AUTORITÉ DES MARCHÉS FINANCIERS

Print from the website of the AMF

18 February 2021

GameStop Mania: a look back over a market phenomenon

In January and early February, financial markets experienced a spell of high volatility focused on certain stocks, mainly in the United States. A look back over the events of recent weeks in a brief series of questions and answers.

What happened in US markets in recent weeks?

In recent weeks, US markets experienced a spell of high volatility focused on certain stocks, during which the prices of equities in which there were significant short positions surged due to strong buying pressure. This pressure was notably fuelled by numerous retail investors, encouraged by certain communities on social media. This buying pressure was magnified by the use of leveraged derivatives, which pushed prices up dramatically, forcing a rush of short sellers to buy back their positions, to limit their losses or meet their margin calls. This is what is known as a short squeeze.

The initial focus of this market move was on GameStop, a company specialised in the distribution of video games, whose shares had been shorted heavily in the preceding months. In January, within a few trading sessions, the GameStop share price went from $20 on 13 January to $347 on 27 January, before falling back very heavily. At the Wall Street close on Friday 5 February, it was worth only $63.77. At the height of this period of speculation, its share turnover ratio on the stock exchange climbed to as much as 200% in a single trading session.

Similar patterns were observed on other stocks in varying proportions. These movements led to a round of buybacks of their positions by short sellers, in anticipation or after suffering heavy losses.

This spike in volatility also led certain US broker platforms, which were no longer able to meet the margin calls demanded by clearing houses, to suspend or restrict trading in certain stocks or products.

The phenomenon spread to other instruments such as silver, to such an extent that the Chicago Mercantile Exchange, on which the US benchmark contracts are traded, decided to increase its margin calls (sums of money or assets deposited as collateral to cover potential market losses).

What factors may have helped exacerbate the movement?

In the United States, the development of low-cost trading brokerage platforms has helped largely democratise access to the stock market in a country where the stock market culture is historically stronger than in France. Some of these platforms operate on a model that is highly attractive for retail investors, because everything is apparently free of charge. They do not charge their clients transaction costs but remunerate themselves indirectly, by directing their flows of orders for trade execution to various partners in exchange for payments (payment for order flow). This compensation varies depending on the profits derived from the flow by the partner brokers, and it may therefore provide an incentive for platforms to propose the products more conspicuously providing them with the best margins, such as highly leveraged products, without this being explicit to clients.

Now, on some of these platforms, it is possible to invest in products that have a significant leverage effect. Using leverage, a trader can invest in the stock market far above than the amount that they have on their account. For example, if they have €1,000 on their account, a leverage of 10 enables them to bet €10,000 in the stock market. However, this leverage mechanism leaves them more vulnerable to price fluctuations: when the trend leans in their favour, their gains will admittedly be increased tenfold, but their losses will be amplified by just as much if the trend is reversed.

Can a stock be lent several times?

Yes. A person holding securities can lend them only once. But an investor who buys securities in the market may have acquired them, unknowingly, from a short seller. In other words, they acquire securities that were borrowed from another investor. Once these securities have been bought, they may in turn decide, likewise, to lend them.

What measures have the US authorities taken?

The Securities & Exchange Commission (SEC) reported twice on this spell of volatility, on 27 and 29 January, stating that it was examining the situation very closely.

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We are aware of and actively monitoring the on-going market volatility in the options and equities markets and, consistent with our mission to protect investors and maintain fair, orderly, and efficient markets, we are working with our fellow regulators to assess the situation and review the activities of regulated entities, financial intermediaries, and other market participants.

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The Commission is closely monitoring and evaluating the extreme price volatility of certain stocks' trading prices over the past several days. Our core market infrastructure has proven resilient under the weight of this week's extraordinary trading volumes. Nevertheless, extreme stock price volatility has the potential to expose investors to rapid and severe losses and undermine market confidence.

As always, the Commission will work to protect investors, to maintain fair, orderly, and efficient markets, and to facilitate capital formation. The Commission is working closely with our regulatory partners, both across the government and at FINRA and other self-regulatory organizations, including the stock exchanges, to ensure that regulated entities uphold their obligations to protect investors and to identify and pursue potential wrongdoing. The Commission will closely review actions taken by regulated entities that may disadvantage investors or otherwise unduly inhibit their ability to trade certain securities.

In addition, we will act to protect retail investors when the facts demonstrate abusive or manipulative trading activity that is prohibited by the federal securities laws. Market participants should be careful to avoid such activity. Likewise, issuers must ensure compliance with the federal securities laws for any contemplated offers or sales of their own securities.

The Commission will continue our work on behalf of investors and the markets. In this regard, we hope to facilitate a robust public dialogue among market participants and investors on the structure and operation of our securities markets. Members of the public can submit tips or complaints through the Commission's website using this online form URL = [https://www.sec.gov/tcr]. Members of the public with questions should contact the Commission's Office of Investor Education and Advocacy URL =

[https://www.sec.gov/page/oieasectionlanding] at 1-800-732-0330, ask a question using this online form URL = [https://www.sec.gov/oiea/QuestionsAndComments.html], or email us at Help@SEC.gov URL = [mailto:Help@SEC.gov].

In early February, the Treasury Secretary, Janet Yellen, called for a meeting with the financial regulatory authorities regarding the recent financial market volatility and the compatibility of recent operations with investor protection and fair, efficient markets.

Could we witness a similar trend in the French market?

Such an episode seems unlikely at present. Today, French equities are far from showing individually a cumulative level of short positions similar to that seen in the United States. They are also far from posting the share turnover ratios observed in the US markets: for CAC 40 and SBF 120 stocks, this ratio is on average around 0.2%, with a median of around 0.3%, and seldom exceeds 1%.

Although new retail investors did enter the market during the Covid-19 pandemic (as in the United States), their number remains comparatively smaller. The number of active investors trading on financial markets via a French financial institution or a French branch of a European Union institution using leveraged products is even smaller.

The average amounts invested, based on observations in 2020 (study on the behaviour of retail investors in the stock market), remain stable. To cause a significant move in a company's share price, large amounts of money are required, and an ability to hold onto positions for a long time without unwinding them, while facing possible risks of losing money, risks that are magnified by any leverage.

However, some share price movements were observed to testify activity on certain French equities, which could, to a lesser extent, bear similarities.

Nevertheless, market practices of retail investors, more inclined to invest for the long term, mechanisms put in place by the regulators([1]), explicit transaction fee with each stock exchange order and market structure with lower share turnover ratios do not seem to be conditions favouring the occurrence of such an episode in France currently, even though it cannot be completely ruled out.

Has the AMF stepped up its supervision?

As part of its remit for market supervision, the AMF closely monitors French stocks constantly, paying special attention when there is a topical event or a risk. To do so we are supported by our systems based on big data technology and artificial intelligence. We also monitor social media, and have done so for many years now. Among other things, we have developed tools to detect messages most likely to influence stock markets and to track scams on social media.

Aware of the growing influence of social media and, with this, greater potential for a new kind of market abuse, we are working on a partnership with the Digital Regulation Expertise Centre (PEReN: Pôle d’Expertise de la Régulation Numérique) of the French Ministry for the Economy and Finance to develop a social media scanning tool for detecting bots possibly creating an impression of mass when only a limited number of people might be at their origin.

On the back of this supervisory work, the AMF may decide to open an investigation and, if it considers that certain behaviours may be qualified as market manipulation, may undertake disciplinary proceedings. Such qualification is always difficult to establish.

As an investor, what are the right habits to adopt?

An investment decision is the result of an analysis of your investment horizon, the composition of your wealth and the risks you are prepared to take. In the stock market, you can lose all or part of your investment.

In recent weeks, certain US and European stocks have posted higher levels of volatility: price trends can reverse rapidly and entail major fluctuations for investors.

And on social media?

Deciding to invest exclusively on the basis of information posted on social media is a strategy that could be risky. It is virtually impossible to verify the source of publications and the reliability of information, and conflicts of interest may not be disclosed. The utmost caution is therefore recommended.

Can a European broker restrict my trading on a stock exchange?

In the absence of specific regulatory provisions, investors should refer to their broker's contractual documentation and general conditions of sale.

[1] In France, for example, given the losses incurred by for retail investors in recent years, measures limiting leverage have been applied to contracts for difference (CFDs) to protect investors and prevent them from losing more than the amount initially invested.

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