AZIMUT
DEFINING INVESTMENT DIRECTION

AZIMUT GLOBAL VIEW

01.
02.
21

Main Events

Azimut Global Network

- Milan
- Abu Dhabi
- Cairo
- Dubai
- Dublin
- Hong Kong
- Istanbul
- Lugano
- Luxembourg
- Mexico City
- Miami
- Monaco
- New York
- Santiago
- São Paulo
- Shanghai
- Singapore
- Sydney
- Taipei

EU CPI — 03.02
The YoY reading is expected to jump by almost 1%, from -0.3% to +0.6%

BoE — 04.02
The Bank of England will publish the results of a consultation about negative rates. Will the BoE adopt this controversial policy?

US PAYROLLS — 05.02
US labour market is expected to remain weak in the first month of 2021

US CPI — 10.02
US inflation should remain substantially unchanged, notwithstanding the growing pressures highlighted by confidence indices

Release the Kraken

What happened in equity markets earlier this year is a modern version of David versus Goliath. Trapped at home in the midst of the pandemic with plenty of time and additional free money received from the new round of government payments, a motley crew of retail traders have given professional investors and hedge funds a run for their money. We won't elaborate on whether or not the approach used, banding together and piling into the most shorted stock, is fair and appropriate. Leaving this to the competent authorities, we will just go over what happened, how it could have happened and what to expect from a financial point of view.

Two factors were required for this saga to unfold. The first one was the creation of communities of investors jumping on the same trade. Self-grown day traders who have approached the stock market in the past year are accustomed to making extensive usage of social media for sharing idea or to follow some charismatic leaders, or to build communities. Reddit, a social platform, has quickly become the most favorite community, most notably the long standing subgroup WallStreetBets with over 4 million users where most retail investors shared trade ideas over past month. One of the most common target in the recent past has been the most shorted stocks. The idea is to buy the stock and make its price increasing to the point where short sellers are forced to cover the short position, squeezing the price up. The second factor needed was the sufficient capital that has been provided largely by the new stimulus checks paid as part of the bill approved in late December. Of course, there have been plenty of people who desperately needed that money to survive in the current situation. But some of the recipients clearly used that money to speculate, as confirmed also by several posts published on social networks.

Putting in a nutshell, the list of stocks with the highest short interest started to circulate in January. The most shorted stock was GameStop with a short position equal to approximatively 140% of its capital. The stock, which had already increased by about 600% from last year's low to the end of 2020, rose by a whopping 2400% to the intraday high in 2021. While GameStop became the most famous example of this huge short squeeze, several other stocks also shared a similar fate.

(continued)

Cust	12/31/20 - 01/29/21
Members (3629)	Return
BBG US Agg Eq Index PR	-0.34%
Best Performing	
KOSS CORP	1760.47%
GAMESTOP CORP-CLASS A	1625.05%
EXPRESS INC	559.34%
AMC ENTERTAINMENT HLDS-CL A	525.47%
TRANSENTERIX INC	373.60%
GRITSTONE ONCOLOGY INC	359.39%
POLAR POWER INC	309.63%
ZOMEDICA CORP	298.96%
ISORAY INC	277.78%
BIONANO GENOMICS INC	258.77%

Source: Bloomberg

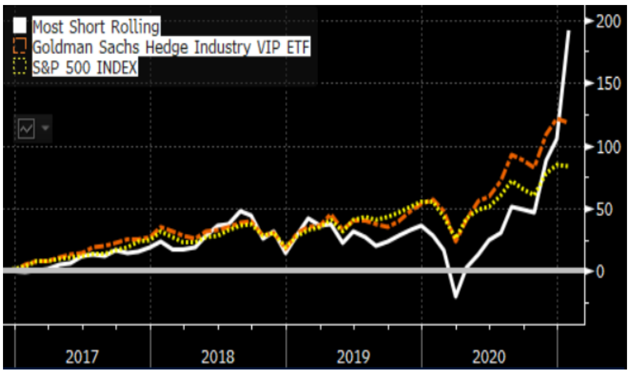
Source: Bloomberg

The graphs above show the 10 best performing stocks for January; when the main indices ended the month broadly unchanged, the Goldman Sachs Most Short Rolling index, an equally weighted basket of the 50 highest short interest names in the Russell 3000, which is up almost five-fold from March lows, reached an intraday maximum of +58% year-to-date.

Such movements are rather irrational and unsustainable in the medium and long term, and most of those increases will likely be reversed once this phenomenon is over or when the focus of retail investors switch to other names.

These short squeezes made several casualties. The first one, paradoxically, was the trading platform most used by retail traders, Robinhood, a victim of its own success. An online investment brokerage and trading app that has attracted thousands of these day traders thanks to a zero commission trading model, was forced to restrict its clients' ability to purchase some of the most shorted stocks. Apparently the move was not an obscure plot, but simply the consequence of market rules that applies to each broker. To put it simply, the market's central clearing hub requires brokers to post collaterals depending on the volume traded and the volatility of the instruments traded. As the majority of Robinhood clients was gorging the stock experiencing the highest volatility due to the short squeeze, the broker received a ten-fold increase in margin requirements, forcing it to restrict trading for those stocks, and raising more than $3.5 billion from its investors and drawing everything possible from credit lines with banks to support the surging demand from its traders. Even if the company should be able to meet the collateral requirements, the damage was done and the series of events unfolded reduced the trust and reputation of a fairly liked app and the company may have to deal with the fallout for quite some time.

But the most important and unexpected victim of these short squeezes was the hedge fund industry. As hedge funds were forced to close their shorts at hyperbolic valuations, they financed their shorts covering by selling their long positions. Shown below is the ETF Hedge Fund VIP (in orange), which should represent the long portfolio of the hedge funds, and the Goldman Sachs Most Short Rolling index (in white). Over the long term, the Hedge Fund VIP was outperforming the S&P 500 (in yellow), while the most shorted stocks that should have weaker fundamentals underperformed. The situation has recently reversed and in the past 10 days the intraday correlation between the two indices became negative, confirming that the short covering caused the disposal of long positions.

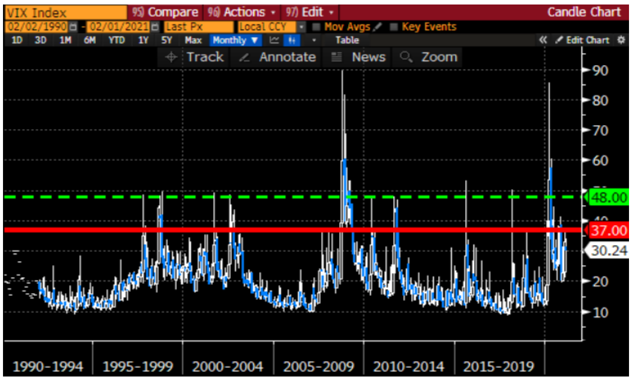


Source: Bloomberg

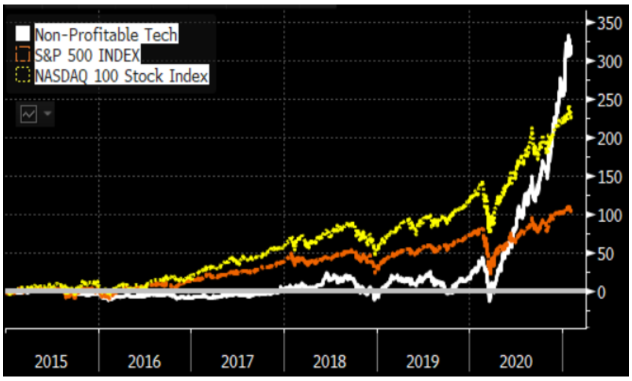
Source: Bloomberg

(continued)

What will be the magnitude and consequence of these short squeezes be and how long will they last? As of today, the consequence appears to be still manageable without any serious problems down the road. Surely, there will be some repercussions for the hedge funds (the one most known is the hedge fund titan, Melvin Capital which lost 53% in January) but no systemic risks seem currently in sight. It can also be expected that some of the retail investors will remain trapped in the correction that will eventually unfold. When some of the stocks that have gone parabolic start causing deep losses among the retail traders, there will be less willingness to participate in further speculation of this kind. But if this won't happen and the short squeezes continue to take place, then we might face a higher volatility and deeper retracement. In January, the VIX index reached an intraday high of 37. In the few occasions when this threshold was broken to the upside, the next stop has always been at least 48. The base case is that this should not happen, and at the time of writing the VIX has come back to about 30.



Source: Bloomberg



Source: Bloomberg

Regardless of what happens to the most shorted stocks, the recent developments may lead to a broader debate on the level and appropriateness of the current monetary and fiscal policies as well as their effects on the financial stability and asset valuations. Speaking of the latter, a final chart is presented: the Goldman Sachs index of Non-Profitable Tech is compared to the S&P 500 and the Nasdaq. While many highly profitable companies are included in the latter indices, the Non-Profitable index has not only closed the gap to the major indices recently, but also largely outperformed them.

Policymakers all agree that there are no bubbles, no incentives for risk taking and nothing to worry about. We all hope that they will be right and able to smoothly unwind the extraordinary measures of the past year, as Mr. Powell confidently reaffirmed during the last press conference after the Fed meeting.

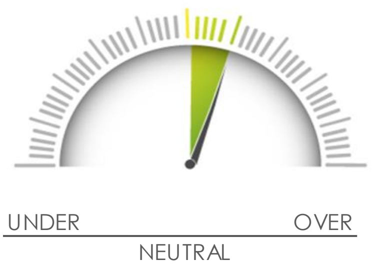
Asset Allocation View

	−	=	+
Equity			
Developed Markets			■
Emerging Markets			■
Fixed Income			
Developed Markets Sovereign	■		
Developed Markets Corporate	■		
Emerging Markets			■
Commodities			■
Currencies		*Commentary below*	

− UNDER = NEUTRAL + OVER

Equity

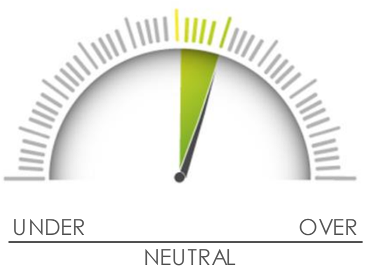
Developed Markets



We keep our stance on Developed Markets Equities as slightly positive. Last week we recommended to increase the equity exposure should a correction of about -5% occur. Last week's correction of about 3 to 4% on most indices was not considered enough to increase the recommendation by one notch. Further downside may be possible in the short term and, if offered, we advise to continue adding to the equity exposure as long term perspectives remain positive. We maintain a preference for European and Japanese equities and a relative underweight in the US.

US	−	**Europe**	=	**Japan**	+

Emerging Markets



We keep our slightly positive recommendation on Emerging Markets unchanged. The overbought condition that was in place in the first half of January has led to a moderate correction, but the retracement does not justify an upgrade on the overall recommendation. In terms of regions, we still prefer Asia compared to other Emerging Market regions, notwithstanding the YTD underperformance of the latter vs the former.

Asia ex-Japan	+	**EEMEA**	=	**LATAM**	=

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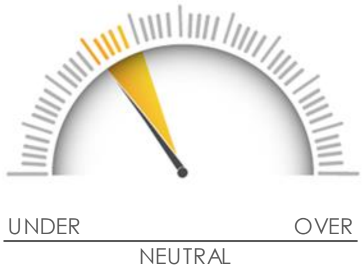
Fixed Income

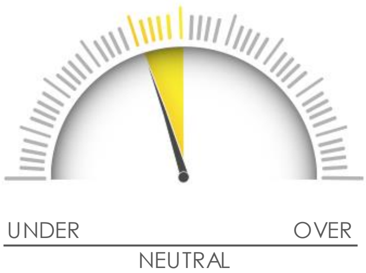
Developed Markets Sovereign



We lowered our recommendation for Developed Markets sovereign bonds to underweight. There is growing evidence from macroeconomic data (ex: EU CPI) that inflation will continue to rise in the coming months. Central banks are clearly not worried about this and the Chairman Powell has made it clear that the Fed expects any spike in inflation to be temporary with no need for monetary policy adjustments. This means that monetary policy will remain accommodative for the foreseeable future and the long-term rates may be free to move (we dedicated our first issue of 2021 to this topic). Within sovereign bonds, we have a strong preference for inflation-linked bonds.

EU Core	−	**EU Periphery**	−	**US Treasury**	−	**Japanese JGB**	−

Developed Markets Corporate



We kept our negative recommendation on Developed Markets corporates. There is no value left in most of the investment grade component, where extremely low yields to maturities and long duration make the risk return profile of those bond very unattractive. There are still some opportunities in the segment between investment grade and high yield, in particular in subordinated bonds.

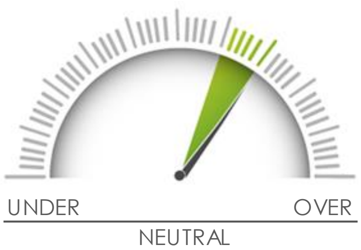
IG Europe	−	**IG US**	−	**HY Europe**	=	**HY US**	=

Emerging Markets

We kept our bullish recommendation on the asset class. EM bonds should benefit from the expectation of a vaccine driven strong global economic recovery. Moreover, the environment of USD18 trillion of negative yielding debt should bode well for EM bonds, especially considering the chase for higher yields. It is projected that EM bonds could benefit both from a spread compression and a recovery in the value of their currencies. Among local currency bonds we have a preference for those denominated in Chinese Renminbi. Only a worldwide spike in inflation and in long term rates may partially change this outlook, as historically rising rates in developed markets have been associated with weakening Emerging Markets currencies.

Local Currency	+	**Hard Currency IG**	+	**Hard Currency HY**	+

Commodities



We maintain our bullish view on the asset class. Precious metals could be sustained by the ample liquidity and could serve as a hedge against the debasement of most currencies after the massive monetary interventions of this year. The recent correction is viewed as a short term consolidation, as expectation for higher inflation later in 2021 should sustain the demand for precious metals. Energy and industrial metals should benefit not only from the expectation of a quick and prompt recovery as soon as the vaccines are distributed, but also because of the very low inventories.

Precious	+	**Energy**	+	**Industrial**	+

Currencies

We maintained our neutral view on the Euro after the recent appreciation. The modest retracement in the past days is mostly due to the recent turmoil in European politics (Italy, Netherland), and to the reduction in vaccine deliveries from Pfizer.
We lowered our stance on the US Dollar, mostly due to the higher then expected fiscal package announced by Biden last week, which is expected to be followed by another one later in 2021.
We kept the neutral view on the Japanese Yen as the country may attract foreign investments if the focus on value stocks, which are well represented in the main equity indices, continues in the near future.
On Emerging Markets currencies, we maintain our positive view considering that any episode of short term volatility will not change the long term positive perspectives for the asset class.

Euro	=	USD	−	Yen	=	Emerging	+