

MAKING SENSE OF *THIS* WORLD

1 February 2021



R&R Weekly Column
By Brunello Rosa



Market Lilliputians At War Against “The System”

Last week, media attention was attracted by the epic fight between day traders and the giants of Wall Street. [That story is largely known now](#). Thousands of retail investors, organising themselves on platforms such as [Reddit](#) and trading on [online exchanges such as Robin Hood](#), have been purchasing the shares of the moribund company [GameStop](#) (considered a sort of “Blockbuster” for gaming), a company that funds such as Melvin Capital, which specialises in equity long/short strategies, had been heavily shorting in previous months.

With the price of the stock rising from \$17 per share on January 4th to \$347 on January 27th, those funds were scrambling to purchase the stocks they needed to cover their short position. But the extent of the bet was such that those shares did not exist, resulting in their prices being pushed up [at the speed of light](#). Eventually, regulators such as the SEC decided to intervene, to calm a market dynamic that was becoming uncontrollable, with retail investors prevailing against hedge funds and [Melvin Capital closing its short position and needing to be rescued by its competitors](#). [As the theory says](#), to be successful a speculative attack needs coordination among the agents involved in it, and a coordinated signal that suggests when the attack should start. The Reddit community had both.

Taking sides in an issue of this sort is hard. One could feel sympathy for [the market Lilliputians revolting against the giants of Wall Street, and especially the millennials behind this movement](#). Nevertheless, the coordination of actions in this way is dangerously close to market manipulation. Hedge funds do not attract popular sympathy, especially hedge funds that short the equities of struggling companies and so can result in the bankruptcy of businesses that might have otherwise survived. But this very strategy – shorting – is also the one instrument that market participants have to signal inefficiencies in the management or unviability of business models.

As for the regulators, they are supposed to be the guardians of the market but tend to act too late, when the damage has already been done. Often, during severe market corrections, some regulators also ban short selling altogether, leaving the impression that market forces should be left free to act only if they push market prices up (the so-called [Bernanke Put](#) – now the Powell put).


In the end, it does not really matter who is the good guy in this story, and who is the felon. The real question is what this episode signals, and what the lessons are that must be learnt. It seems to us that this “Reddit army” is following the tradition of fight-the-system/anti-globalisation movements that started with the [Seattle WTO protests at the end of the 1990s](#) (remember [Naomi Klein’s “No Logo”](#)?) and continued with protests such as [Occupy Wall Street](#). One could even claim that the entire crypto-asset movement (net of its abundant scams, illegal activities and manipulation) was originally a way to disrupt “the System”.


So, there is a *fil rouge* that connects all these protest movements in their [“rage against the machine”](#), represented in dystopian movies such as [The Matrix franchise](#). But one needs to be careful here. History teaches us that most revolts and revolutions aimed at democratising the system end up with autocratic regimes or even ferocious dictatorships. Even the mother of all revolutions, the French Revolution of 1789, ended up with Napoleon’s empire and eventually the “restoration” of the Congress of Vienna.


The revolutions of 1848 (the year in which the Manifesto of the Communist Party by Karl Marx was published), which led to the temporary fall of many absolutist monarchies in Europe, similarly ended up with the [election of Napoleon III to become the President of France](#). He too later became Emperor and an absolutist ruler. On a much smaller scale, the anti-globalisation sentiment prevailing among the middle- and low-income classes in the United States was eventually channelled by a plutocrat from New York: Donald Trump.

The lessons to learn here seem to be the following: 1) Social malaise due to the restriction and loss of job opportunities induced by the pandemic is leading people to find other sources of income perceived as rapid and safe, such as day stock trading. 2) Central bank liquidity, issued to help banks survive and sovereigns monetise public debts, is making one-way bets too widespread in the markets, thanks to the perceived “Bernanke put”. 3) The financial system seems more de-anchored from economic fundamentals than ever, increasing the chances of all sorts of distortions and manipulations occurring, which can end in devastating market crashes. 4) The revolt of the people by way of coordination through electronic platforms is a signal of the underlying social malaise that, though exacerbated by the pandemic, originated decades ago with the decoupling of salary and productivity growth and the beginning the globalisation process. 5) These events are further confirmation that politics, markets and geopolitics these days are taking place first and foremost within cyber space. Politicians around the world should take note of these events, if they do not want to see this revolt exiting the computer screens and taking to the streets.

Our Recent Publications

 [Emerging Markets Outlook: Economic Recovery In H2-2021, Liquidity To Support Financial Markets](#), by Alessandro Magnoli Bocchi and Fawaz Sulaiman Al Mughrabi, 28 January 2021

 [Preview: FOMC Looking Through the Soft Patch](#), by Nouriel Roubini and Alessandro Magnoli Bocchi, 25 January 2021

 [Flash Review: Federal Reserve Remains On Hold While Sounding Cautiously Upbeat](#), by Brunello Rosa, 27 January 2021

 [GEOPOLITICAL CORNER: Britain After Brexit: The World Did Not End, But A New One Began](#), by John C. Hulsman, 26 January 2021

Looking Ahead

The Week Ahead: US And EZ Unemployment Expected To Stay Unchanged, With Bank of England Remaining on Hold

In the US, in January the non-manufacturing PMI is expected to increase to 57 (p: 52.2), while unemployment is expected to stay unchanged at 6.7%.

In the EZ, December's unemployment rate is expected to remain unchanged at 8.3%, while retail sales are likely to rebound to 0.8% m-o-m (p: -6.1%).

In the UK, the Bank of England is expected to leave its policy stance unchanged.

The Quarter Ahead: Delayed Vaccine Distribution To Weigh On Global Growth; Central Banks To Remain Dovish

In the US, President Joe Biden's USD 1.9tn relief plan - which includes proposals for: i) additional direct checks; and ii) a higher federal minimum wage - is likely to be approved by Congress, thanks to a democratic majority in both the House and the Senate.

Still in the US, throughout 2021, the US Fed is likely to maintain its loose policy stance, even as economic growth accelerates.

In the EU, a slow rollout of COVID-19 vaccines has been blamed on: 1) the European Commission - the institution leading the purchase agreements - for not securing enough doses; and 2) the EU's medical agency "for taking too long to approve jabs that had received the green light elsewhere".

In China, the army sent 26 military aircrafts into the south-western corner of Taiwan's air defense zone, to simulate missile attacks on a US aircraft carrier, according to US intelligence.

Last Week's Review

Real Economy: DM Economic Recovery Remains Fragile; Global Vaccine Distribution Slows

In the US, in Q4-2020 q-o-q GDP rose by 4.0% annualized (c: 4.2%; p: 33.4%), as consumption was hampered by the: i) withdrawal of fiscal support; and ii) resurgence in coronavirus infections. In December: i) 'durable goods orders' decelerated to 0.2% m-o-m (c: 0.9%; p: 1.2%); while ii) 'nondefense capital goods orders excluding aircraft' - a closely watched proxy for business spending plans - rose by 0.6% m-o-m (c: 0.6%; p: 1.0%). December's 'PCE price index' rose to 1.3% (c: 1.1%; p: 1.1%) while 'core-PCE prices' - the Fed's closely watched inflation gauge - rose to 1.5% (c: 1.3%; p: 1.4%).

During its first meeting of 2021, the US Fed left the 'target range for federal funds' rate unchanged at 0-0.25%. The QE monthly program was also maintained at: i) USD 80bn of USTs; and ii) USD 40bn of MBS. In a post-FOMC meeting statement the Fed declared "the pace of the economic rebound" (...) "has moderated in recent months, with weakness concentrated in the sectors most adversely affected by the pandemic". According to the Fed Chairman Powell: i) nearly half a million jobs were shed by the leisure and hospitality sectors in December; and ii) "the economic recovery hinges on vaccination progress".

In the EZ, January's 'economic sentiment indicator' fell by 0.9 pts to 91.5 (c: 89.5; p: 92.4), driven by: i) sliding 'confidence in retail trade'; and ii) smaller-than-expected reductions in 'services confidence' and 'consumer confidence'.

In Japan, December's retail sales fell by -0.3% y-o-y (c: -0.4%; p: 0.6%), driven by lower purchases of general merchandise and fuel.

Financial Markets: Volatility And Trading Volumes Rose, Equities Fell; USD Up, As Safe Haven

Market drivers: Retail investors supported a few "short squeezes", driving heavy price fluctuations in selected stocks.

Global equities closed lower w-o-w (MSCI ACWI, -3.6%, to 643). In the US: i) the S&P 500 Index posted the worst week since October (-3.3%, to 3,714); and ii) total trading volume hit a record high of 23bn shares - a significant increase from the y-t-d average daily volume of about 14bn. In the EZ, European shares fell (Eurostoxx 50, -3.4%, to 3,481) amid worries about a slowing economic recovery, due to: i) the still-raging COVID-19 pandemic; and ii) delays in the distribution of vaccines. Going forward, risky assets are likely to be supported by: 1) the global recovery; and 2) accommodative fiscal and monetary policies.

Fixed Income: w-o-w global bonds remained flat (BAML Global, 0.0% to 297.8), as well as USTs (0 bp, to 1.09%). Going forward, government bond yields are likely to remain at low levels.

FX: w-o-w, the USD traded higher against other currencies (DXY, +0.4%, to 90.584; EUR/USD +0.7%, to 1.217), largely driven by a deterioration in risk appetite; however, as the markets normalize, the USD downward trend is likely to resume.

Commodities: Oil prices rose (Brent, +0.8% to 55.9 USD/b), as China - the world's second-biggest oil user - reported its lowest daily rise in COVID-19 cases, bolstering hopes of a pick-up in demand. Gold fell (0.3% to 1,846 USD/Oz.), as the US Fed kept its monetary policy unchanged without hinting to any more stimulus - supporting the USD as the preferred short-term safe haven asset.

Farah Aladsani contributed to this Newsletter.

The picture in the front page comes from [this website](#)



@RosaRoubini



Rosa & Roubini



Rosa&Roubini Associates

For more information, please call us on +44 (0)207 1010 718 or send us an email to info@rosa-roubini-associates.com

www.rosa-roubini-associates.com

118 Pall Mall, London SW1Y 5ED



Abbreviations, Acronyms and Definitions

a	Actual	LN	Northern League, Italy
AKP	Justice and Development Party, Turkey	MSS	Five Star Movement, Italy
ann.	annualized	m-o-m	Month-on-month
ARS	Argentinian Peso	mb	Million barrels
avg.	Average	mb/d	Million barrels per day
bn	Billion	MENA	Middle East and North Africa
BoC	Bank of Canada	MHP	Nationalist Movement Party, Turkey
BoE	Bank of England	mn	Million
BoJ	Bank of Japan	MPC	Monetary Policy Committee
bpd	Barrels per day	NAFTA	North-American Free Trade Agreement
bps	Basis points	NATO	North Atlantic Treaty Organization
BS	Balance sheet	OECD	Organization for Economic Cooperation and Development
c	Consensus	Opec	Organization of Petroleum Exporting Countries
C/A	Current account	p	Previous
CB	Central bank	P2P	Peer-to-peer
CBB	Central Bank of Bahrain	PBoC	People's Bank of China
CBK	Central Bank of Kuwait	PCE	Personal Consumption Expenditures
CBT	Central Bank of Turkey	PE	Price to earnings ratio
CDU	Christian Democratic Union, Germany	PM	Prime minister
CNY	Chinese Yuan	PMI	Purchasing managers' index
CPI	Consumer Price Index	pps	Percentage points
DJIA	Dow Jones Industrial Average Index	pw	Previous week
DJEM	Dow Jones Emerging Markets Index	QCB	Qatar Central Bank
d-o-d	Day-on-day	QAR	Qatari Riyal
DXY	US Dollar Index	QE	Quantitative easing
EC	European Commission	q-o-q	Quarter-on-quarter
ECB	European Central Bank	RE	Real estate
ECJ	European Court of Justice	RBA	Reserve Bank of Australia
EIA	US Energy Information Agency	RRR	Reserve Requirement Ratio
EM	Emerging Markets	RUB	Russian Rouble
EP	European Parliament	SWF	Sovereign Wealth Fund
EPS	Earnings per share	tn	Trillion
EU	European Union	TRY	Turkish Lira
EUR	Euro	UAE	United Arab Emirates
EZ	Eurozone	UK	United Kingdom
Fed	US Federal Reserve	US	United States
FOMC	US Federal Open Market Committee	USD	United States Dollar
FRB	US Federal Reserve Board	USD/b	USD per barrel
FX	Foreign exchange	UST	US Treasury bills/bonds
FY	Fiscal Year	VAT	Value added tax
GCC	Gulf Cooperation Council	VIX	Chicago Board Options Exchange Volatility Index
GBP	British pound	WTI	West Texas Intermediate
GDP	Gross domestic product	WTO	World Trade Organisation
IMF	International Monetary Fund	w	Week
INR	Indian Rupee	w-o-w	Week-on-week
IPO	Initial public offering	y	Year
IRR	Iranian Rial	y-o-y	Year-on-year
JPY	Japanese yen	y-t-d	Year-to-date
k	thousand	ZAR	South African Rand
KSA	Kingdom of Saudi Arabia	2y; 10y	2-year; 10-year



Rosa & Roubini Associates Ltd is a private limited company registered in England and Wales (Registration number: 10975116) with registered office at 118 Pall Mall, St. James's, London SW1Y 5ED, United Kingdom. VAT registration number GB 278 7297 39. **Analyst Certification:** We, Brunello Rosa and Nouriel Roubini, hereby certify that all the views expressed in this report reflect our personal opinion, which has not been influenced by considerations of Rosa & Roubini Associates's business, nor by personal or client relationships. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the views expressed in this report. **Disclaimer:** All material presented in this report is provided by Rosa & Roubini Associates-Limited for informational purposes only and is not to be used or considered as an offer or a solicitation to sell or to buy, or subscribe for securities, investment products or other financial instruments. Rosa & Roubini Associates Limited does not conduct "investment research" as defined in the FCA Conduct of Business Sourcebook (COBS) section 12 nor does it provide "advice about securities" as defined in the Regulation of Investment Advisors by the U.S. SEC. Rosa & Roubini Associates Limited is not regulated by the FCA, SEC or by any other regulatory body. Nothing in this report shall be deemed to constitute financial or other professional advice in any way, and under no circumstances shall we be liable for any direct or indirect losses, costs or expenses nor for any loss of profit that results from the content of this report or any material in it or website links or references embedded within it. The price and value of financial instruments, securities and investment products referred to in this research and the income from them may fluctuate. Past performance and forecasts should not be treated as a reliable guide of future performance or results; future returns are not guaranteed; and a loss of original capital may occur. This research is based on current public information that Rosa & Roubini Associates considers reliable, but we do not represent it is accurate or complete, and it should not be relied on as such. Rosa & Roubini Associates, its contributors, partners and employees make no representation about the completeness or accuracy of the data, calculations, information or opinions contained in this report. Rosa & Roubini Associates has an internal policy designed to minimize the risk of receiving or misusing confidential or potentially material non-public information. We seek to update our research as appropriate, but the large majority of reports are published at irregular intervals as appropriate in the author's judgment. The information, opinions, estimates and forecasts contained herein are as of the date hereof and may be changed without prior notification. This research is for our clients only and is disseminated and available to all clients simultaneously through electronic publication. Rosa & Roubini Associates is not responsible for the redistribution of our research by third party aggregators. This report is not directed to you if Rosa & Roubini Associates is barred from doing so in your jurisdiction. This report and its content cannot be copied, redistributed or reproduced in part or whole without Rosa & Roubini Associates' written permission.

