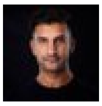
Twitter Thread by Sahil Bloom



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Short Squeeze 101

If you follow financial markets (or if you watch Billions), you've heard the phrase "short squeeze" used quite frequently.

But what is a "short squeeze" and how does it work?

Here's Short Squeeze 101!

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1/ First, the basics.

The "short" in "short squeeze" refers to the concept of short selling.

The basics are covered in my thread below.

https://t.co/xecJYNCxMs

TL;DR - short selling is a way of betting against a stock - i.e. betting that its price will decline.

> 1/ Short Selling 101
>
> With the markets continuing to rally, there has been more talk of \u201cshorting\u201d or \u201cshort selling\u201d stocks.
>
> But what does that mean and how does it work?
>
> Here\u2019s a quick educational primer: Short Selling 101 pic.twitter.com/JTrJmuY7fI
>
> — Sahil Bloom (@SahilBloom) July 6, 2020

2/ "Short interest" is a measure of how heavily an asset is shorted by the market.

It is the total number of shares that have been sold short (borrowed and sold), but have not yet been covered (bought and returned).

It is usually measured as a % of the # of shares outstanding.

3/ A "short squeeze" occurs when a heavily-shorted asset experiences a rapid upward price movement.

When this happens, short sellers may be forced to close their short positions (i.e. buy the stock and return it to the broker), further accelerating the upward price movement.

4/ Let's look at a simple example to show this in action.

We will use Tesla, one of the most heavily-shorted stocks in the world.

Imagine the stock price is $1,000 per share. This seems crazy. Ricky Rational decides to short the stock at this level.

5/ Ricky borrows 1 share from his broker, agreeing to return the borrowed share in the future.

He sells it short at $1,000.

If the price declines, great. He is now able to buy a share at $800.

Ricky returns that share to his broker and closes his short with a $200 profit!

6/ If the price rises, not so great.

His broker gets nervous about his ability to pay and forces him to replace the borrowed share. He buys a share at $1,200 and closes the short in a loss.

In both cases, the "closing" of the short requires a purchase of shares of the stock.

7/ Therein lies the makings of the short squeeze!

If Tesla stock rises rapidly (which it does far too often), Ricky and many others may all be forced to close their shorts at once.

This creates a surge of buying (to return the borrowed shares) and drives the price up further.

8/ Short sellers are literally squeezed out of the market.

You can track short interest in specific stocks to determine when one may be occurring.

So next time you see a chart that shows a sharp rise, followed by another, even sharper rise, you may be seeing a short squeeze.

9/ That was Short Squeeze 101! I hope it was helpful.

For more educational threads on money, finance, and economics, check out my meta-thread below and follow along for more. https://t.co/Jyqunbg8uM

> 1/ An Allegory of Finance
>
> I have been posting a lot of educational (and humorous!) threads on finance, money, and economics.
>
> My mission is simple: to demystify these concepts and make them accessible to everyone.
>
> All of the threads can be found below. Enjoy and please share!
>
> — Sahil Bloom (@SahilBloom) July 18, 2020