

Title: The GameStop Market Hedge Thesis. A comprehensive analysis using the data this sub has accumulated over the last 18 months

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Created 2022-06-23 12:55:53 UTC

Permalink: /r/TheGloryHodl/comments/viwb9v/the_gamestop_market_hedge_thesis_a_comprehensive/

Url: /r/Superstonk/comments/vhe37m/the_gamestop_market_hedge_thesis_a_comprehensive/

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This is going to be a long one.

This analysis contains no memes, no hype dates, no cryptic tweet analysis, and minimal speculation based on known market mechanics. This is a cumulative fact-based report of what we know to-date. The abstract is the closest you will get to a TLDR. This is *The GameStop Market Hedge Thesis*.

##Abstract

GameStop is primed for the biggest short squeeze the market has ever seen. **The January 2021 "Sneeze" section uses SEC reports to show that short covering was a small fraction of the buy volume in the sneeze. Massive short positions are open and hidden in ETFs and swaps which don't have to be reported. **Current Market Conditions** is speculative but shows strong signs of an impending recession and/or market downturn. **The GameStop Squeeze is Inevitable** shows the company is in good health and at no risk of bankruptcy. Borrow and utilization rates prove the stock is illiquid and hard to find. Negative beta is a strong indicator that GameStop tracks inverse to the market which is headed for a major downturn. Even with current reported SI and no hidden short positions GameStop is primed to move many multiples above its current market cap. ComputerShare DRS statistics provide proof of a closing exit for shorts to squeeze out of, day by day making it harder for them to close their positions entirely.

#Why Short Squeezes Happen

##Prime Short Squeeze Conditions

>Short interest ratios tend to be quite low; for large non-financial stocks, they are often less than 2.5% whereas for small non-financial stocks they still tend to be less than 13%. **Few stocks, if any, have short interest greater than 50% on a given date.**^(76) Until recently, short interest of more than 90% was observed only a few times—in 2007 and 2008. When examining short interest as a percent of shares outstanding, **GME is the only stock that staff observed as having short interest of more than shares outstanding in January 2021.**

[[SEC.gov Staff Report on Equity and Options Market Structure](https://www.sec.gov/files/staff-report-equity-options-market-struction-conditions-early-2021.pdf)]

> **Short squeezes tend to occur more often in smaller-cap stocks, which have a very small float** (supply), but large caps are certainly not immune to this situation.

[[Investopedia What Short Interest Tells Us](https://www.investopedia.com/articles/01/082201.asp)]

#The January 2021 "Sneeze"

>Some institutional accounts had significant short interest in **GME prior to January 2021.61 GME short interest (as a percent of float) in January 2021 reached 122.97%,** far exceeding other meme stocks like Dillard's, Inc. (symbol: DDS) (77.3%), Bed Bath & Beyond, Inc. (symbol: BBBY) (66.02%), National

Beverage Corp. (symbol: FIZZ) (62.59%), Koss Corp. (symbol: KOSS) (0.92%), Naked Brand Group, Ltd. (symbol: NAKD) (7.3%), and [AJMC Entertainment Holdings Inc. (symbol: [AJMC) (11.4%).

[[SEC.gov Staff Report on Equity and Options Market Structure](<https://www.sec.gov/files/staff-report-equity-options-market-struction-conditions-early-2021.pdf>)]

FINRA reported GameStop's short interest at 226% as of 2/9/2021

[FINRA NYSE:GME 2/9/2021](<https://i.redd.it/1vc7zl4yzgg61.jpg>)

>January 27th 2021 1% of all NSCC members were margin called because of idiosyncratic risk in one named stock GameStop

[[2021 Financial Stability Oversight Council Annual Report](<https://home.treasury.gov/system/files/261/FSOC2021AnnualReport.pdf>)]

>"If the short squeeze happens the stock could go to infinity practically because the shorts have to borrow the stock and once there is no more stock to borrow they cannot deliver. So the broker has to buy the shorts at any price. So there is no solution to this unless shorts are liquidated."

Thomas Peterffy

Billionaire Founder and Chairman of IBKR

[[Bloomberg Markets and Finance](https://youtu.be/kV_P8wnY854?t=407)]

##Why did GameStop Short Interest drop after January 2021?

[GME Short Interest 2007-2021](<https://i.imgur.com/Wrob3MR.png>)

>As GME increased in value, price changes in XRT became increasingly driven by those of GME.

Shorting XRT could have served as an indirect, though imperfect, way of shorting GME. In fact, staff observed a large spike in net redemptions of nearly 6 million shares in XRT on January 27, which may be consistent with short selling activity. This redemption activity was generated nearly entirely by ETF market making firms. It therefore was likely the result of net selling of XRT by market participants against market makers (e.g., market makers buying from investors selling short) where the market makers, rather than offsetting those purchases, subsequently redeemed the XRT shares from the ETF sponsor for shares of the underlying stocks. Such shorting could have led XRT to trade either at a premium or discount relative to its NAV depending on market dynamics.

>**While a short squeeze did not appear to be the main driver of events,** and a gamma squeeze less likely, the episode highlights the role and potential impact of short selling and short covering.

[[SEC.gov Staff Report on Equity and Options Market Structure](<https://www.sec.gov/files/staff-report-equity-options-market-struction-conditions-early-2021.pdf>)]

##Market Makers' Role

>The vast majority of GME stock trades executed off exchange in January 2021 were internalized (approximately 80%) as opposed to executed on ATSs.⁽⁹⁹⁾ The market for internalization of GME was highly concentrated, with 88% of internalized dollar volume in January executed by just three wholesalers.⁽¹⁰⁰⁾ Citadel Securities accounted for nearly 50% of internalizer dollar volume during the month, rising to as high as 55% of daily internalized dollar volume twice.⁽¹⁰¹⁾ Virtu Americas accounted for approximately 26% of the internalized volume during January.⁽¹⁰²⁾ While the percentage of GME trading internalized declined during **the last week in January, the absolute volumes executed by internalizing firms during the days of the most intense trading in this period were, in some cases, an order of magnitude larger than what had previously been typical for these firms. For example, Citadel internalized an average of just under \$37 million of GME per day in December 2020.⁽¹⁰³⁾ On January 27, Citadel internalized nearly \$4.2 billion of GME.⁽¹⁰⁴⁾ Similarly, Virtu internalized an average of \$23.4

million of GME each day in December 2020 and \$2.2 billion of GME on January 26.⁽¹⁰⁵⁾ On January 29, Citadel internalized approximately \$2.2 billion of GME stock, while Virtu internalized approximately \$1.4 billion.⁽¹⁰⁶⁾

[[SEC.gov Staff Report on Equity and Options Market Structure](<https://www.sec.gov/files/staff-report-equity-options-market-struction-conditions-early-2021.pdf>)]

##SEC Conclusions

[Figure 6](<https://i.imgur.com/PjB8y9h.png>)

>Figure 6 shows that the run-up in GME stock price coincided with buying by those with short positions. **However, it also shows that such buying was a small fraction of overall buy volume,** and that GME share prices continued to be high after the direct effects of covering short positions would have waned. The underlying motivation of such buy volume cannot be determined; perhaps it was motivated by the desire to maintain a short squeeze. Whether driven by a desire to squeeze short sellers and thus to profit from the resultant rise in price, or by belief in the fundamentals of GameStop, ***it was the positive sentiment, not the buying-to-cover, that sustained the weeks-long price appreciation of GameStop stock.***

[[SEC.gov Staff Report on Equity and Options Market Structure](<https://www.sec.gov/files/staff-report-equity-options-market-struction-conditions-early-2021.pdf>)]

##XRT Price and Short Interest

[ORTEX ARCA:XRT](<https://i.imgur.com/a2N3Bv5.png>)

##NSCC Financial Stability (Clearing House)

>**The maximum backtesting deficiency, or margin breach, at DTCC's FICC clearing services fell off for the twelve months ending March 31, 2021 as market volatility observed in the first quarter of 2020 rolled off** (Chart 3.6.1.2). In contrast, NSCC reported a backtesting deficiency of \$1.1 billion on January 22, 2021, the largest since public disclosure began in the third quarter of 2015. In its quarterly Principles for Financial Market Infrastructures (PFMI) disclosure, **NSCC attributed the backtesting deficiency mainly to a single security exhibiting idiosyncratic risk.**

[[NSCC 2021 Financial Stability Oversight Council Annual Report](<https://home.treasury.gov/system/files/261/FSOC2021AnnualReport.pdf>)]

##Total Return Swaps

How did Archegos manage to get away by not disclosing its positions?

>**Archegos is estimated to have managed about \$10 billion of its own money, according to people familiar with the fund. Its total positions that were unwound approached \$30 billion thanks to leverage Archegos obtained from banks.**

[[WSJ What Is a Total Return Swap and How Did Archegos Capital Use It?](<https://www.wsj.com/articles/what-is-a-total-return-swap-and-how-did-archegos-capital-use-it-11617125839>)]

>**These losses were made possible due to the unique characteristics of total return swaps and Archegos' formation as a family office, both of which permitted Archegos to skirt trading regulations and reporting requirements.** Archegos essentially purchased beneficial ownership in large amounts of stocks, particularly ViacomCBS Inc. and Discovery Inc., on credit. Under Regulation T of the Federal Reserve Board, up to 50 percent of the purchase price of securities can be borrowed on margin. However, to avoid these rules, Archegos instead entered into total return swaps with the banks whereby the bank is the actual owner of the stock, but Archegos would bear the risk of loss should the price of the stock fall and reap the benefits if the stock were to go up or were to make a distribution.

[[Social Science Research Network - Total Return Meltdown: The Case for Treating Total Return Swaps as Disguised Secured Transactions](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4065946)]

>According to reports by Bloomberg and The Wall Street Journal, Archegos built up these positions through a derivative instrument called total return swaps. **According to this Forbes report, family offices are required to report stock and derivative positions above \$100 million in 13-f filings on the Securities Exchange Commission's EDGAR website. However, swaps are excluded from 13-f filings.**

[[CNBCTV Explained: Why regulators failed to spot the ticking time bomb at Archegos](<https://www.cnbctv18.com/market/stocks/explained-why-regulators-failed-to-spot-the-ticking-time-bomb-at-archegos-8806301.htm>)]

##Swap Reporting Delayed until October 2023

>The Commodity Futures Trading Commission's Market Participants Division today issued a time-limited no-action letter concerning capital and financial reporting obligations for swap dealers (SDs) subject to capital requirements of a prudential regulator (Bank SDs) under the CFTC's SD financial reporting rules.

>**The no-action letter was issued in response to a joint request received from the Securities Industry and Financial Markets Association and the International Swaps and Derivatives Association on behalf of their SD members who are otherwise required to comply by October 6, 2021 with the CFTC's newly adopted capital and financial reporting requirements.** The relief granted by the letter would expire on the earlier of October 6, 2023 or the adoption by the CFTC of any revised financial reporting and notification requirements applicable to such Bank SDs.

[[CFTC Staff Provides Temporary No Action Relief from Certain Financial Reporting Requirements to Bank Swap Dealers](<https://www.cftc.gov/PressRoom/PressReleases/8422-21>)]

#Current Market Conditions

[Inflation rises to highest level since 1981](<https://i.imgur.com/g5Ruues.jpeg>)

##Reverse Repo Rate

>***"With more market rates threatening to go negative (either explicitly or through deposit fees), pouring money into the RRP facility at a zero rate is the least painful alternative,"** said Lou Crandall, chief economist at Wrightson ICAP, in an email to MarketWatch.

[[MarketWatch Why demand for Fed's reverse repo facility is surging again](<https://www.marketwatch.com/story/why-demand-for-feds-reverse-repo-facility-is-surging-again-11621904689>)]

>The amount of money parked at a major Federal Reserve facility **climbed to yet another all-time high, surpassing the \$2 trillion milestone for the first time, as investors struggled to find places to invest their cash in the short term.**

[[Bloomberg Fed Facility Tops \$2 Trillion as Investors Scramble to Park Cash](<https://www.bloomberg.com/news/articles/2022-05-23/fed-s-reverse-repo-facility-exceeds-2-trillion-for-first-time>)]

[Overnight Reverse Repurchase Agreements: Treasury Securities Sold by the Federal Reserve in the Temporary Open Market Operations](<https://i.imgur.com/q5sqtn.png>)

[S&P; 500 March 2019 - June 2022](<https://i.imgur.com/gIDm926.jpg>)

[Global Cryptocurrency Market Capitalization August 2020 - June 2022](<https://i.imgur.com/7ie6Q2N.png>)

#The GameStop Squeeze is Inevitable

##Thesis

Shorts have not closed, some of the biggest market makers and institutions have been trying to hold a beach ball (GME) underwater for the last 18 months.

##Risks v. Reward: Risks of Investing in a Short Squeeze

>Contrarian investors may buy stocks with heavy short interest in order to exploit the potential for a short squeeze. A rapid rise in the stock price is attractive, but it is not without risks. **The stock may be heavily shorted for good reason, such as a dismal future outlook.**

[[Investopedia Short Squeeze Definition](<https://www.investopedia.com/terms/s/shortsqueeze.asp>)]

##GameStop Fundamentals

Cash and Cash equivalents of \$1.035B

Merchandise Inventories of \$917.6M

[[GameStop 10-Q Quarterly Report](<https://news.gamestop.com/static-files/5df55006-eb2-478e-8058-d88a7b5b3d88>)]

[GMEdd Tech Hire Database](<https://www.gmedd.com/report-model/>) - From February 2021 to-date GameStop has hired 428 executives and engineers from Amazon, Chewy and more.

##Borrow rates are above January 2021 levels

[ORTEX NYSE:GME](<https://i.imgur.com/VxePpw3.png>)

>Lending fees to borrow GME were around 25% in January 2021 and fell as short interest began to decline into February 2021.

[[SEC.gov Staff Report on Equity and Options Market Structure](<https://www.sec.gov/files/staff-report-equity-options-market-struction-conditions-early-2021.pdf>)]

##Insider Buying

INSIDER TRADE	3 MONTHS	12 MONTHS
Number of Shares Bought	112,500	257,633
Number of Shares Sold	743	2,833
Total Shares Traded	113,243	260,516
Net Activity	111,757	254,750

[[NASDAQ GME Insider Activity](<https://www.nasdaq.com/market-activity/stocks/gme/insider-activity>)]

##Negative Beta

What Is Beta?

>Beta is a measure of a stock's volatility in relation to the overall market. **By definition, the market, such as the S&P; 500 Index, has a beta of 1.0, and individual stocks are ranked according to how much they deviate from the market.**

>Negative beta: **A beta less than 0, which would indicate an inverse relation to the market, is possible but highly unlikely. ** Some investors argue that gold and gold stocks should have negative betas because they tend to do better when the stock market declines.

[[Investopedia What Beta Means When Considering a Stock's Risk](<http://investopedia.com/investing/beta-know-risk/>)]

[Zacks GameStop Fundamental Charts Beta](<https://i.imgur.com/IPuFkr9.png>)

##Utilization Rate

>The utilization rate is the number of shares borrowed divided by the number of shares that institutional investors are willing to lend. **A higher rate indicates that more of the supply of shares in the securities lending market is being borrowed. A higher utilization rate also increases the likelihood that short sellers could face a buy-in if investors recall their loaned shares.**

[[Seeking Alpha Stocks with the largest increase in utilization rate](<https://seekingalpha.com/instablog/682063-shortside/149448-stocks-with-the-largest-increase-in-utilization-rate>)]

[GameStop Utilization Rate](<https://i.imgur.com/fADB8n5.png>)

##Reported Short Interest

Exchange Reported short interest is up to 24% of the free float and ORTEX estimated short interest is up to 28%.

[ORTEX NYSE:GME](<https://i.imgur.com/b2tn2f7.png>)

>In early 2020, Tesla was the most-shortest stock on the U.S. exchanges, with more than 18% of its outstanding stock in short positions. From late 2019 through early 2020, Tesla stock soared by 400%.

[[Investopedia Short Squeeze Definition](<https://www.investopedia.com/terms/s/shortsqueeze.asp>)]

##Stock Split Dividend

>**GameStop plans to seek shareholder approval for a stock split in the form of a dividend. ** If approved, the stock split would increase the number of GameStop Class A common shares from 300 million to 1 billion.

[[Investopedia GameStop (GME) Flags Stock Split, Shares Surge](<https://www.investopedia.com/gamestop-flags-stock-split-shares-surge-5224459#:~:text=Key%20Takeaways,300%20million%20to%201%20billion.>)]

GameStop shareholders approved the amendment to increase the number of authorized shares of Class A Common Stock [the "common stock"] to 1,000,000,000 on June 2, 2022

>Shareholders of dividend-paying companies as of the record date are entitled to collect declared dividends. **If, however, you are short a dividend-paying stock, you are not entitled to receive the dividend and must pay it instead to the lender of the borrowed shares.**

[[Investopedia Are Investors Short a Dividend-Paying Stock Entitled to the Dividend?](<https://www.investopedia.com/ask/answers/042215/if-investor-short-dividendpaying-stock-record-date-are-they-entitled-dividend.asp>)]

##Direct Registration of Shares

What is Direct Registration v. Street Name?

>You may have your security registered in street name and held in your account at your broker-dealer. Many brokerage firms will automatically put your securities into street name unless you give them specific instructions to the contrary. **Under street name registration, your firm will keep records showing you as the real or "beneficial" owner, but you will not be listed directly on the issuer's books.** Instead, your brokerage firm (or some other nominee) will appear as the owner on the issuer's books.

[[SEC Holding Your Securities Get the Facts]](<https://www.sec.gov/reportspubs/investor-publications/investorpubsholdsechtm.html#:~:text=Under%20street%20name%20registration%2C%20your,owner%20on%20the%20issuer's%20books.>)

##What does DRS do?

[Flow chart demonstrating shares held in ComputerShare remove the stock from the DTC](<https://i.imgur.com/acXwGGI.png>)

##A Closing Exit

As of today shareholders have directly registered over 43% of GameStop's free float.

[GameStop's Available Float with Retail DRS subtracted](<https://i.imgur.com/4DWLRKI.png>)

[[ComputerShared.net]](<https://www.computershared.net/>)

#In Conclusion

Shorts have not closed. Markets are on edge and GameStop becomes more illiquid with each day that passes. MOASS will come and when it does it will be unlike anything the markets have seen before.