for stocks over the medium term, according to Sundial Capital Research Inc.
>
> Traders established fresh bullish positions last week by buying 35.6 million new call options on equities, according to Sundial founder Jason Goepfert. That's up from a peak of 28.7 million in February, when speculative activity was rampant, he wrote in a note Monday. ...
>
> At the heart of the speculative activity are smaller investors, according to Sundial. Small trader call buying made up more than 50% of total volume last week, the highest since 2000, it said.

This is also a model for Hertz, etc.: Famously, the stock of a company is a call option on the company's assets, with a strike price of the nominal value of the company's debt. When the company is bankrupt, the call option is out-of-the-money, cheap and highly speculative. That is, it *feels* more like a call option; if you are trading for fun, and call options are fun, then you will prefer option-y stocks like Hertz.

BMH: Nikola Tesla

When I formally introduced the boredom markets hypothesis last month, we talked about how retail traders loved Tesla Inc. even before the pandemic. The closer a company is to Tesla in its combination of social mission, high volatility, general drama and business of making cool toys, the more appealing it will be to bored retail traders. "There has to be more to investing than just Tesla," a trading YouTube star told Bloomberg. I wrote:

> There has to be more to investing than just Tesla! You need a Netflix algorithm that is like "if you enjoy Tesla, here are some other funny stocks." It is a market opportunity; if you're weird and like rockets and

> Twitter, you should start a cannabis-and-laser-guns company and sell stock to people who enjoy Tesla but would like to get a little deeper into the genre. “I love how unfiltered Argon Dusk is on Twitter,” your fans will say on r/wallstreetbets, “and how many ‘420’ jokes he makes, and how he took a stand against outdated safety regulations when he launched his death-ray space station. I’m gonna buy lots of call options and you should too.”

“Argon Dusk,” you see, was a small tweak to the name of Elon Musk, Tesla’s chief executive officer and social media manager. “People love Elon Musk and will rush to give their money to a slightly altered clone of him,” was my thinking there.

I was so close:

> No stock in the automotive sector is a better indication of equity-market exuberance than Nikola Corp.
>
> The aspiring battery-electric and hydrogen fuel-cell truck maker debuted on the Nasdaq last week following a reverse merger with a blank-check company headed by a former General Motors Co. executive and board director. It’s forecasting zero revenue for 2020 and its first $1 billion year won’t be until 2023.
>
> Ford Motor Co., by comparison, is expected to report about $115 billion of revenue for this year. And yet Nikola, whose stock more than doubled Monday, traded up another 30% to as high as $95 after the close, giving the company a richer market capitalization than the almost 117-year-old maker of the F-150.
>
> Skeptics have long questioned the market’s valuation of Tesla, which has yet to post an annual profit. But by pushing Nikola’s market cap to $26 billion at Monday’s close, investors have taken appraisals of zero-emission vehicle manufacturers named after a celebrated Serbian-American inventor to another stratosphere.

Not a small tweak to *Musk’s* name, but a small tweak to *Tesla’s*. Twenty-six billion dollars! The founder's stake is worth $9 billion. “As far as I can ascertain,” tweeted my Bloomberg Opinion colleague John Authers, “Nikola Tesla didn't have a middle name,” meaning that this particular trade might be tapped out, but just in case I am quitting my job to launch a company called Tessla Inc. “Electric tanks!,” I will scrawl on the single piece of paper that makes up my S-1, just typing this joke here has made me a billionaire, modern stock markets are weird.

BMH: Oil

In general, the apparent pandemic-era bored-retail-trader behavior of buying cheap beaten-down things as a fun low-stakes gamble seems to be working out pretty well so far. Bankruptcy stocks might turn out to be an exception: “Hey Hertz stock is cheap, maybe it will go up,” might just be a misunderstanding of how bankruptcy works. But the worst trade of all would be buying *oil futures* in April, thinking “hey a barrel of oil is so cheap, that’s a good gamble with high upside and little downside.” It was not. Here’s Bloomberg's Matthew Leising:

> Ben Whitesides was trading on ETrade from his home near Salt Lake City when he bought three 500 barrel oil contracts at an average price of 75¢ a barrel, he says. When prices turned negative, he wanted to sell immediately, but ETrade’s system froze. Whitesides says he couldn’t buy or sell, and was completely shut out. He estimated the most he could lose was about $1,500. Two days later, ETrade withdrew $57,000 from his account.

Front-month oil contracts closed at negative $37.63 per barrel one day this April, meaning that if you bought contracts for a dollar the most you could lose was 3,800% of your money, which is not how it usually works.

The particular problem for retail traders seems to have been not only that they bought stuff cheap and then it went negative, but also that they had trouble selling when it went negative due to market and/or systems glitches. ETrade:

> “Their system had no ability to exit those contracts,” Whitesides says. “I was at the mercy of the market with no ability to get in or out based on ETrade’s system.”
>
> When he complained to ETrade, the brokerage was unsympathetic. ETrade “has determined that there was not enough liquidity in the market to support exiting the position you maintained in your account,” the company said in a May 26 letter to a lawyer representing Whitesides. “Accordingly, ETrade will not be making any adjustments to your account.”

TD Ameritrade:

> The same thing happened to a trader on TD Ameritrade. The loss there was $92,000 for three contracts bought for about $21 each that day, according to the trader, who asked not to be named for fear of reprisal. When he tried to sell, TD Ameritrade's system rejected his attempts, saying it couldn't process negative prices. The trader says a TD Ameritrade representative told him two days later that operations on the exchange where oil is bought and sold worked perfectly and that he should have used a market order, which allows for a sale at the current price, rather than a limit order, which specifies a minimum selling price.

Imagine being a retail broker and *telling your customers they should have used market orders instead of limit orders*. The world is really upside down.

BMH: BETZ

We could keep doing this all day:

> The Roundhill Sports Betting & iGaming ETF [ticker symbol BETZ] debuted last Thursday and the first exchange-traded fund dedicated to the rapidly growing online betting and sports wagering themes is already attracting investors in a predictable venue.
>
> What Happened: Younger investors are already showing an affinity for BETZ, particularly those on the popular Robinhood app. Last Friday was merely the second day of trading for BETZ, but when markets closed that day, more 8,600 Robinhood users were holding the rookie ETF.
>
> That's good for a 273% increase from the prior day, making BETZ the biggest gainer on a percentage basis in terms of one-day additions among Robinhood account users, according to the brokerage app.

If you can't bet on sports, bet on sports betting!

Meanwhile in efficient markets

Okay, sure:

> According to new research, the earnings forecasts of securities analysts who share a first name with the CEO of a covered firm ("matched" analysts) are more

> accurate—especially when it is an unusual name—than forecasts of analysts whose names don't match the CEO's. The study was conducted by researchers at the University of California, Berkeley, and the University of California, Los Angeles.
>
> The finding suggests that a chief executive officer is more likely to share private information with an analyst with whom that executive shares a first name, the researchers say.

Here is the paper, by Omri Even-Tov, Kanyuan Huang and Brett Trueman. One way to read this result is that stock markets must be incredibly efficient if this is the sort of anomaly that people look for and find and publish.

Stock exchanges

Speaking of incredibly efficient stock markets:

> Nasdaq Inc. has edged past the New York Stock Exchange in initial public offerings this year as the coronavirus pandemic has curtailed activity and reined in celebrations of corporate debuts on the NYSE's historic trading floor. …
>
> The coronavirus forced the NYSE to shut its floor for two months, after two people at the exchange tested positive for Covid-19.
>
> Although closing the floor had little impact on investors—the NYSE's markets continued to function in all-electronic mode—it disrupted the exchange's playbook for winning IPOs. Debuts at the Big Board typically involve parties and bell-ringing ceremonies at its building on the corner of Wall and Broad streets in Manhattan, a once-in-a-lifetime media and branding opportunity for many companies. …
>
> "The floor has been a superb marketing weapon for NYSE," said Patrick Healy, CEO of Issuer Network LLC, which advises companies on their choice of listing exchange. "Without that weapon, they're not quite the same."

See I actually disagree that ringing the NYSE bell, as opposed to like beeping the Nasdaq button, is a particularly valuable media and branding opportunity *for a company*. Doing an *IPO* is generally good publicity, sure, but nobody thinks “I should buy that company’s product because they had a party at the NYSE.” The party at the NYSE is marketed to the company’s executives; if you like ringing bells in fancy rooms (and who doesn’t), a NYSE IPO is more personally satisfying than a Nasdaq one. Except in a pandemic, when NYSE loses market share.

Perhaps the point here is that fun, in stock markets, is not exclusively a concern for retail investors.

Things happen

Pandemic sparks surge in equity fundraisings. Hong Kong hedge funds explore exit as national security law looms. Behind HSBC’s Rare Foray Into Politics Over Hong Kong. Wall Street Doubts Fed’s $600 Billion Lending Plan Can Succeed. Bank of America Eases Sales Targets for Merrill Advisers During Pandemic. OPEC+ Tries Novel Strategy to Turn Oil Price Curve Upside Down. PG&E Chases Hot Debt Markets Ahead of Bankruptcy Plan Approval. BlackRock’s Green Dreams Got Complicated Fast. BNP has Goldman in its sights after beefing up hedge fund business. EY fights fires on three audit cases that threaten its global reputation. New Yorkers Anxiously Exit Covid Lockdowns After 80 Days of Hell. Boxed Lunches and Plexiglass Will Welcome Back Wall Street’s Workers. In the Feud Between Two of U.K.’s Richest Men, Family Members Say They Bugged Uncle. How Four Americans Robbed the Bank of England. Man Allegedly Throws ‘Large Pickle’ Out Window in Vermont, Hurting Worker. Angry Edinburgh local hits out after swan faces brutal insult on city litter bin.

If you'd like to get Money Stuff in handy email form, right in your inbox, please subscribe at this link. Or you can subscribe to Money Stuff and other great Bloomberg newsletters here. Thanks!

[1] To be fair, the bankruptcy rally might also be a technical artifact of short selling. If you shorted Hertz or Whiting because you thought they were going to go bankrupt, and then they did, you might be buying the stock now to collect your winnings. Or if you shorted the stock after the bankruptcy, because the trading price seemed too high, you might not be able to hold on to that position, due to mark-to-market losses or the high cost (or unavailability of stock borrow. Shorting a company in bankruptcy is not a lot safer than buying it.