Title: How share (re)hypothecation creates counterfeits, and how DRS chips away at float leading to hyper low liquidity
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Disclaimers

* I'm not a financial/investment advisor, and none of what's stated here is any sort of advice
* I'm not experienced in memes, so apologize if I've messed it
* Some of the terminologies here are built on my last post, am not copy-pasta-ing for brevity
* My understanding is based on what I've read and heard, so there will likely be mistakes. This effort is for others like me to discuss and have constructive dialog
* This post is not to predict ***when*** squeeze begins. I believe the company, it's leadership, and direction are solid; they have huge growth potential
* I'm also a long term investor, and believe in Buffet's quote:

>Stock market is a device to transfer money from the impatient to the patient

* Having said that, when moass happens, I won't be disappointed. Though I might lose some sleep

#

TL;DR

* Hypothecation is a common practice of pledging asset to lender when buying asset
* Rehypothecation is an uncommon practice of pledging of pledged assets for money
* In stock market there's no return date for loans, this makes borrowing as safe as owning, as long as the underlying securities are *somewhere* in the system
* In reality investors/traders are holding on to borrowed shares or IOUs (aka counterfeit shares)
* SHFs are banking on investors/traders paperhanding when price keeps dropping without hope
* The principle of (re)hypothecation is that there is access to underlying asset/security in the event of borrower's default
* With DRS, the underlying security vanishes away from DTCCs control to owners name
* This increases counterparty risk for DTCC, especially as real shares become scarce due to DRS
* NSCC is the central counterparty for all equities transactions, so they carry all the risk
* With DRS, SHFs need to post value of 2 shares for every 4 shares DRS-ed; they also have to post more collateral when price goes up, or if price swings (volatility)
* This leads to hyper low liquidity and several scenarios, where any buying/buy-back pressure will induce sharp and uncontrolled price increase (moass)

Terminologies

Few terms have already been covered in this [post](https://www.reddit.com/r/DDintoGME/comments/q33pu5/share_counterfeiting_drs_and_where_we_may_be/)

[**Hypothecation**, from Investopedia](https://www.investopedia.com/terms/h/hypothecation.asp):

>Hypothecation occurs when an asset is pledged as collateral to secure a loan. The owner of the asset does not give up title, possession, or ownership rights, such as income generated by the asset. However, the lender can seize the asset if the terms of the agreement are not met.

In simpler terms, it's borrower giving rights on asset to lender in case of payment default.

[**Rehypothecation**, from Investopedia](https://www.investopedia.com/terms/r/rehypothecation.asp)

>Rehypothecation is a practice whereby banks and brokers use, for their own purposes, assets that have been posted as collateral by their clients. Clients who permit rehypothecation of their collateral may be compensated either through a lower cost of borrowing or a rebate on fees.

In simpler terms, it's lender (mis)using assets posted as collateral by borrower, for further lending

Shares and counterfeit shares

* Shares are securities that represent full or fractional claim on underlying security/basket-of-securities
* GME^(DTC) is a DTCC (derived) security that represents certain benefits of owning the underlying GME^(GM)**^(E)** share, referred to as `global securities` in Gamestop's prospectus
* GME^(DTC) is the the one traded by brokers and exchanges (`dematerialized` security) whereas GME^(GME) is held in one place (`immobilized`)
* Counterfeit shares are basically IOUs (unsettled asset purchases) without `term` i.e. they have no hard return-by date
* When a share is shorted, it's *indefinitely borrowed*, so long as the lender does not recall. This creates **hypothecated share** GME^(HY)
* When no shares are available to short, a hypothecated share is *indefinitely borrowed* by paying full cash value plus risk premiun (`haircut`) as collateral. This creates **rehypothecated share** GME^(DTC-RE)
* Key to understanding counterfeiting is that **(re)hypothecation becomes an issue when there is no term (return date)**, only lenders can force recall. But **lenders are part of securities hedge-fudgery**
* It's not clear how (re)hypothecation) is tracked as shares are non-serialized and fungible. DTCC offers `guaranteed locate` service for institutional investors, so there are mechanisms (`locate control id`) to track real shares that are free of claims
* A buyer does not see whether they bought a real share or (re)hypothecated share (IOU)
* I'd like to use the term `counterfeit share` vs IOU/re(hypothecated) share, because the seller claims them to be shares and not otherwise – which is plain false marketing

Following illustrations are oversimplified

* Apes can have multiple accounts with, and across brokers
* Broker-Dealers, Prime Brokers, and Market Makers hold inventories of shares, and they can lend between themselves, with DTCC being the record keeper
* Pool-a-del ■ represents SHFs (short market makers colluding with short hedge funds/short prime brokers) and is not one entity
* The clearing process is much more involved, [here's DTCC resource](https://dtcclearning.com/products-and-services/equities-clearing.html) for details

Hypothecation

* In this case, we're assuming there are 4 shares issued by Gamestop
* DTCC in turn issues 4 GME^(DTC) derivative shares that have been bought by three apes
* DTCC actually has ***4 more shares that are owned by institutions and funds***; bringing float to 8
* Institutional/fund holding is not in the illustrations to keep it simpler – I'll just talk to it
* When apes buy more shares than there is float, SHFs sell borrowed shares to the extent that real shares exists to lend
* Market participants holding inventories in this case, have lent assets to SHFs for interest rate

* DTCC sees that there are more shares than issued, so they conveniently let market participants ***park*** them in [Obligation Warehouse](https://www.dtcc.com/clearing-services/equities-clearing-services/ow)
* So apettes and apes, the float has been doubled, or **issuer's share-value is halved just like that!**

https://preview.redd.it/tninsmo5bps71.png?width=827&format;=png&auto;=webp&s;=e2629ec97b8dfdaf1c9ed2e10a5136afd6b45bf9

Re-hypothecation

* More apes are interested in the company and want to buy shares
* Poop-a-del don't want to disappoint them (wink wink); plus they expect to buy it back at a lower price later
* All real shares have been borrowed now, so they ***borrow the borrowed shares***
* Only in this case, they have to post full value of share as collateral plus haircut (volatility risk premium)
* The money they gained by selling shares, plus some, is now locked-up
* This is not an issue as long as the price does not move up; because if price moves up they have to pay delta collateral
* They also need to keep the price swings (up/down) in check, because `volatility` increases haircut
* In effect, they are losing some money, but are adding bigger and bigger risks
* They're able to ***suppress price*** and ***raise money by PFOF*** – payment for order flow
* PFOF allows them to front-run your transactions and avoid immediate purchase from lit-exchanges, so **buying pressure does not translate to price increase**
* It's a form of price manipulation that has been unchecked in the past – wonder who let it slide under the table
* Sidebar point: They are campaigning heavily against new SEC lead's attempt to ban PFOF because it'll be their death knell

https://preview.redd.it/i3eist27bps71.png?width=827&format;=png&auto;=webp&s;=fb9e7014bd272e69984f4d4a39e47f193757b9cd

The situation

* As apes continue to buy, they've sold \~4x the float, i.e. 32 shares accounting for institutional holding *(numbers in same post linked above for terminologies)*
* The number of counterfeit shares is **DOUBLE** of what's illustrated here
* I don't know how to illustrate accurately it without making a mess (which the situation actually is)
* Poop-a-del have locked up over $25B of customers capital in collateral, with every dollar increase in price and/or haircut straining their cashflow
* Every day, where short sale volume exceeds long sales, they make the problem worse
* If they short attack furiously triggering SSR, volatility increases, which increases haircut; plus apes have developed taste for discount
* If they let it go sideways, they're slowly bleeding cash
* If they let buying pressure increase price, they bleed faster
* Put another way, **time is not their friend** – they want you to become impatient and impulsive – exactly how they're feeling now, so ape's best reaction would be to stay calm and carry on

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Purple ring effect

* When an ape puts purple ring on their share, that GME^(GME) is transferred to **their name** away from **street name**; GME^(DTC) has to be retired
* GME^(HY) now has to be re-hypothecated with full collateral
* Applying law of averages, **for every 4 share that is DRS-ed, SHFs have to post value of 2 full shares** as additional collateral
* GME^(RE) has be rehypothecated again, this is likely just additional accounting
* But the ratio of real shares to counterfeit shares (i.e. counterparty risk) increase exponentially; this should alarm any risk manager

[DRS Counterparty Risk Profile](https://preview.redd.it/14gdb7u9bps71.png?width=1582&format;=png&auto;=webp&s;=1f680a9339b95948b92d5a74cebcdc979349bf3d)

https://preview.redd.it/s1la9g2bbps71.png?width=827&format;=png&auto;=webp&s;=a85ecb0e7fd2a55b2743b940fa0392f94947ca84

Purple ring on counterfeit share

* When ape with counterfeit shares want to DRS them, **brokers have to swap it out for real shares** from their inventory (another unwitting account), or, beg/borrow from other market participants
* Of course, the official word from them would be something along the lines of "*due to high volume, our back-office resources are overworked, extending the processing timeline*"

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When DRS gets close to float

* When there are more DRS requests than available shares, few things could happen:
* Brokers/SHFs put pressure on institutions to shed their share so keep order
* When that fails, there will be some failed DRS due to "system issues"
* Eventually word gets out on the street that, there are no shares left in `street name`
* This will indicate that the float is locked, or is pretty close to it

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Full float lock

* When DTCC is left with no float, or, very little float that's guaranteed to institutions – liquidity is gone
* SHFs counterparty risk will be at all time high, volume traded will be at all time low
* FUD will be intense from all angles; DTCC will look for a *narrative* to spin it's involvement
* Investors who backed SHFs will be putting intense pressure to exit quickly
* We will be in uncharted territory, so a lot of things could happen
* Due to low liquidity, any buying pressure on lit market will launch a squeeze

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End game scenarios

There could be many ways this can play out, I can think of four scenarios:

1 - Even before the float is locked, SHFs may run out of money to post as collateral because

* Earnings are great and institutional buying pressure triggered gamma squeeze
* SHFs fail to maintain steady price, so volatility increases, and they're unable to post haircut

2 - Someone in DTCC's risk department has "Oh Shit" moment like in the movie *Margin Call*, and decide to throw `bad actor(s)` under the bus

* Not unlike to how Lehman Brothers was sacrificed during 2008 financial crisis

3 - Gamestop pulls the plug on having their shares at DTCC, because their fully issued shares are `directly owned` as per Computershare

* [Page 37 para 2 of Gamestop's June 424B5 filing](https://news.gamestop.com/static-files/4ef3fc60-b489-42e3-9436-1c6f55c772fa), states that if DTCC fails in it's obligation they can issues securities directly, making DTCC shares illegal

>If a depository for a series of securities is at any time unwilling, unable or ineligible to continue as depository and a successor depository is notappointed by us within 90 days, we will issue individual securities of such series in exchange for the global security representing such series ofsecurities. In addition, we may, at any time and in our sole discretion, subject to any limitations described in the applicable prospectus supplementrelating to such securities, determine not to have any securities of such series represented by one or more global securities and, in such event, will issueindividual securities of such series in exchange for the global security or securities representing such series of securities.

4 - Gamestop issues NFT/Krypto dividend that does not have cash value

* If Gamestop issues krypto dividend, especially non-fungible type (NFT), and a cash value cannot be established
* Then, DTCC will be unable to fulfill it's obligation to beneficial owners via Broker-Dealers
* SHFs will be forced to close their position; all the while SHFs keep pressuring Gamestop to name a price equivalent for NFT/Krypto

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EDIT: formatting; EDIT 2: Added missing Buffet quote

EDIT 3: replaced TA;DR with TL;DR; EDIT 4: updated incr. # of shares that need full collateral (1 to 2)