

Title: Melvin Capital wind down, history lesson from Bear Stearns hedge fund collapse

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As we all know, Melvin Capital has announced an intention to wind down their hedge fund after sustaining substantial losses - down 39% in 2021, down ~21% in 2022 (so far). For my own understanding, I researched previous examples of well known hedge funds collapsing/closing and Bear Stearns caught my eye (in my view, the first domino to fall in what would culminate in total economic depression by the end of 2008). Michael Lewis' *'The Big Short'* & *'Panic'* do a better job than I ever could of explain the decade leading up to 2008, but the important point is that Bear Stearns operated 2 hedge funds that had charged into the thick of things with Mortgage Backed Securities and Collateralized Debt Obligations.

More plainly - Bear Stearns took a massive, unsustainably bullish position on the health of the MBS market. Just like Melvin Capital took a massive, unsustainably bearish position on Gamestop stock.

* **AUM. Similar scale.**

* Melvin Capital has [\$8.7 Billion

AUM](<https://www.ft.com/content/f1a3990b-e262-4bb4-9879-5fc22ed13a38>) according to Financial Times. Leveraged bets/positions can only be estimated (because they know how to cover their tracks) but latest quarterly filing shows a value of ~\$20 Billion in positions.

* [Prior to collapse](<https://www.wsj.com/articles/SB118230204193441422>), Bear Stearns two hedge funds contained ~\$1.6 Billion of investor money and \$6 Billion in borrowed capital. Data showed these two hedge funds held nearly ~\$30 Billion in leveraged bets.

* [**Bear Stearns Collapse Timeline**](<https://www.reuters.com/article/us-bearstearns-chronology/timeline-a-dozen-key-dates-in-the-demise-of-bear-stearns-idUSN1724031920080317>)*:**

* June 15, 2007 - WSJ reports that Bear Stearns funds have suffered extensive losses.

* June 23, 2007 - Bear Stearns sources/pledges \$3.2 Billion to bail out their own hedge fund.

* July 31, 2007 - Bear Stearns files bankruptcy paperwork for its two failed hedge funds.

* October 5th, 2007 - Criminal probe launched.

* March 16, 2008 - JP Morgan acquires Bear Stearns for pennies on the dollar. Federal Reserve guarantees \$30 Billion in MBS to secure the deal and contain the financial contagion.

* September 2008 - Stock market collapse begins.

* **Melvin Capital Collapse Timeline:****

* January, 2021 - Melvin Capital makes headlines for substantial losses on Gamestop short position. Claims to have closed but DD proves otherwise.

* January 25, 2021 - [Citadel & Point72 invest \$2.75 Billion](<https://www.wsj.com/articles/citadel-point72-to-invest-2-75-billion-into-melvin-capital-management-11611604340>) into Melvin Capital.

* December 10, 2021 - [DOJ announces probe](<https://www.reuters.com/markets/europe/us-doj-launches-expansive-probe-into-short-selling-bloomberg-news-2021-12-10/>) into short sellers.

* April 21, 2022 - Under immense pressure to return capital and with no way to charge performance fees, Melvin Capital announces plans to wind down. Cover story is that he plans to start a new fund.

So what happens now? I truly don't know, obviously there are some key differences here. Bear was also a traditional investment bank and not a pure hedge fund. In 2008, Federal bailouts and interventions didn't start in earnest until mid-2008 whereas our Federal reserve/government has been in bailout mode for 2+ years. ****But here's what I think happens next:****

1. Melvin fails wind down procedures because Gamestop short positions become an unavoidable issue. Melvin is completely bought out by a larger hedge fund or finds a way to transfer their positions to another bag holder with more stamina, analogous to JP Morgan's buyout of Bear(ex. Citadel).
2. Friendly press ties a nice bow on it, claims Melvin closed in good standing and prospects are excellent for the new buyer. Sweeps it under the rug where it rests for a few months.
3. But the short position sits there festering, needing to be fed more synthetic shares and ETF shorting like

a ravenous monster.

4. Buyer (ex. Citadel) tries to strike a deal with the Federal Reserve like JPM did. No dice, Fed is completely tapped out.

5. Complete and total market collapse as positions are liquidated to cover the short shares. Gamestop stock skyrockets in value.