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2020: Year Of The 'New Retail' Investor

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Summary

- New retail investors like the Robinhood crowd have influenced the market in multiple ways since March and could continue to do so.
- The younger generation (first-time investors) can absorb more risk into a portfolio from a longer outlook, with many popular names in beaten down sectors.
- The market's valuations today could start to be cemented in, and a new trajectory higher could be aided from new retail investors.

2020 is coming to a close, wrapping up an extreme market cycle, from record highs to a record plunge to record highs again, as the market twisted from heavy optimism to panic selling to euphoric buying. Yet the COVID-19 associated recession has yet to fully abate, with millions of citizens domestically feeling monetary pressure and businesses struggling to stay afloat. Even so, the market's rally to new highs could very well be sustainable into 2020, with vaccine development potentially leading to more market rotation into beaten down sectors from the emergence of 'new retail' investors - the so-called 'Robinhooders.' While this isn't solely descriptive of users of the app, it's more a broader involvement of a younger generation tapping into equities and possibly fundamentally changing markets.

Source: StockCharts *(horizontal lines added at previous/current highs and low)*

As the markets rolled into the quickest fall in the modern era *[shown above with the SPDR S&P 500 ETF (SPY)]*, stocks in nearly every sector plunged to abnormally low valuations (some record, near-bankrupt valuations), opening the door for new money to snap up shares at 'discount' prices, while absorbing inherently more risk due to the uncertainty circulating the market during the springtime. Some of this new money came in the form of Robinhood investors, as well as other new retail investors entering in due to zero-commission or stock 'slices' trading.

Robinhood co-CEO Vlad Tenev pointed out that Robinhood users contributed to market stabilization during the March selloff, corroborated by the National Bureau of Economic Research, which "*concluded that investors on Robinhood 'did not panic or experience margin calls' during the market meltdown and 'collectively acted as a (small) market-stabilizing force.'*" Yet the institution also pointed out that decision-making from this group steered away from traditional picks, in some cases with money pouring into to beaten down travel/airlines and entertainment names.

Yet the younger generation, many of them first-time investors, can absorb more risk into a portfolio; while the group might not have the same nest egg or investable cash on hand as old retail, the relative low average age of investors on Robinhood (20s/30s) opens them up to far longer pictures in terms of recovery and growth. Therefore, there might not be the same emphasis on passive income generation through dividends and more of the rapid growth mindset, chasing high growth names and deep discounted 'bargain' buys in companies like cruises which could require multiple years to fully recover.

Some of the 'most popular' on Robinhood are duly earned - Apple (AAPL) holds the top spot, Tesla (TSLA) the second; Microsoft (MSFT), Amazon (AMZN), Disney (DIS) and Pfizer (PFE) also make the top ten.

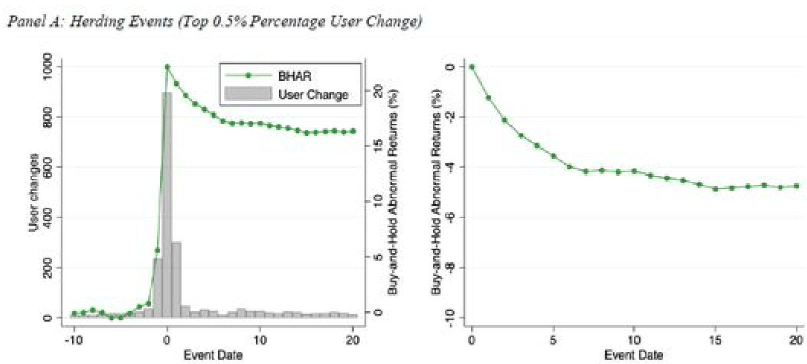
But there's names that are surprisingly popular - American Airlines (AAL) in sixth, Delta (DAL), Aurora Cannabis (ACB), Carnival (CCL), Plug Power (PLUG) and GoPro (GPRO) hold spots eleven to fifteen. Also making the top hundred most popular are Norwegian (NCLH), Boeing (BA), Hexo (HEXO), Canopy Growth (CGC), Nikola (NKLA), Royal Caribbean (RCL), OrganiGram (OGI), AMC (AMC), Marathon Oil (MRO), Exxon Mobil (XOM), JetBlue (JBLU), Genius Brands (GNUS); all these have more users holding them than SPY. Arguably, there could be many 'better' choices to invest in, yet the favorable long-term timeline plays into the higher risk in some of these names.

As we head into 2021, not much seems to be changing besides the calendar year. Macroeconomic conditions lightening alongside positive vaccine development is likely, and fundamental issues within travel (cruises/airlines) and other heavily impacted segments like oil and energy aren't likely to clear, even with a vaccine, although animal spirits and optimism from that could relate to share price appreciation from old and new retail alike. Yet there's still other trends and new developments from the massive entry of new retail investors that could continue to change trading patterns as well as cement sustainability of current market valuations and even push the market higher.

One development is that seemingly negative news is instead being bought in a positive light - underwhelming jobs reports, showing shrinking monthly gains, isn't being sold; it's being bought under the pretense that more fiscal stimulus will be necessary. More infusions of cash and ultra low interest rates could be enough fuel to push returns significantly higher, even as recession-like conditions exist. Job gains aren't likely to occur as rapidly as they evaporated due to the pandemic, as the long-term effects on small businesses, which are very important for job creation and employment, such as impacted operating capacity and revenues, still remain.

Similar company-specific negative news, such as bankruptcy, also has attracted flocks of new retail investors. While outright fears of bankruptcy across the board have abated, company-specific cases, like small retail, could still have high chances of bankruptcy. Such was the case with Hertz (OTCPK:HTZGQ) just after the company first announced bankruptcy - users HOLDING SHARES ON ROBINHOOD more than doubled that week as shares rallied from below $1 to over $5.50 intraday. More company-specific news around debtor-in-possession financing sent shares up 140% on over 1 billion in volume.

Yet such frenzies by new retail are apt for exploitation from institutional names to targeted short selling groups. With up to half of Robinhood's over 13 million users first-time investors, there's a tendency to be attracted to 'attention-grabbing' stocks ranking high in the news, causing herding and rapid rallies, typically in small-cap stocks, but also sometimes into mid-cap names like Appian (APPN). Cases of herding typically lead to underperformance following frenzied buying, in such predictable manners that short sellers can profit easily.



Source: Bloomberg Quint

An analysis of 'herding' found that "[w]hen Robinhood users pile into a stock in large numbers, the average excess return on the day surges to 14%. But this is followed by a reversal of nearly 5% over the subsequent month,...[spurred by] the combination of naïve investors and the simplification of information." Short selling cases of herding from Robinhood demand led to average returns of 3.5% in five days, or 7% in excessive scenarios. And this had been the case with Hertz.

Source: ORTEX Analytics

When shares popped on the DIP news on the 1 billion volume, shares short likely increased by almost 50%, from an estimated 34 million to 53 million following the news (as cost to borrow quadrupled); many of those newly opened positions were closed quickly after, for returns of 50% to 70%.

Such a dynamic could very well continue to be in play throughout 2021, given some of the names finding their way on the most popular list - it's heavy with EV, cannabis, and travel stocks, with some residual popularity in energy. Vaccine news could accelerate buying in some of the travel names, potentially causing mini-herding events and quick rallies, while outright popularity in EV over the past quarter has led to rapid value accretion even with little fundamental changes. Long-time favorite Tesla also has continued to climb, and recent inclusion into the S&P could see more translation of Tesla's gains impacting market performance due to animal spirits.

New retail investors are here to stay, and have already shown the level of influence that they can exert over the market and individual companies. Large inflows into the hardest hit sectors and continued popularity up until now point to the higher levels of risk that some of these investors are willing to take, given the longer-term timeframe some could have, or the hunt for a 'discount' apt for a 'herd'. These new retail investors are also influencing crowd behavior within the herd, buying massive (billion share and/or billion dollar volume) amounts in micro/small-caps and even bankrupt names, causing triple digit returns in extremely short time frames, and opening the doors for targeted shorts and institutions to capitalize on selling pressure and make significant profits on the ride back down. Heavy popularity in beaten sectors could bode well in market rotation, with most travel, oil and financials all lagging market returns since the plunge, and positive developments within stimulus or vaccines could lead to positive returns in those names. Combining that with stellar, top tech and the flying work-from-home names, the market's valuations today could start to be cemented in, and a new trajectory higher could be aided from new retail investors.

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