Aviator Update – February 2021
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AVIATOR CAPITAL

Markets in the age of the "influencer"

It's now late February, which means the majority of summer has already passed us by. Weather-wise, however, it seems that summer has only just arrived to my part of the Australian east coast – seemingly endless days of that fine, warm weather we normally associate with summer replacing seemingly endless days of cool and wet.

Taking advantage of the proper summer weather, I've by-passed the usual gym routine some mornings and instead taken a long walk for my morning cardio. This often sees me by the beach at sunrise. Over the past weekend, I had plenty of company at sunrise.

There were people everywhere - the water filled with surfers, people walking or running along the beach, sitting enjoying a coffee or a bike ride... However, my attention was mostly captured by the number of people with their phones out taking photos of the sunrise. For many, it seemed to be their only purpose – pulling up in their cars and jumping out to snap a few pics before promptly jumping back in the car and speeding off.

At the risk of offending anyone, I just find this perplexing. Why do this? Is "now" not good for them – "I'll take a photo and savour it later." Perhaps they are fearful the sun won't rise again tomorrow?

But of course, we know that in this day and age many of these images are destined to find their way onto the internet. Maybe with some inspirational quote:

"Each day is a new opportunity to improve yourself. Take it and make the most of it."
"The biggest adventure you can take is to live the life of your dreams."
"Do something today that your future self will thank you for."
"The best time for new beginnings is now."

… or other such un-original quotes Googled-up in the same way I found these in 30 seconds.

For these people, whether its conscious or not, they are seeking to influence others. They might not be what we would refer to as an "influencer" (i.e. someone deliberately seeking to influence others, often for financial gain), but they are still trying to grab people's attention and influence the way they are thinking and feeling at that moment.

Me being 'me', my mind shifted to thinking what impact this whole "influencer culture" is having on financial markets. In today's world, the online-world is the centre of many individuals' existence – especially when much of the world remains in some degree of "Covid lockdown".

One outcome of the internet era has been that we need not be subjected to an opinion that differs from our own – we can opt to visit only those websites that reflect our world view – re-enforcing what we already believe. Of course, that's not an original thought – it's been a trend for 20 years and you may hear it referred to as 'confirmation bias'.

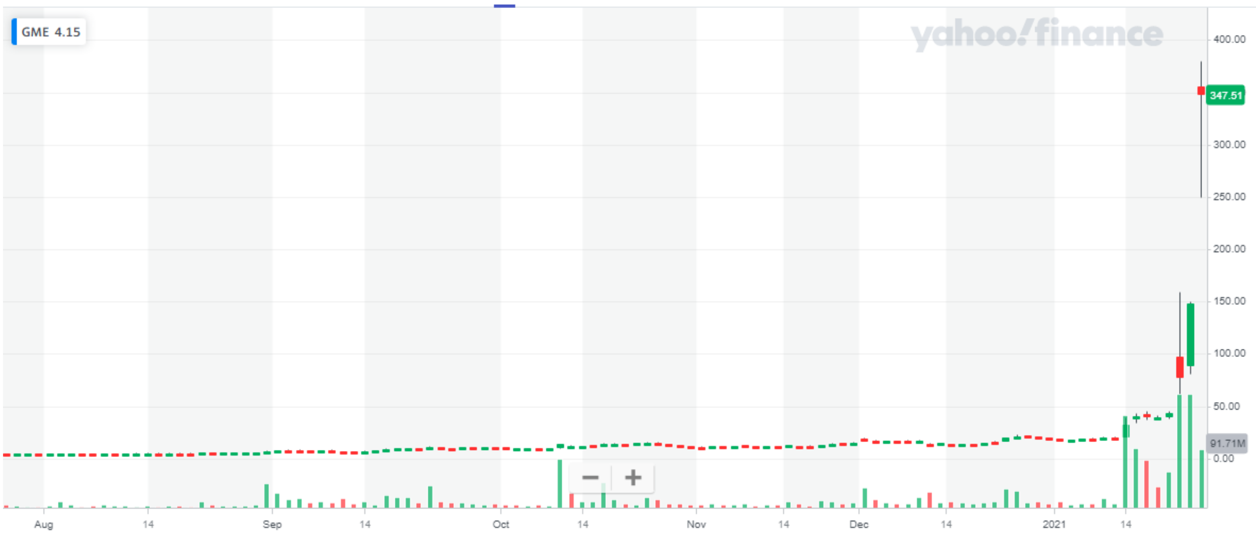
Financials markets are perfect for "influencers" – always have been. Investing is something almost everyone in the developed world engages in (whether directly or passively). The industry is therefore huge. There are fortunes to be made (and lost) and, most importantly, <u>nobody</u> knows what tomorrow will bring to financial markets. Its binary – up or down. And therefore anyone can be right and everyone's opinion can be valid.

Coincidentally, the market recently handed us one amazing example of what appears to be the handywork of "influencers". A NYSE-listed company called GameStop. Here's the company profile from Yahoo Finance:

GameStop Corp. operates as a multichannel video game, consumer electronics, and collectibles retailer in the United States, Canada, Australia, and Europe. The company sells new and pre-owned video game platforms; accessories, including controllers, gaming headsets, virtual reality products, and memory cards; new and pre-owned video game software; and in-game digital currency, digital downloadable content, and full-game downloads, as well as network points cards, and prepaid digital and prepaid subscription cards. It also sells collectibles comprising licensed merchandise primarily related to the video game, television, and movie industries, as well as pop culture themes. The company operates its stores and e-commerce sites under the GameStop, EB Games, and Micromania brands; and collectibles stores under the Zing Pop Culture and ThinkGeek brand, as well as offers Game Informer, a print and digital video game publication featuring reviews of new title releases, game tips, and news regarding the video game industry. As of February 1, 2020, the company operated 5,509 stores across 14 countries. The company was formerly known as GSC Holdings Corp. GameStop Corp. was founded in 1996 and is headquartered in Grapevine, Texas.

The highest its shares have been in the last 5 years is about $30. Its spent much of the last 12 months between $5 and $10. You see, fundamentally, the outlook is not considered too rosy for this business – essentially a dying "bricks and mortar" store that has failed to keep up in this online world.

And then this happened:



The numbers on the chart are a bit small, but you're seeing that correctly – the stock has gone from around $20 to well north of $350 in a handful of sessions! Incredible!

What's the news? Surely something completely transformative – a crazy takeover offer? Discovered the world's largest oil reserve under their Texas office? Cured Coronavirus?

No – there's been no news. Or actually to be more accurate - "*price is news*".

The stock has been the benefactor of an amazing collusion of influencers. Some supposedly young, amateur traders discovered that GameStop had a massive outstanding "short interest" – positions taken by traders expecting a decline in the stock. It's reported that an incredible 140% of the shares on issue were sold short. This sort of data is collated and reported by the exchanges so we shouldn't doubt its accuracy. And it is absolutely possible for short interest to exceed shares on issue – the same shares can be borrowed and short-sold multiple times.

It's also possible to get an understanding of which entities are short the stock – many larger investment firms have reporting obligations that provide a glimpse into what positions they hold.

So… these traders got on internet forums and managed to create a frenzy. They explained that the shares are being sold short by evil banks and hedge funds… that there's the opportunity to really screw them over. If we all band together and buy this thing we will cause huge losses for said evil hedge funds who are perpetually manipulating markets and screwing the little guy with their collusion, corruption and general evil-ness.

It worked. Spectacularly. It appears they managed to rally literally millions of small investors.

Its speculation in its purest sense. Even most of these inexperienced investors know the price is totally unjustified. They don't care. They are convinced that they will be able to sell their stake to someone else at a higher price. There's no real "plan" – no specific price target

– either to buy at or to sell at. This a big part as to why the increases are so incredible – the buyers literally do not care what price they pay. They have been promised that if we all buy, we, the little guys, will all make money and we will screw over the big bad hedge funds in the process!

Or course, by definition somebody has to buy at the top. Wherever that might be during a speculative frenzy such as this, *somebody* will have to buy the absolute top in order for that top transaction to occur. It follows that *somebody* (in fact many people) will end up holding the bag, given that every share has to be held by someone at every point in time. Most of these traders do know this… it's just that they are confident it won't be them!

This internet influencer-driven, "crowdsourced" speculative frenzy is clearly new – we've never quite seen this before. But if we think harder about it, we basically have.

To a large extent, this is nothing more than a good old "pump-and-dump" scheme. Buy some shares… promote the company as the next amazing thing and then (hopefully) sell into the strength you've created.

The subtle difference is that the pump-and-dump generally requires you to make up the story - the spreading of mis-information - therein making it an illegal practice. But this new scheme doesn't rely on mis-information – you're simply influencing people to buy something on the basis that it will go up and they will make money. Everyone will make money!

Above, I described these traders as "supposedly young, amateur traders". Whilst that's probably true, I can't help but wonder whether a bunch of big, bad hedge fund guys are in fact behind some of this. Its genius – tap into the growing resentment of "the establishment" along with the extreme speculative impulses present in the current environment and put them together to trigger the most epic short squeeze in history!

Turning back to the broader markets, I'm increasingly of the opinion that US equity markets are in the final stages of this long bull market that began after the Global Financial Crisis of 2008. When looking back through history, there's a number of hallmarks that tend to be present at market peaks. One of those is a surge in speculative behaviour, particularly amongst "retail investors".

We note from history that during such episodes, the stock market gets a lot of coverage and attention… but "news" tends to dry up. We enter this "price is news" state where the only financial news to report is really that prices have gone higher and this alone is enough to encourage further interest in the markets. Take Bitcoin for example…

If everyone would like to pull out their "indicators of a market bubble" checklist from their top drawer... I think we can safely tick "explosion in crazy speculative behaviour amongst retail investors" off the list.