OWNING DOWNSIDE VOL/HEDGES WINS BIG – LEGENDARY FACTOR TRADE SHOWS DIVERGENCES DEBUNKING THE MYTH OF TECH AND RATES- EARNINGS VOL TRADES

VOLATILITY SUMMARY

Rates, rates, rates, every day, rates. It's a bear steeping-tastrophe. It goes without saying, I suppose, that we wouldn't be in a mess where we have to look at rates spike nearly every day, watch equity markets *tank* on the news of people being hired and spike when the economy looks worse if it wasn't for Jay being asleep at the printer again. You can't turn on Bloomberg/CNBC and even attempt the "Fed" drinking game, you wouldn't get an hour into any day.

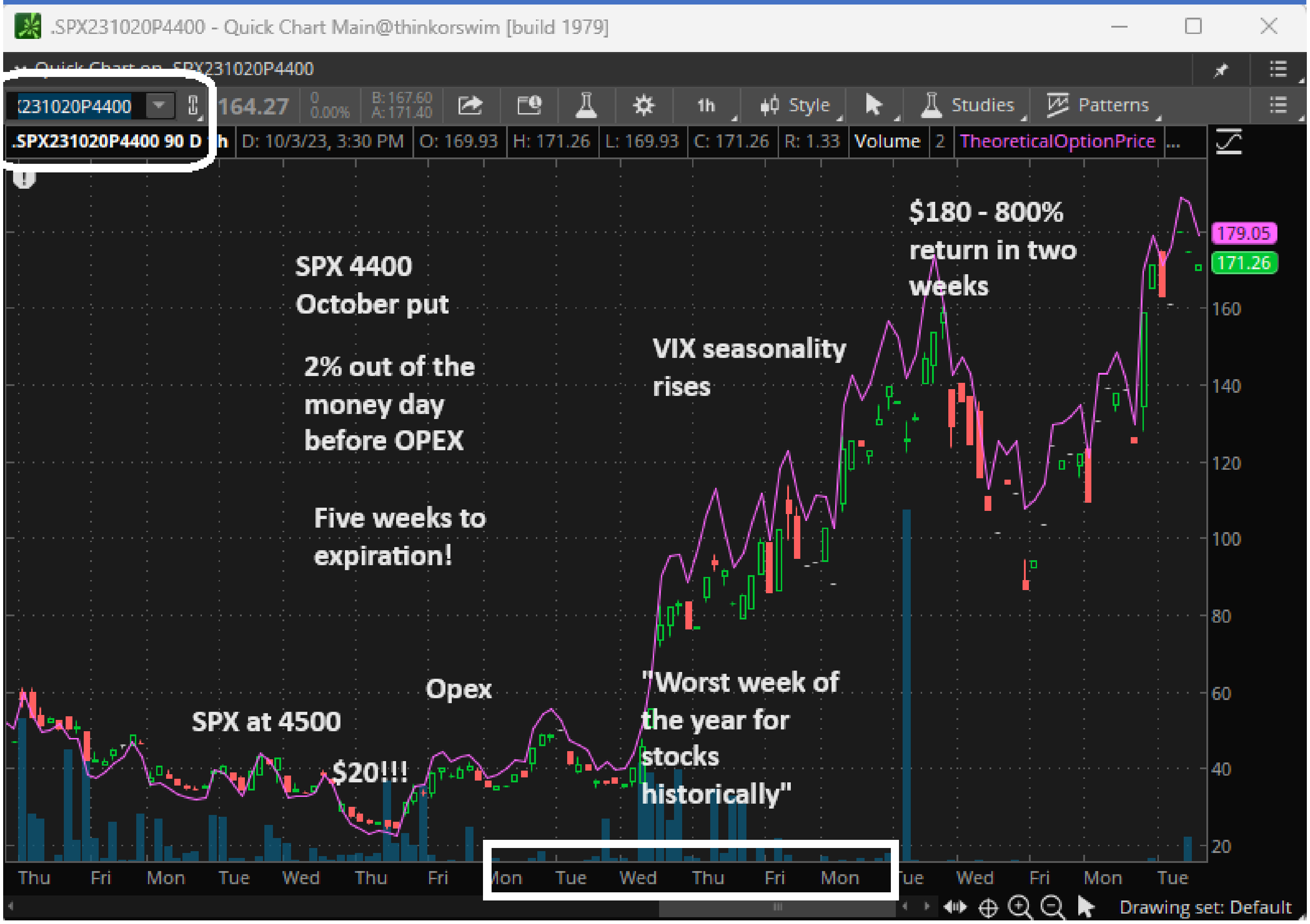
(JOLTS is the new CPI apparently, 65-70 SPX point intraday ranges last two releases..)

What amazes me lately, is that even in what appears to be a trendless equities market is really embedded with smaller but pervasive and repeating trends. And the trends are seasonal as well, which begs the question, if everyone is a trend follower (seems that way) and everyone knows the seasonality, why do both keep happening?

Well, I should make a top ten list of market dogma that is pure BS. A lot of the stuff you either hear on tv or learn in finance classes that is just a bunch of made up malarky. Clearly, I've pounded on the 'forward-looking' twaddle for a while, but let's add to the list 'random walk' and 'efficient markets'.

The answer probably lies in the fact that so much money is invested/traded now when trends are established and vol is lower in CTA and systemic strats. It's simply self-reinforcing.

And since markets keep trending, and do it seasonally to boot, combine those observations with volatility that keeps getting sold for income in new tenors and higher volume (0-1DTE for example) and in new forms (more vol selling ETFs launching like QQQY) and you get things like this, that should have been totally predictable:

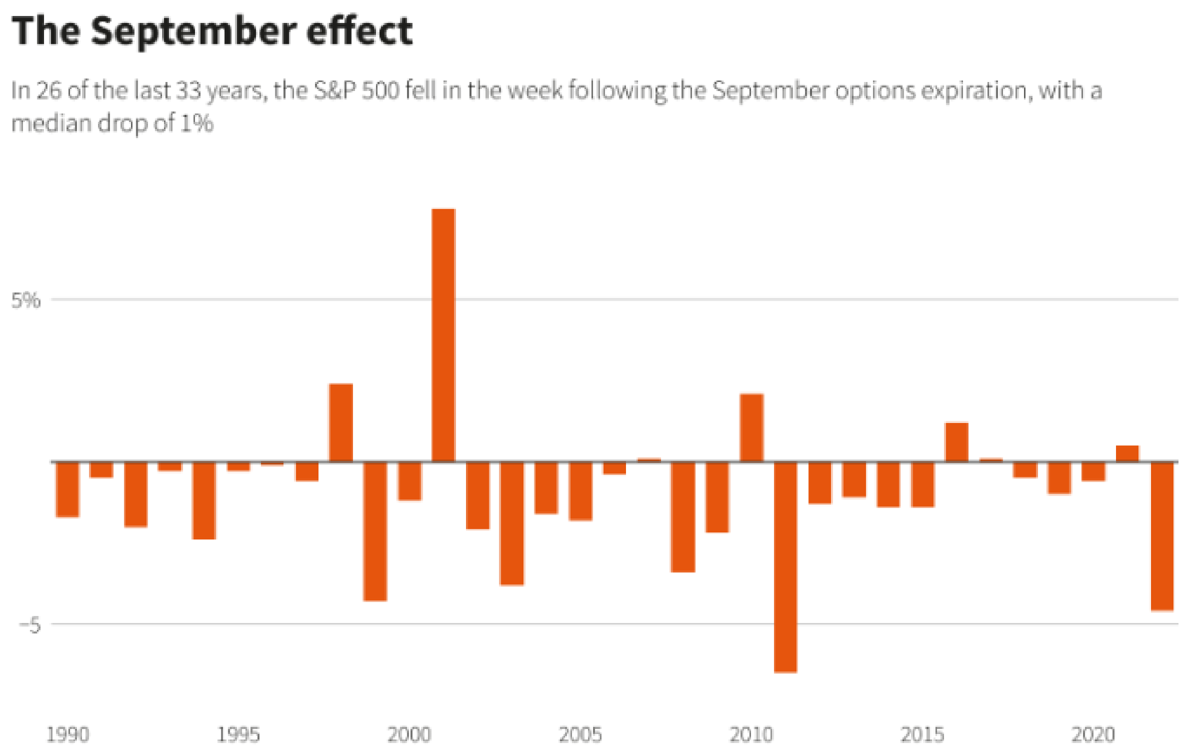


Yet, you and I both know, there was plenty of this stuff going around:

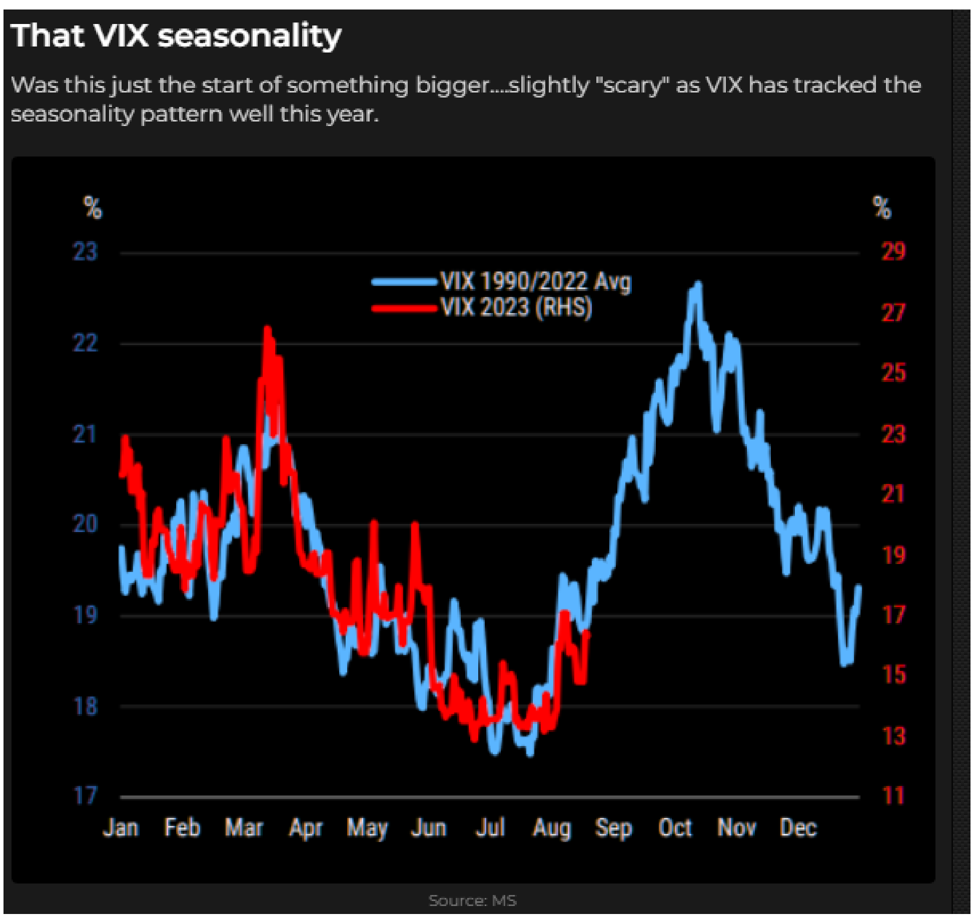
From Sep 21st note:

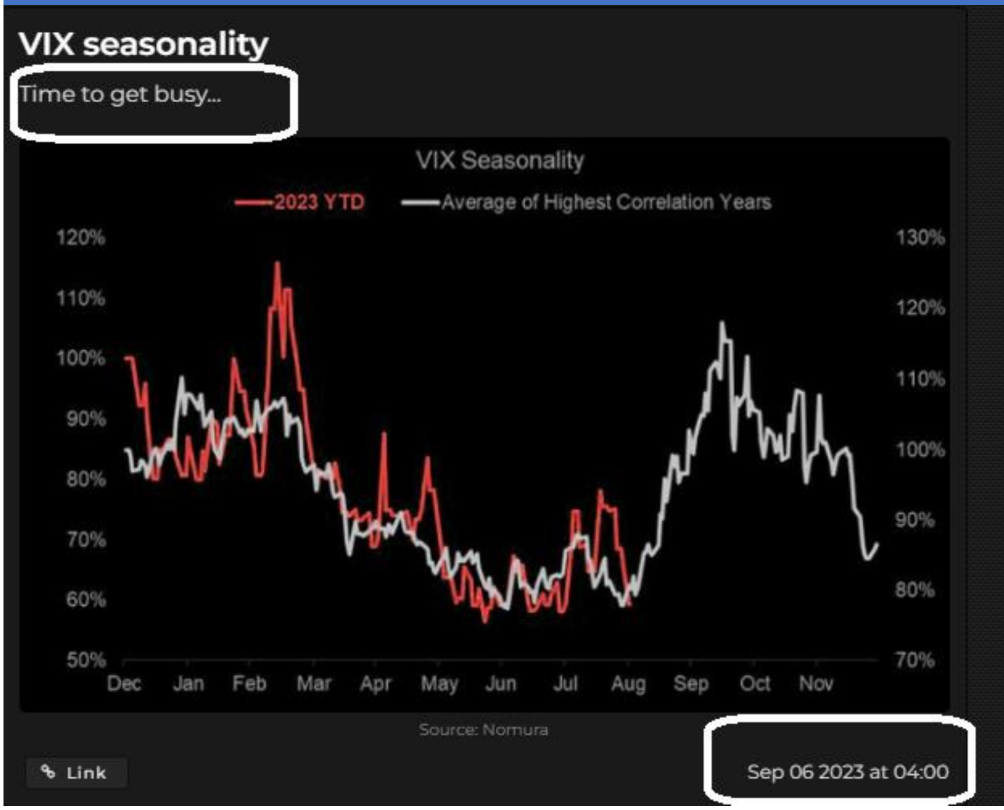
And, on top of this, weren't we besieged with warnings about how this was the worst week of the year for stocks?

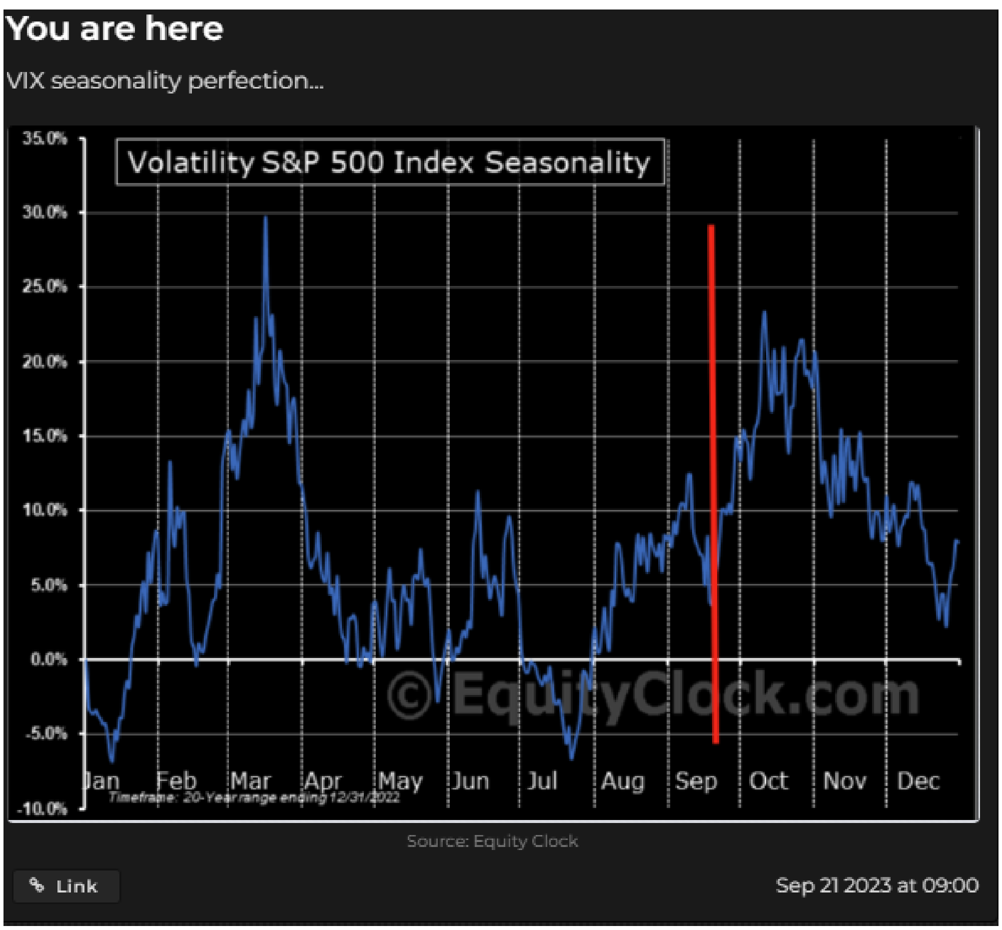
Source: https://www.reuters.com/markets/us/fed-meeting-comes-during-historically-tough-week-us-stocks-2023-09-12/


The September effect
In 26 of the last 33 years, the S&P 500 fell in the week following the September options expiration, with a median drop of 1%
5%
−5
1990
1995
2000
2005
2010
2015
2020

And this:


That VIX seasonality
Was this just the start of something bigger....slightly "scary" as VIX has tracked the seasonality pattern well this year.
%
%
VIX 1990/2022 Avg
VIX 2023 (RHS)
23
22
21
20
19
18
17
29
27
25
23
21
19
17
15
13
11
Jan
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Dec
Source: MS


VIX seasonality
Time to get busy...
VIX Seasonality
2023 YTD
Average of Highest Correlation Years
120%
110%
100%
90%
80%
70%
60%
50%
130%
120%
110%
100%
90%
80%
70%
Dec Jan Feb Mar Apr May Jun Jul Aug Sep Oct Nov
Source: Nomura
Link
Sep 06 2023 at 04:00


You are here
VIX seasonality perfection...
Volatility S&P 500 Index Seasonality
35.0%
30.0%
25.0%
20.0%
15.0%
10.0%
5.0%
0.0%
-5.0%
-10.0%
Jan Feb Mar Apr May Jun Jul Aug Sep Oct Nov Dec
Timeframe: 20-Year range ending 12/31/2022
© EquityClock.com
Source: Equity Clock
Link
Sep 21 2023 at 09:00

All you had to do was buy naked long vol; I'm going to write this here over and over again in the hopes that I can get it through my head that vol remains cheap relative to realized vol and especially to what I call trendvol. Directional vol can be even cheaper than it appears due to the potential for convexity magnification, similar to how a leveraged ETF keeps growing faster than its implied leverage when it feeds on itself repeatedly.

So, can we apply this instead of sounding like the Herald of Hindsight? Well, if trends inside of ranges are the thing now, let's call them 'trangy' seasonal markets, let's look at IWM, the Russell 2000 ETF for some clues to where cheap vol might be hiding out:

Clearly, boat missed on buying puts on IWM or owning the TZA 3x bear ETF staring in August (By the way, IWM is down 13% and TZA is up 53%, see what I mean....) but earnings season clearly has been quite good for IWM. Let's look at what rates did last year for some context as well:

Interestingly, a rapid rise in the 10-year rate petered out in mid-October, the day ***CPI 'relieved' folks by rising month on month .4% and year over year 8.2%, both worse than forecasts!*** It almost makes you chuckle, but the real story, was that the next day, on the 14th of October, JPM reported better than expected and earnings season did what earnings season seems to do most of the time, the markets grind higher on the better than expected game.

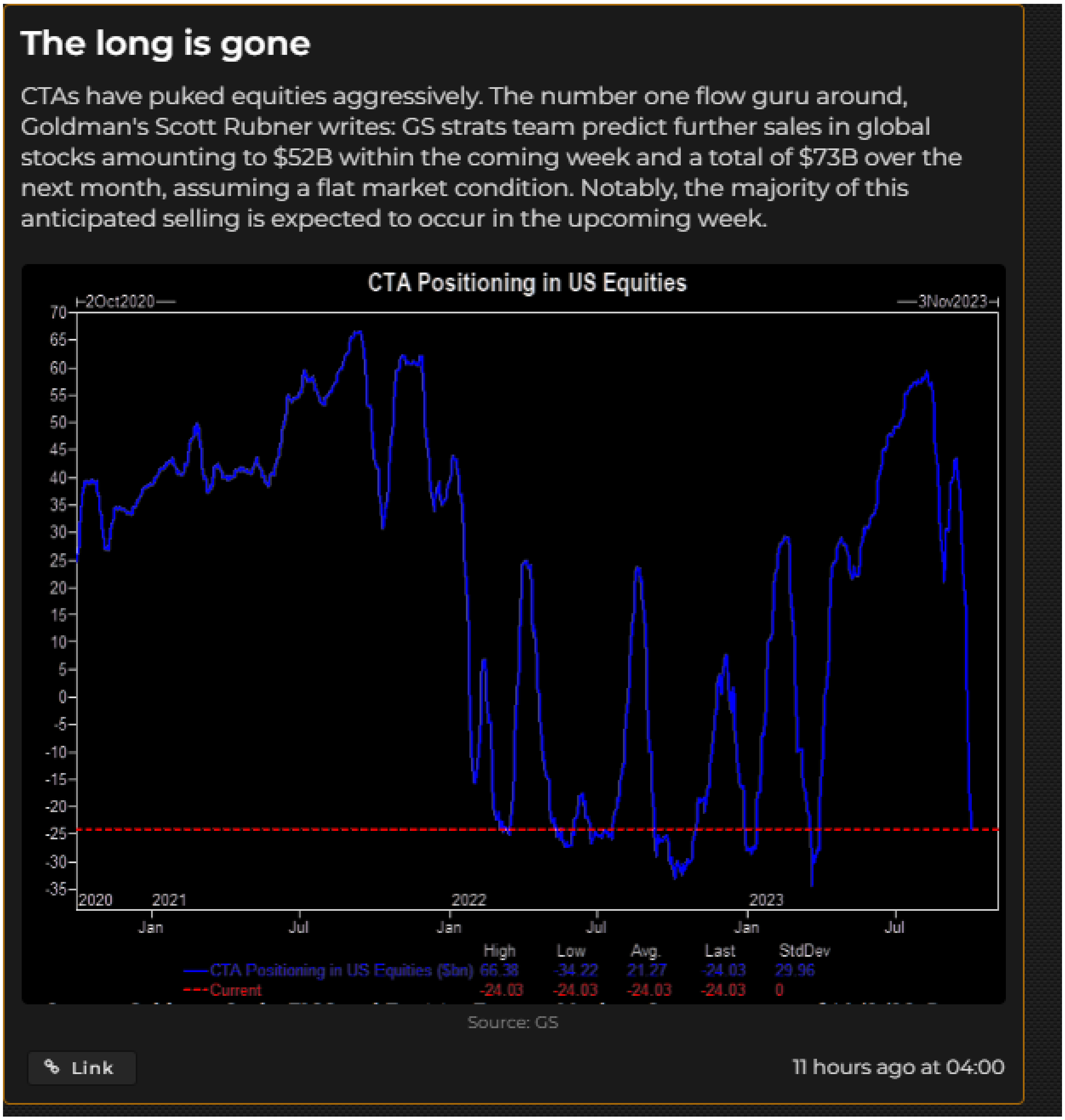
And to add a little fuel to this idea, that small caps might come out of the sewer, is this compelling chart:

So, if you were a genius hedge fund manager and you went long the Nasdaq 100 and short the Russell 2000, you are up over 100% year to date and will probably have to turn away new investors for winning the Crystal Ball Investing Award for 2024. (I remember as a kid, there was movie where this youngster looked at the newspaper and saw the future winning horses highlighted https://www.imdb.com/title/tt0082849/)

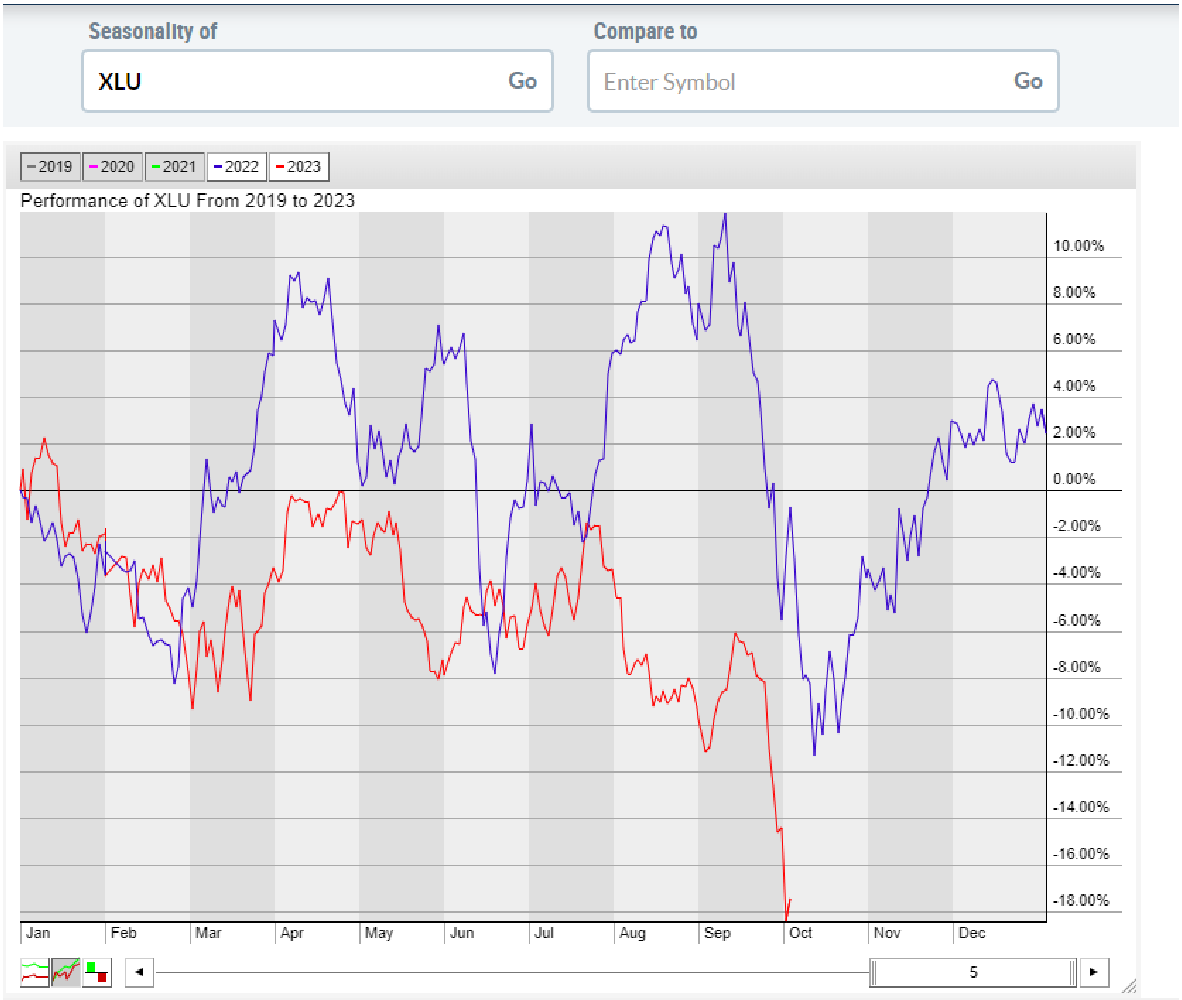
Imagine thinking, 'Oh, higher rates for longer plus value stocks must be a sign to go long QQQ/short IWM'. Anyway, this trade is ripe for one of those huge factor unwind days, where the Bloomberg/Nomura/McElligott article says it was an 8 standard deviation factor day or whatever.

My point is that the universe of stocks not giga tech related is due for a catchup of sorts, potentially, and what better time than October opex and earnings season for that to begin, while the news/sentiment is pretty darn sour.

I'm thinking that we might be in for a bit of a pre-earnings purgatory here, seeing that so many stocks are near 52-week lows, a lot of hedge fund folks have sold and are leaning short, and CTAs are leaning short now:



Even utilities have followed last year's pattern of crashing around now:



A lot has happened price-wise since the last earnings season ended, mostly bad, and it might be time for sentiment to improve a little.

Volatility Trades:

NFLX Oct 13th call condor spread

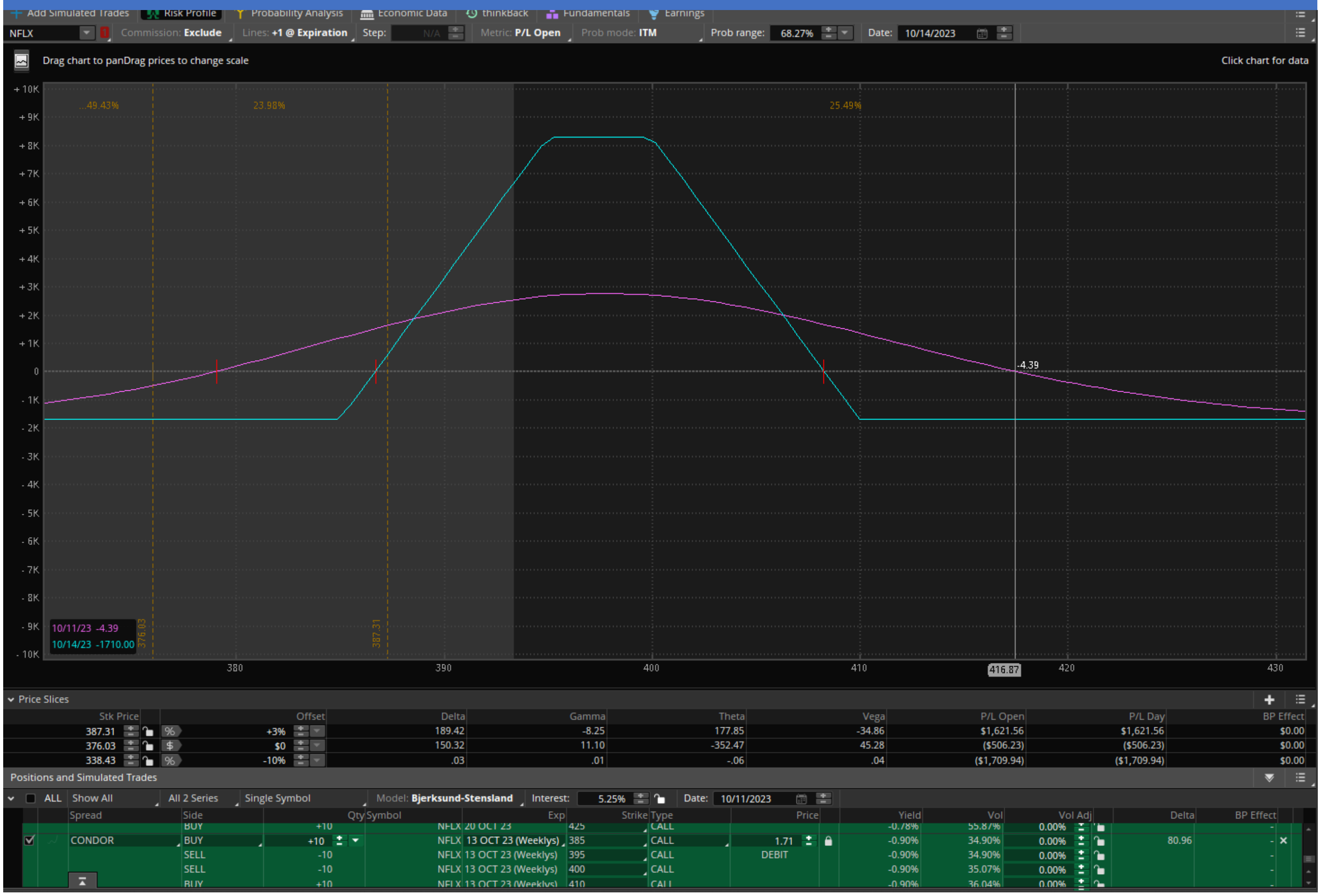
Buy $385 call

Sell $395 call

Sell $400 call

Buy $410 call

Net debit: $1.70-1.75



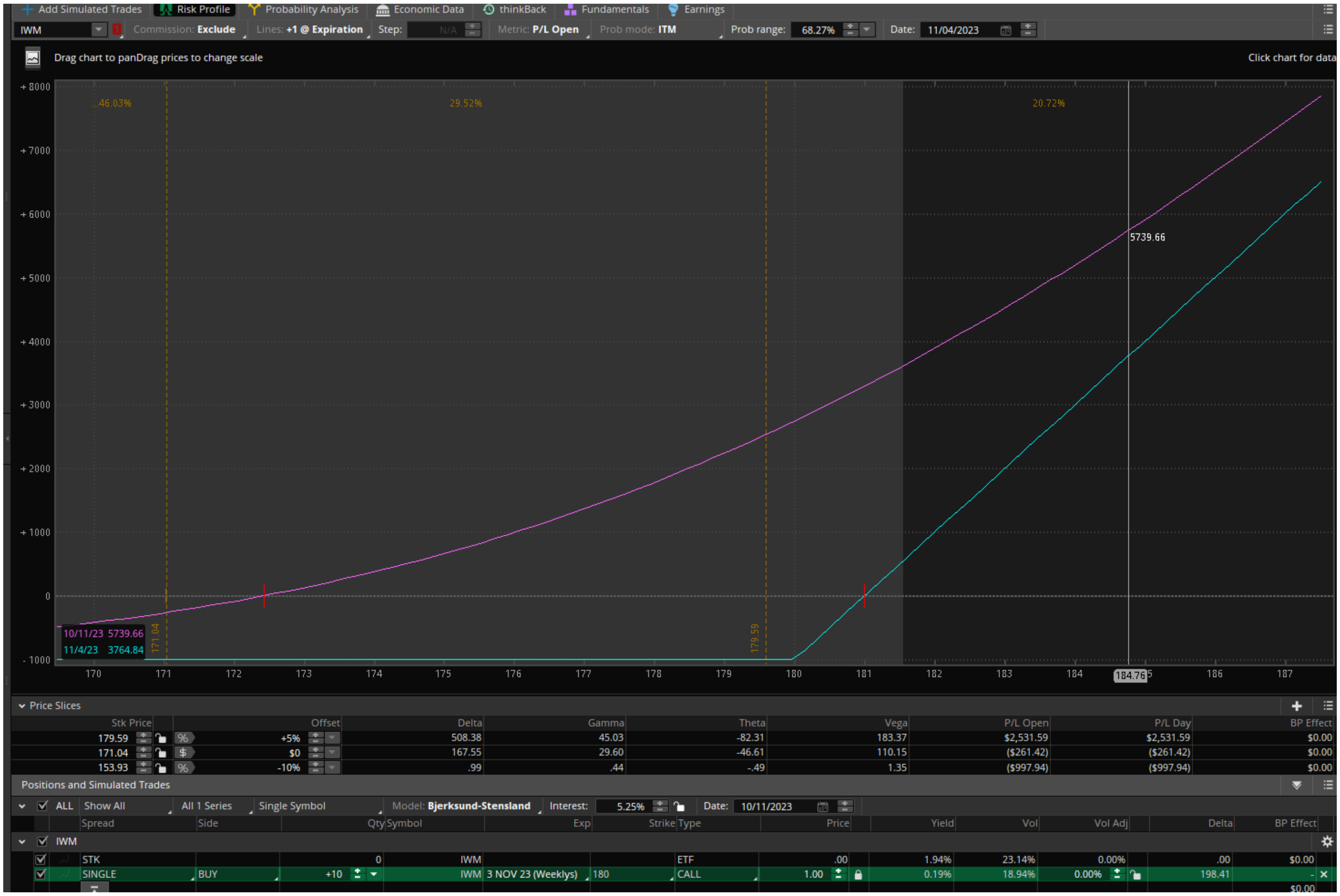
Earnings are on the 18th, and the chart looks like it’s rounding out a bottom:

The chart shows $400 as a logical pivot in the past, and it's $100 down since before it last reported. Also, as you can see in July, and in the chart below it tends to float into earnings in October, not to mention that they are about to announce a price hike, which usually is a spike day for the stock. The news of that this week was squelched by a horrible market day.

Stock Price Performance - Last 12 Quarterly Earnings										
	Before Earnings (Not Including Day of Earnings)					Day of Earnings				
Date	2 Weeks	1 Week	3 Days	2 Days	1 Day	Earnings Move	Opening Gap	Open-to-High	Open-to-Low	Drift Open-to-Close
19-Jul-2023 AMC	+7.1%	+7.6%	+8.1%	+6.1%	+0.6%	-8.4%	-6.5%	+0.4%	-3.3%	-2.1%
18-Apr-2023 AMC	-3.8%	-1.3%	-3.6%	-1.5%	+0.3%	-3.2%	-3.1%	+0.7%	-2.3%	-0.1%
19-Jan-2023 AMC	+2.0%	-4.4%	-5.1%	-3.2%	-3.2%	+8.5%	+6.5%	+2.3%	-1.1%	+1.9%
18-Oct-2022 AMC	+0.1%	+12.4%	+3.6%	+4.7%	-1.7%	+13.1%	+10.1%	+5.4%	-0.9%	+2.7%
19-Jul-2022 AMC	+8.5%	+15.6%	+15.4%	+6.6%	+5.6%	+7.4%	+3.3%	+4.2%	-3.9%	+3.9%
19-Apr-2022 AMC	-8.3%	+1.3%	-0.5%	+2.2%	+3.2%	-35.1%	-29.7%	+1.5%	-13.3%	-7.7%
20-Jan-2022 AMC	-8.1%	-2.1%	-3.3%	-0.5%	-1.5%	-21.8%	-21.3%	+2.3%	-5.0%	-0.6%
19-Oct-2021 AMC	+0.7%	+2.3%	+0.8%	+1.7%	+0.2%	-2.2%	-2.2%	+2.0%	-1.3%	0.0%
20-Jul-2021 AMC	-2.0%	-1.8%	-2.2%	+0.1%	-0.2%	-3.3%	-0.9%	+0.9%	-3.9%	-2.4%
20-Apr-2021 AMC	+0.9%	-0.8%	+0.1%	+0.6%	-0.9%	-7.4%	-7.7%	+1.6%	-0.8%	+0.3%
19-Jan-2021 AMC	-3.7%	+1.5%	-1.2%	+0.2%	+0.8%	+16.9%	+12.5%	+5.1%	-1.3%	+3.9%
20-Oct-2020 AMC	+3.9%	-5.2%	-3.1%	-1.0%	-1.0%	-6.9%	-4.6%	+1.1%	-2.6%	-2.4%

IWM November 3rd $180 call

Net Debit: $1



I know you never thought you'd see this in my note. Reminds me of Rocky III, "If you can change then I can change, we all can change.." or something. Anyway, why Nov 3rd? Well, Fed vol, non-farm payrolls vol, JOLTs vol all in this window. Target, $2.50.

I should have another short note Saturday with a few more ideas post-NFP.

END OF QUARTER PANICKY FIXED INCOME TRADING BECOMES CONCRETE SHOES FOR EQUITIES – WILL REALIZED VOL REMAIN HIGHER? – TRADES FOR EARNINGS/CPI

VOLATILITY SUMMARY

July 14th note:

"I've said this before but allow me to repeat myself. Equity markets (and bond markets for that matter) are not forward-looking. They are more like teenage parties; they don't end until the cops show up or get kicked in the nuts."

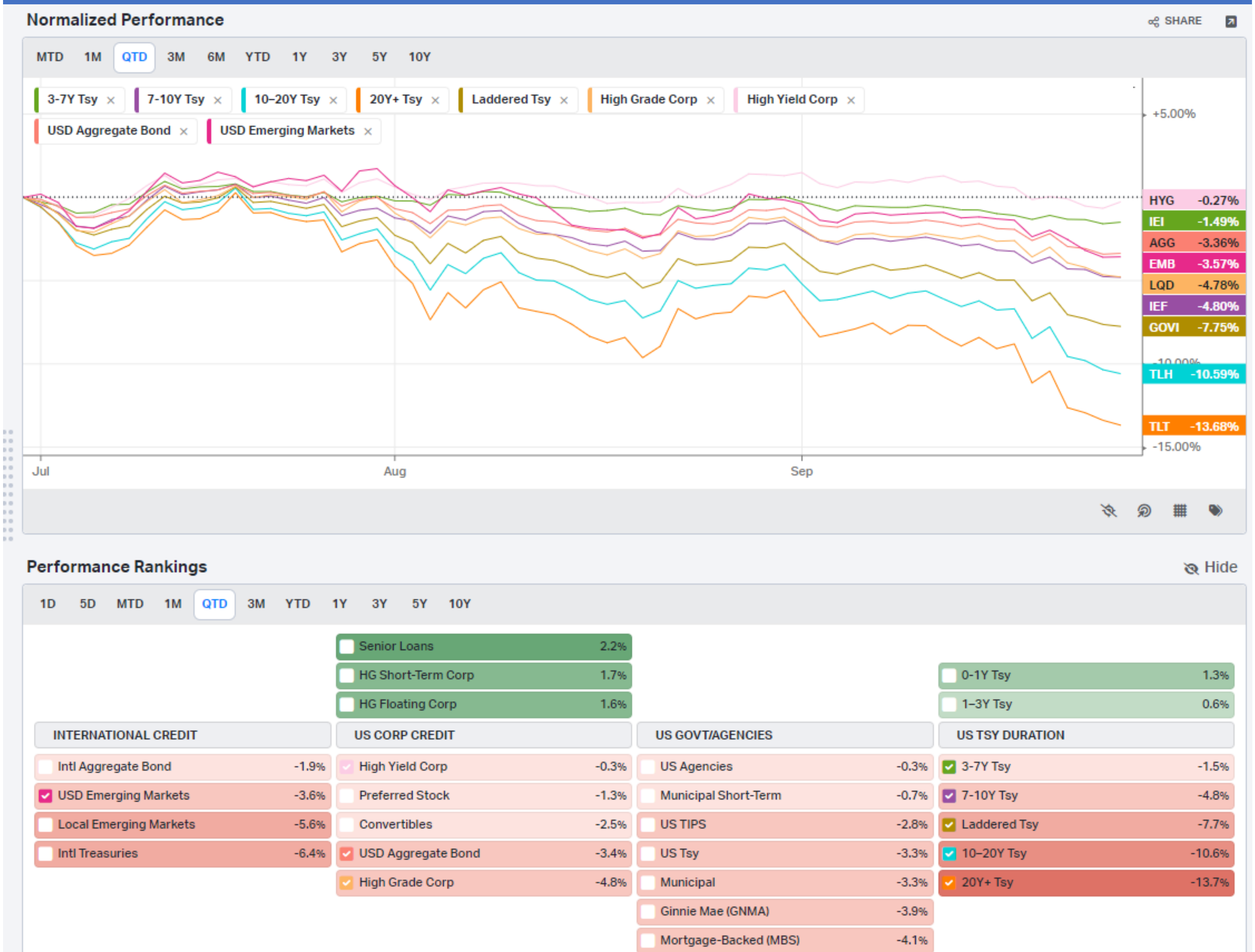
Well, how's it going, fixed income managers? The 'smart' ones in the room. The conservative, prudent stewards of capital. The ones that do their extra homework and have advanced degrees from the Church of Finance (CFAs).

They wouldn't get caught in, say, rushing to buy things in the hopes that they would go up into year end, would they? Because it's the end of the Fed hiking cycle? Because inflation will come down? Because rates won't stay higher for longer? I think they forgot who flies the friendly skies of global fixed income airlines, oh yes….he's back to bring this bird in:

While you are contemplating if the entire rates complex going berserk (purely coincidental to the end of the quarter, right?) will finally cause more havoc in the banking system, or shadow banking system, or whatever real estate/private equity/leveraged loan/ system…..How did 2018 go you ask? When 'autopilot Jay' was tightening into year-end?

A lot to chew on there.

Well, here is how the 'smart guys in the room' did this quarter, in an array of fixed income areas:



Absolute carnage; the end of quarter statements are going to be quite a Picasso, attempting to paint a rosier picture with some tax advantaged maneuvering and window dressing. Comically, the riskiest bonds (HYG/JNK junk ETFs) did the best this quarter into a worsening economy/quantitative tightening, how funny is that?

I mean, how could these managers have known things like:

A. Jay Powell repeating one thousand times over that rates would be higher for longer, or
B. That the dot plot was going to show a higher curve for next year, or
C. That there was going to be huge fresh new supply of treasuries to refill the TGA and to pay off the additional budget deficit interest, or
D. That these higher rates/QT would negatively affect corporate bonds or …….

That's just a start, right? For these forward-looking 'smarter' markets. (Insert frustrated eye-roll emoji)

In the meantime, a lot of non giga-tech herd stocks look similar to Boeing's chart, which is quite the thing, going down every day by almost the same amount with amazing symmetry?

So, it seems to me that realized vol is going to be here for a while as the markets wonder if the summer of looking-forward to a future of AI induced profit bliss might have been just a bit of a drunken market summer dream. And back to reality with all the concerns the summer tried to look through, a slowing economy, tightening consumers and banks, etc.

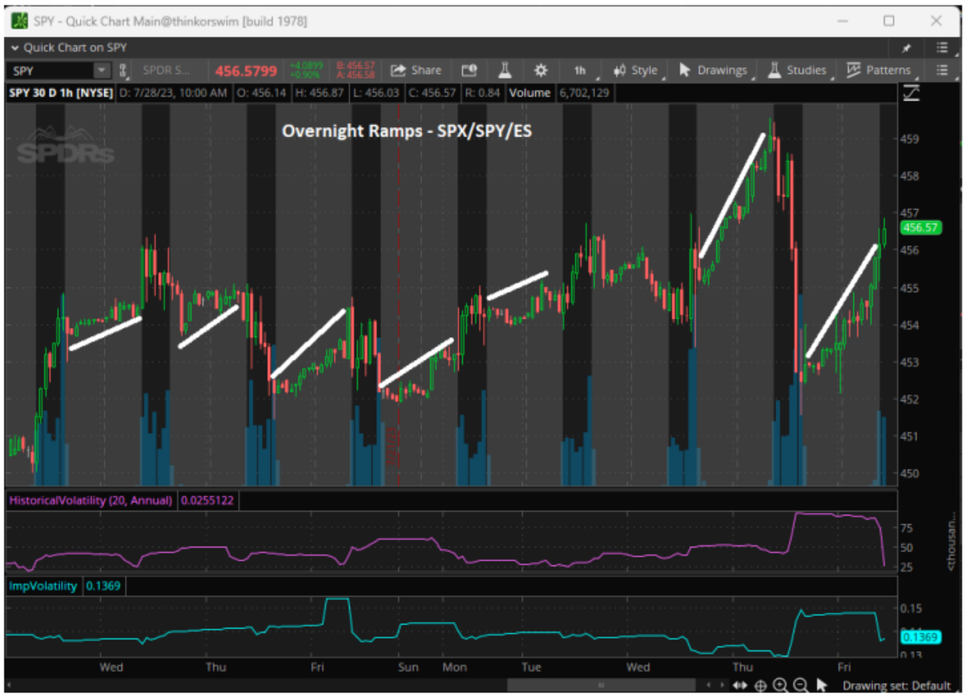
Let's be realistic, if the areas of the market that are supposed to be relatively quiet, like highly liquid corporate bond ETFs (LQD) are acting like this, how quickly are we going back to July-like overnight tractor-beam S&P futures daily ramps of +10? Remember July earnings season, it was the last one we had, seems so long ago already:

VOLATILITY ANALYTICS NEWSLETTER – JULY 28TH

OVERNIGHT RAMPING APPROACHING COMICAL – VOL MAY INCREASE POST AAPL/AMZN AS CORRELATIONS RISE – TRADES FOR NFP/CPI/POST TECH EARNINGS

VOLATILITY SUMMARY

I'm trying to remember when I last saw this, probably October into November of 2021, when every night it seemed the futures just seemed to be caught in a tractor beam higher, down wasn't an option, and it's happening again:



So, the first day of the month is almost here, it's almost always bullish, first day or two of the month, and part of the reason this time may be perhaps related to the fixed income space in a different way. Yes, the end of quarter managers' duck duck goose/musical chairs games will be over, folks will be positioning in some of those beaten down spaces for the fourth quarter, but also, a gigantic amount of fixed income ETFs go ex-distribution early next week:

VettaFi ETF Database Channels Tools Research Webcasts Themes Multimedia

Symbol	ETF Name	Total Assets ($MM)	YTD	Avg Volume	Previous Closing Price	1-Day Change	Overall Rating
BND	Vanguard Total Bond Market ETF	$94,767.10	-0.76%	5,847,134	$69.88	-0.10%	
AGG	iShares Core U.S. Aggregate Bond ETF	$91,140.70	-0.89%	7,708,700	$94.18	-0.13%	
BNDX	Vanguard Total International Bond ETF	$51,014.40	2.26%	2,140,651	$47.94	-0.06%	
VCIT	Vanguard Intermediate-Term Corporate Bond ETF	$39,107.20	0.74%	4,912,878	$76.19	-0.25%	
TLT	iShares 20+ Year Treasury Bond ETF	$38,224.00	-8.83%	27,846,788	$88.87	-0.35%	
VCSH	Vanguard Short-Term Corporate Bond ETF	$36,380.50	1.92%	3,824,123	$75.13	-0.07%	
MUB	iShares National Muni Bond ETF	$34,223.00	-0.58%	2,904,123	$103.09	-0.11%	
BSV	Vanguard Short-Term Bond ETF	$33,040.60	1.27%	2,888,511	$75.09	-0.04%	
BIL	SPDR Bloomberg 1-3 Month T-Bill ETF	$30,742.50	3.48%	6,590,645	$91.75	0.01%	
LQD	iShares iBoxx $ Investment Grade Corporate Bond ETF	$30,074.00	-0.13%	20,074,356	$102.54	-0.28%	
IEF	iShares 7-10 Year Treasury Bond ETF	$27,518.80	-2.45%	6,976,854	$91.73	-0.03%	
VTEB	Vanguard Tax-Exempt Bond ETF	$27,212.20	-0.52%	3,866,986	$48.33	-0.08%	

So, I expect a little calm here for a bit and then, probably as we get into earnings season, folks will have a lot to digest regarding the outlook for stocks/earnings, their end of year statements, the economic outlook for next year, what to sell for tax losses, and numerous other considerations. Let's see how forward looking the Sybil-like/schizophrenic markets will be.

Volatility Trades:

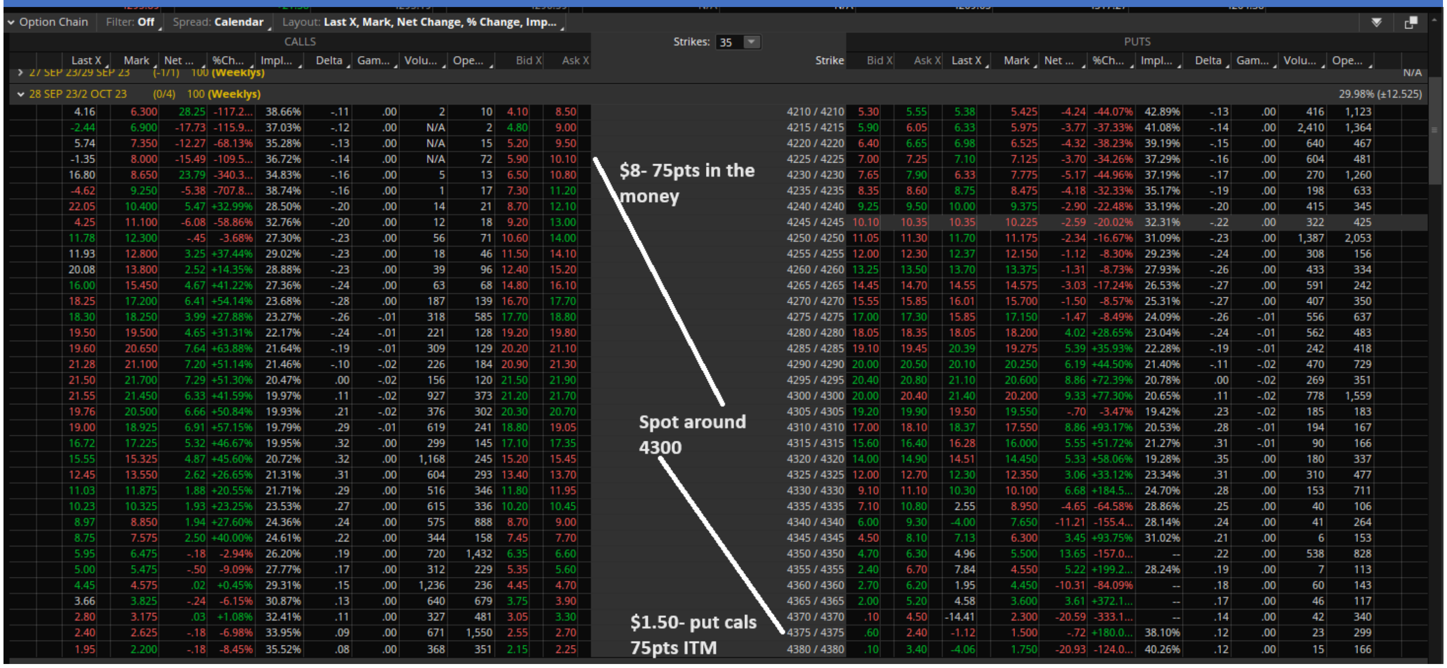
SPX CPI call calendar spread

Sell Oct 11th 4325 call

Buy Oct 13th 4325 call

Net debit: $6.00-40

I'm flipping the script a little. And there are two reasons why I'm gravitating to calls instead of puts. The IV structure and the gain/loss distribution. Look at today/Tuesday two-day call calendar spreads:



Option Chain Filter: Off Spread: Calendar Layout: Last X, Mark, Net Change, % Change, Imp...

Strikes: 35

27 SEP 23/29 SEP 23 (-1/1) 100 (Weeklys) N/A

28 SEP 23/2 OCT 23 (0/4) 100 (Weeklys) 29.98% (±12.525)

CALLS

Strike	Last X	Mark	Net ...	%Ch...	Impl...	Delta	Gam...	Volu...	Ope...	Bid X	Ask X
4210 / 4210	4.16	6.300	28.25	-117.2...	38.66%	-.11	.00	2	10	4.10	8.50
4215 / 4215	-2.44	6.900	-17.73	-115.9...	37.03%	-.12	.00	N/A	2	4.80	9.00
4220 / 4220	5.74	7.350	-12.27	-68.13%	35.28%	-.13	.00	N/A	15	5.20	9.50
4225 / 4225	-1.35	8.000	-15.49	-109.5...	36.72%	-.14	.00	N/A	72	5.90	10.10
4230 / 4230	16.80	8.650	23.79	-340.3...	34.83%	-.16	.00	5	13	6.50	10.80
4235 / 4235	-4.62	9.250	-5.38	-707.8...	38.74%	-.16	.00	1	17	7.30	11.20
4240 / 4240	22.05	10.400	5.47	+32.99%	28.50%	-.20	.00	14	21	8.70	12.10
4245 / 4245	4.25	11.100	-6.08	-58.86%	32.76%	-.20	.00	12	18	9.20	13.00
4250 / 4250	11.78	12.300	-.45	-3.68%	27.30%	-.23	.00	56	71	10.60	14.00
4255 / 4255	11.93	12.800	3.25	+37.44%	29.02%	-.23	.00	18	46	11.50	14.10
4260 / 4260	20.08	13.800	2.52	+14.35%	28.88%	-.23	.00	39	96	12.40	15.20
4265 / 4265	16.00	15.450	4.67	+41.22%	27.36%	-.24	.00	63	68	14.80	16.10
4270 / 4270	18.25	17.200	6.41	+54.14%	23.68%	-.28	.00	187	139	16.70	17.70
4275 / 4275	18.30	18.250	3.99	+27.88%	23.27%	-.26	-.01	318	585	17.70	18.80
4280 / 4280	19.50	19.500	4.65	+31.31%	22.17%	-.24	-.01	221	128	19.20	19.80
4285 / 4285	19.60	20.650	7.64	+63.88%	21.64%	-.19	-.01	309	129	20.20	21.10
4290 / 4290	21.28	21.100	7.20	+51.14%	21.46%	-.10	-.02	226	184	20.90	21.30
4295 / 4295	21.50	21.700	7.29	+51.30%	20.47%	.00	-.02	156	120	21.50	21.90
4300 / 4300	21.55	21.450	6.33	+41.59%	19.97%	.11	-.02	927	373	21.20	21.70
4305 / 4305	19.76	20.500	6.66	+50.84%	19.93%	.21	-.02	376	302	20.30	20.70
4310 / 4310	19.00	18.925	6.91	+57.15%	19.79%	.29	-.01	619	241	18.80	19.05
4315 / 4315	16.72	17.225	5.32	+46.67%	19.95%	.32	.00	299	145	17.10	17.35
4320 / 4320	15.55	15.325	4.87	+45.60%	20.72%	.32	.00	1,168	245	15.20	15.45
4325 / 4325	12.45	13.550	2.62	+26.65%	21.31%	.31	.00	604	293	13.40	13.70
4330 / 4330	11.03	11.875	1.88	+20.55%	21.71%	.29	.00	516	346	11.80	11.95
4335 / 4335	10.23	10.325	1.93	+23.25%	23.53%	.27	.00	615	336	10.20	10.45
4340 / 4340	8.97	8.850	1.94	+27.60%	24.36%	.24	.00	575	888	8.70	9.00
4345 / 4345	8.75	7.575	2.50	+40.00%	24.61%	.22	.00	344	158	7.45	7.70
4350 / 4350	5.95	6.475	-.18	-2.94%	26.20%	.19	.00	720	1,432	6.35	6.60
4355 / 4355	5.00	5.475	-.50	-9.09%	27.77%	.17	.00	312	229	5.35	5.60
4360 / 4360	4.45	4.575	.02	+0.45%	29.31%	.15	.00	1,236	236	4.45	4.70
4365 / 4365	3.66	3.825	-.24	-6.15%	30.87%	.13	.00	640	679	3.75	3.90
4370 / 4370	2.80	3.175	.03	+1.08%	32.41%	.11	.00	327	481	3.05	3.30
4375 / 4375	2.40	2.625	-.18	-6.98%	33.95%	.09	.00	671	1,550	2.55	2.70
4380 / 4380	1.95	2.200	-.18	-8.45%	35.52%	.08	.00	368	351	2.15	2.25

PUTS

Strike	Bid X	Ask X	Last X	Mark	Net ...	%Ch...	Impl...	Delta	Gam...	Volu...	Ope...
4210 / 4210	5.30	5.55	5.38	5.425	-4.24	-44.07%	42.89%	-.13	.00	416	1,123
4215 / 4215	5.90	6.05	6.33	5.975	-3.77	-37.33%	41.08%	-.14	.00	2,410	1,364
4220 / 4220	6.40	6.65	6.98	6.525	-4.32	-38.23%	39.19%	-.15	.00	640	467
4225 / 4225	7.00	7.25	7.10	7.125	-3.70	-34.26%	37.29%	-.16	.00	604	481
4230 / 4230	7.65	7.90	6.33	7.775	-5.17	-44.96%	37.19%	-.17	.00	270	1,260
4235 / 4235	8.35	8.60	8.75	8.475	-4.18	-32.33%	35.17%	-.19	.00	198	633
4240 / 4240	9.25	9.50	10.00	9.375	-2.90	-22.48%	33.19%	-.20	.00	415	345
4245 / 4245	10.10	10.35	10.35	10.225	-2.59	-20.02%	32.31%	-.22	.00	322	425
4250 / 4250	11.05	11.30	11.70	11.175	-2.34	-16.67%	31.09%	-.23	.00	1,387	2,053
4255 / 4255	12.00	12.30	12.37	12.150	-1.12	-8.30%	29.23%	-.24	.00	308	156
4260 / 4260	13.25	13.50	13.70	13.375	-1.31	-8.73%	27.93%	-.26	.00	433	334
4265 / 4265	14.45	14.70	14.55	14.575	-3.03	-17.24%	26.53%	-.27	.00	591	242
4270 / 4270	15.55	15.85	16.01	15.700	-1.50	-8.57%	25.31%	-.27	.00	407	350
4275 / 4275	17.00	17.30	15.85	17.150	-1.47	-8.49%	24.09%	-.26	-.01	556	637
4280 / 4280	18.05	18.35	18.05	18.200	4.02	+28.65%	23.04%	-.24	-.01	562	483
4285 / 4285	19.10	19.45	20.39	19.275	5.39	+35.93%	22.28%	-.19	-.01	242	418
4290 / 4290	20.00	20.50	20.10	20.250	6.19	+44.50%	21.40%	-.11	-.02	470	729
4295 / 4295	20.40	20.80	21.10	20.600	8.86	+72.39%	20.78%	.00	-.02	269	351
4300 / 4300	20.00	20.40	21.40	20.200	9.33	+77.30%	20.65%	.11	-.02	778	1,559
4305 / 4305	19.20	19.90	19.50	19.550	-.70	-3.47%	19.42%	.23	-.02	185	183
4310 / 4310	17.00	18.10	18.37	17.550	8.86	+93.17%	20.53%	.28	-.01	194	167
4315 / 4315	15.60	16.40	16.28	16.000	5.55	+51.72%	21.27%	.31	-.01	90	166
4320 / 4320	14.00	14.90	14.51	14.450	5.33	+58.06%	19.28%	.35	.00	180	337
4325 / 4325	12.00	12.70	12.30	12.350	3.06	+33.12%	23.34%	.31	.00	310	477
4330 / 4330	9.10	11.10	10.30	10.100	6.68	+184.5...	24.70%	.28	.00	153	711
4335 / 4335	7.10	10.80	2.55	8.950	-4.65	-64.58%	28.86%	.25	.00	40	106
4340 / 4340	6.00	9.30	-4.00	7.650	-11.21	-155.4...	28.14%	.24	.00	41	264
4345 / 4345	4.50	8.10	7.13	6.300	3.45	+93.75%	31.02%	.21	.00	6	153
4350 / 4350	4.70	6.30	4.96	5.500	13.65	-157.0...	--	.22	.00	538	828
4355 / 4355	2.40	6.70	7.84	4.550	5.22	+199.2...	28.24%	.19	.00	7	113
4360 / 4360	2.70	6.20	1.95	4.450	-10.31	-84.09%	--	.18	.00	60	143
4365 / 4365	2.00	5.20	4.58	3.600	3.61	+372.1...	--	.17	.00	46	117
4370 / 4370	.10	4.50	-14.41	2.300	-20.59	-333.1...	--	.14	.00	42	340
4375 / 4375	.60	2.40	-1.12	1.500	-.72	+180.0...	38.10%	.12	.00	23	299
4380 / 4380	.10	3.40	-4.06	1.750	-20.93	-124.0...	40.26%	.12	.00	15	166

For a while now, there has been a skew toward calls, could be rates, could be demand, but essentially, calls have been holding IV better. Put smashing/vol offering is a hot market dynamic lately. So in the case of put calendars, when they go deep ITM when the market drops, they are worthless or even have to be closed for a debit. And when the market shoots higher, the IV gets annihilated and the put calendars 1%+ out of the money evaporate quickly.

Conversely, when we get a spike up, the call calendars do just fine with the call skew in place. You can see here, 2% in the money, they still earn. They cost more initially but they have more of a yield type behavior with a larger margin for error. Target, $10.

VIXPIRATION AND THE FED MEETING COMBINE AS THE REAL UNCLENCH – IMPLIED VOL REMAINS UNDERPRICED – OUTSTANDING TRADE OPPORTUNITY TO OWN NOVEMBER FED MEETING VOLATILITY

VOLATILITY SUMMARY

From the August 25th note:

Vixpiration comes the day the Fed meets the week after all that. A nice recipe for more volatility.

From the August 14th note:

You might be able to use declining vol around vixpiration to get this at a better price through Wednesday morning or move the strikes up a bit.

Good ole vixpiration. A recurring theme in this note, in that it often represents vol's watershed between low/lower vol and rising vol. And it just so happened that the September quarterly unclench waited for it this month. It got no fanfare because, well, once in a while it comes *after* options expiration Friday, the three or four months per year when you have a five-week opex cycle. So, print out this calendar or put it on your computer desktop lest you forget about it:

https://cdn.cboe.com/resources/options/Cboe2023OPTIONSCalendar.pdf

It really amazes me, the returns attainable in naked long options these days. I've been talking about this in individual names with charts the last few weeks. You don't even need to get the direction right a lot of the time, strangle/straddle long premium folks are actually making money these days, in quite the flip of conventional thinking/trading. The markets have discounted options to the point where they are cheap to own outright, and by a significant margin.

And, the market hands them out in front of volatility events for cheap prices no less!

So, way back on Tuesday, the 0DTE crowd was enjoying yet another low volume option driven bounce off the morning lows, and folks went to the usual vol playbook; they smashed vol for the millionth time this year, selling puts and buying calls and yet again the Tuesday 0DTE call minted a fortune in a few hours, demonstrating the cheapness of vol and why folks are gravitating to this arena:

This is way better than state lottery tickets by a long shot. It happens multiple times a week in the indices, you don't even have to pick the right stock! (Right? It's not like, "I'll take 10 #52s and 20

#37s") Imagine if folks in my state, the greatest degenerate lotto state in the U.S. realized these returns were out there:

Scott @VolatilityWiz · Sep 16

A pretty alarming stat, Mass leads the nation in lottery spending per person (lottery sales/population). Look how insane that number is:

Massachusetts

- **Annual amount spent on lottery per person:** $951.92
- **Annual lottery prize per person:** $701.50

Massachusetts residents spend over $400 more than residents of Georgia when it comes to buying lottery tickets – a whopping $951.92 per person. They do see a return, however. Just over $700 per person went to prize money in 2020.

7 12 2,550

Now, fast forward to the infamous vixpiration and the Fed meeting. Yes, Ye Olde Dot Plot did it's thing, but it's not like there wasn't advance warning, right?

September sees Fed dot plot thicken

By **Mike Dolan**

August 30, 2023 3:44 AM EDT · Updated 23 days ago

Aa

LONDON, Aug 30 (Reuters) - Markets appear to have batted away next month's Federal Reserve gathering as a paused 'also ran' meeting in favor of second-guessing about a November rate hike - but next month may hold the key to finally unlocking the end of the tightening cycle.

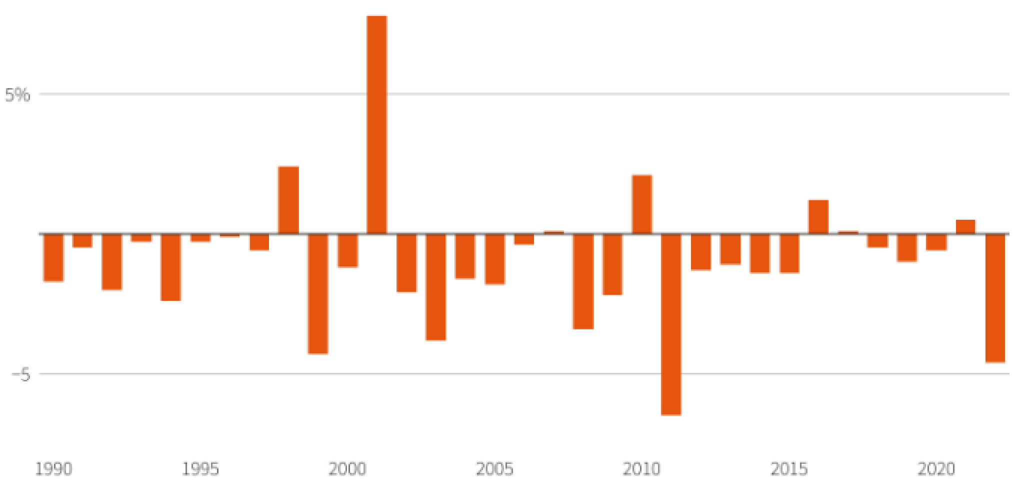
https://www.reuters.com/markets/europe/september-sees-fed-dot-plot-thicken-2023-08-30/

And, on top of this, weren't we besieged with warnings about how this was the worst week of the year for stocks?

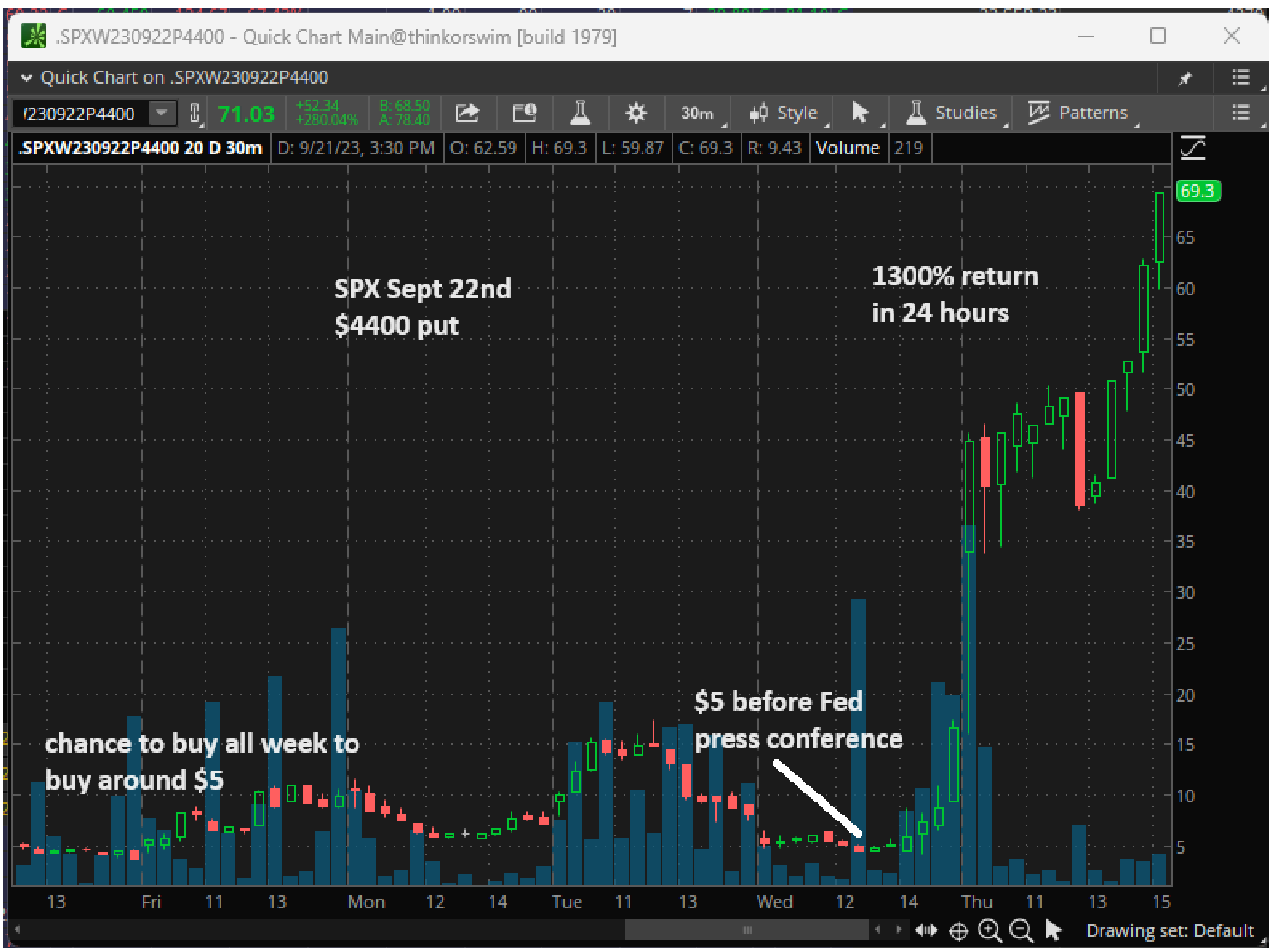
Source: https://www.reuters.com/markets/us/fed-meeting-comes-during-historically-tough-week-us-stocks-2023-09-12/

The September effect

In 26 of the last 33 years, the S&P 500 fell in the week following the September options expiration, with a median drop of 1%

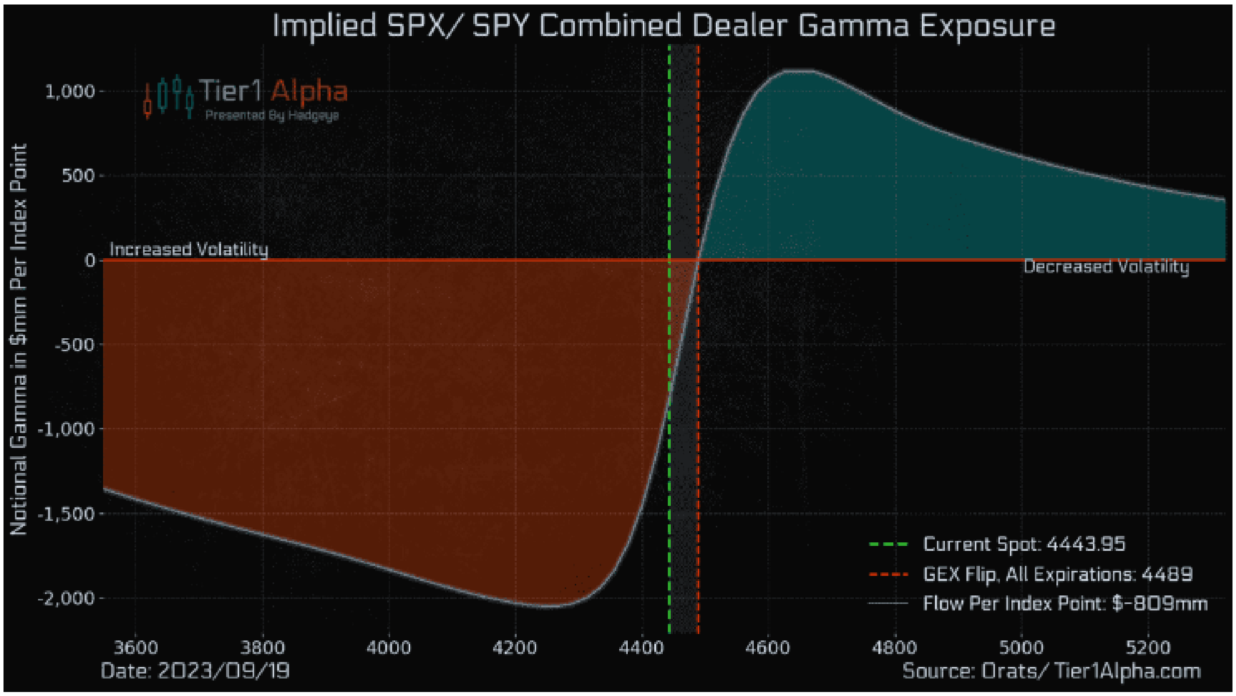


So, we have a volatility event, for which there was clear notice that the Fed could come out hawkish in their rates curve, and we had proof that the equity markets hate this week, so how do you explain this???



And to boot, it's not like the gamma surface wasn't signaling/hinting that a swift slide down was quite possible at these prices:

GAMMA EXPOSURE:



Dealers remain in negative gamma, with yesterday's intraday chase almost textbook. Expect more of the same today, punctuated by last-minute hedging activity around the Fed's release. With significant gamma expiring today, the most likely outcome is high intraday vol and a rush to monetize hedges following the Fed. All else equal, this biases us higher as volatility exits the equity market.

Source: Tier1Alpha Tuesday AM note

You'll see one thing here and read another. What you see is the market sitting on a steep gamma slope, which means that down means more and more dealer selling to hedge delta/gamma. What you read is what everyone expected, a vol crush post Fed will push markets up by the opposite dynamic.

One big problem with that though.

The 1% out-of-the-money $4400 put in the chart above, the one that printed someone a fortune today, well, that was only $5. So, when you think about it, how much premium is there actually to burn to push up the market? Almost none, as it turns out. Owning it was the brilliant move even though the warnings signs were everywhere.

(Did I own this? No, I primarily spent the week closing out all the vol trades I had set up going into this week for CPI/Fed and wasn't focused on vixpiration; I most certainly won't make that mistake again- vixpiration and the Fed collide in December during a quarterly opex week, Mon Dieu!)

But the patterns of routine vol crushing, the habitual trading of vol crushing, the new funds/growing space in funds that sell vol, the army of 0DTE vol sellers, all this has warped/contorted option markets away from one of/the original primary purpose. Do you remember what that was? I know this is going to sound strange to you, but.....portfolio hedging/insurance!

Remember when folks would think about, wow, this sounds strange to write it, but imagine, ahem, purchasing a put option to protect gains in your portfolio if you are up significantly year to date. What a novel concept. Let's say you did that this week, because you:

A. Are up big on the year because you bought giga tech stocks late last year/early this year
B. Realize that the markets are narrow and that giga tech is basically the market these days
C. Knew this was the worst week of the year for stocks
D. Expected the Fed to raise the outlook for rates this year/dot pot
E. Saw that vol was as cheap as ever before all this

Hey now, was that a puzzle that was tough to put together? And what if it didn't work out? Not even a paper cut, right? You don't have to be a degenerate lotto junkie to have bought a -1% OTM put when you consider the simple rationale above.

But what a time to hedge! You pay almost nothing into what implied vol used to consider to be binary market events, you make a thousand percent sometimes, and make enough to pay to do it again and maybe fail nine more times. Is this how the insurance industry works? This is what Buffett would call a soft insurance market, one where the insurance premiums are too low and eventually the sellers get forcibly dragged out of the business of selling it. (See volmageddon.)

It's difficult to change methods when markets change, I know. I've been writing about this for some time now, looking at options in a way I generally don't, owning premium outright sometimes. It might be easier if you can set some parameters for doing it, like checking a few boxes on the setup. For example, regarding that Tuesday call, perhaps a future similar situation might be:

A. Is it cheap, like 1-2 SPX points?
B. Is the mkt down .5% or more?
C. Have the European markets closed?
D. Is there a risk event the next day?

That's a basic start for an afternoon 0DTE. When it comes to today, well, see points A to E above.

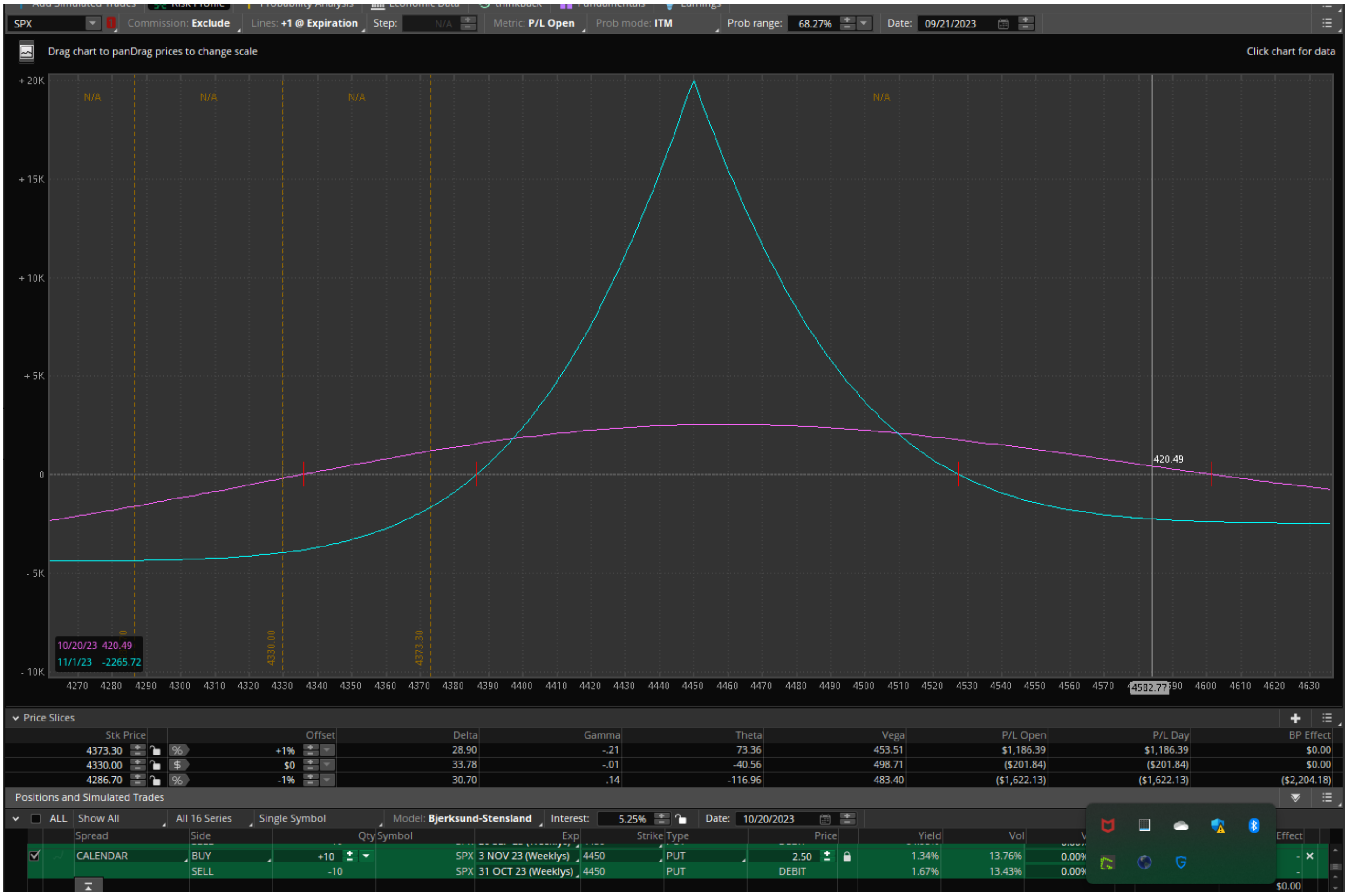
Volatility Trades:

SPX Fed meeting week put calendar spread

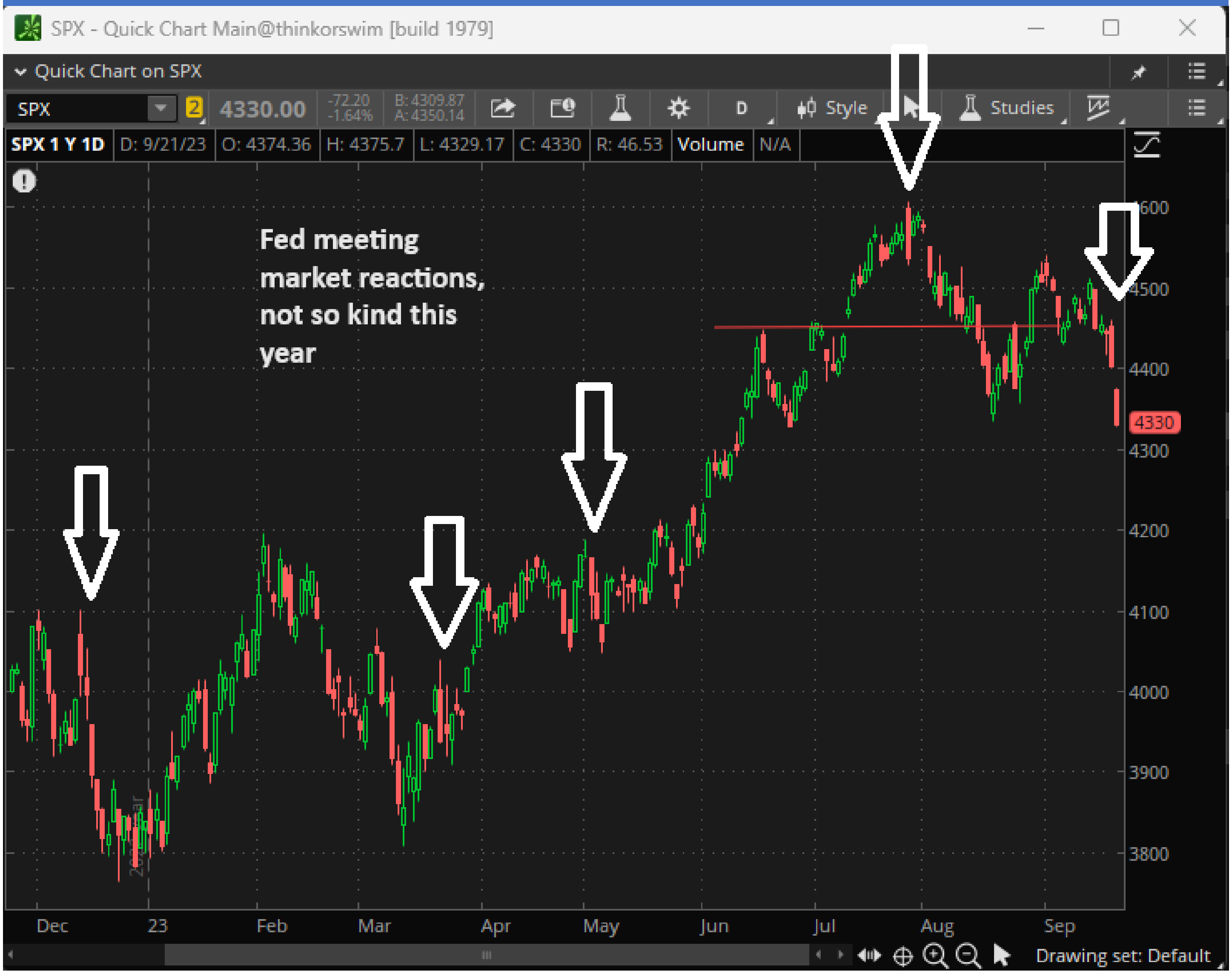
Sell SPX Oct 31st 4450 put

Buy SPX Nov 3rd 4450 put

Net debit: $2.50-3.00



I started these for $3 but they are probably only 2.50 to 2.75 now. Amazing price, when you consider it finally might dawn on markets/vol sellers to not get run over by Fed day reactions when they have been pretty much horrible with consistently mispriced vol:

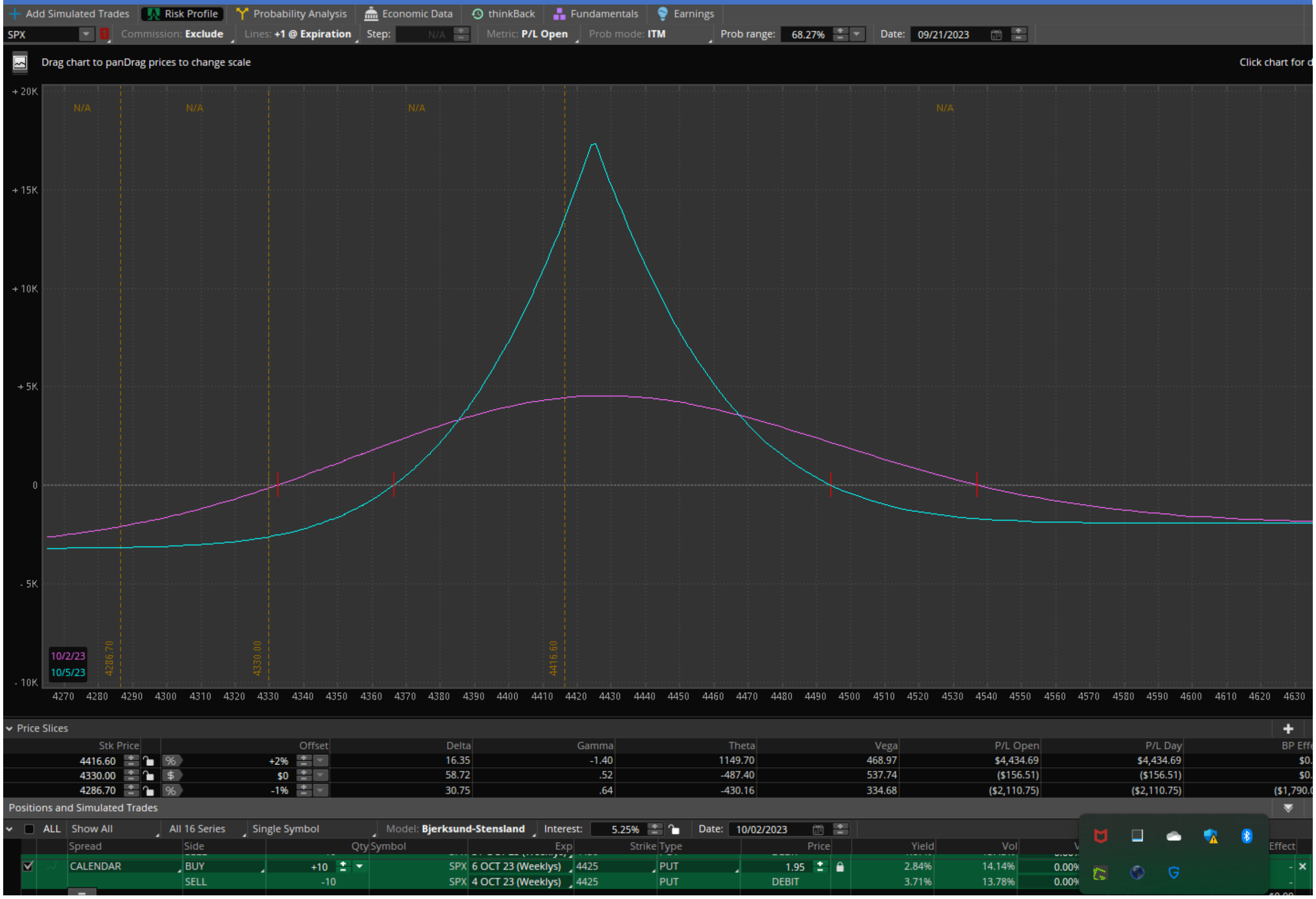


SPX non-farm payrolls release put calendar spread

Sell $4425 Oct 4th put

Buy $4425 Oct 6th put

Net debit: $1.50-2



I set these above spot anticipating a bounce into either end of month/first day of the month, and if it goes lower into next week I will add hoping to get some closer to $1 or potentially adjust by adding cheap call diagonal spreads. Additionally, JOLTS is the day before the short leg, and the market shot up sizably in early September.

QUARTERLY OPEX/EX-DIV PATTERN HOLDS SERVE- VOL CONTINUES TO BE SOLD REGARDLESS OF EVENT RISK – TRADES FOR NFLX EARNINGS/END OF MONTH

VOLATILITY SUMMARY

From the September 6th note:

In the meantime, when IV gets stupidly oversold, you can simply grab insanely cheap puts in giga herd stocks like AAPL. I was going to put a bearish long put spread trade of some sort in today's note for after the Iphone event. And then, it has a -3% day and I missed the trade. Look at how stupidly low priced the puts for this week were:

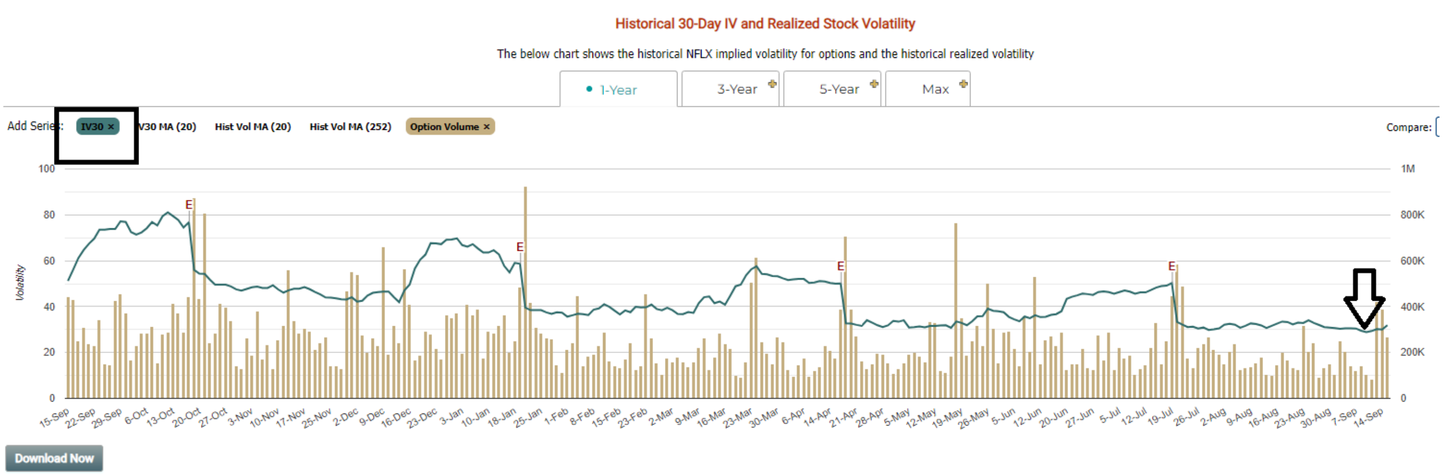
Oh well, I'm sure there will be more opportunities like this as folks continue to offer vol and the opex cycles/0DTE/systematic funds continue to do their thing.

The options markets are always changing, and I'm constantly trying to figure out where vol is over or underpriced; there is always some area of the vol surface that is offering an opportunity.

While the trades in the note have been doing quite well, I'm aggravated by missing another asymmetric risk to reward opportunity, especially when I specifically wrote two weeks ago to keep an eye out for stupidly low vol in the giga/popular tech names. This time it was in NFLX:

(As of this writing, these options are now up 4200%)

Now, here's the thing. Look at the NFLX implied vol chart:



Implied vol was sitting at around 28% heading into this week, easily a 52-week low for a stock that consistently sees IV over 50%. And, the stock was up over 100% on a one-year basis and 50% this year.

And…they were presenting at the BofA communications and entertainment conference. This is corporate conference season and often where news/revelations/updates/guidance comes out and boy did they drop the hammer with a downbeat outlook on the ad-based streaming subscriptions.

So, opportunity missed. The good news is that this depressed implied vol situation is not going away, and that is why it's time to continue to focus on underpriced vol going forward. Folks keep smashing it for yield, and it's not just the 0DTE crowd either; vol out on the surface (out in tenor) is extremely inexpensive and it comes at a time when mega tech, being up so much this year, is most certainly vulnerable to a rapid exit from managers that got it right and don't want to see that outperformance melt away before the year-end statements are mailed.

In fact, Charlie the celebrity quant pointed out this week that a mega tech earnings surprise is most certainly a general market risk considering how propped they've made the entire market being up so much YTD:

> At the same time, not everyone believes high yields are currently the market's biggest risk. Charlie McElligott, managing director and cross-asset macro strategist at Nomura, said the market was vulnerable to an "earnings shock" to one of the handful of megacap stocks that have led markets higher this year, such as Nvidia (NVDA.O). Companies will begin reporting third-quarter earnings next month.
>
> "If [the AI] story starts to lose air it doesn't matter what the interest rates do because there is so much earnings growth built into their share prices," he said. "Earnings are what matter from here, particularly with an AI sector that needs to justify expectations."

Source: https://www.reuters.com/markets/us/higher-longer-rates-remain-threat-us-stocks-after-inflation-data-2023-09-13/

Now, you'd think with a Fed meeting imminent, people would be buying cheap puts on their darling giga tech right? Well, not so much, SPX 9-day vol, the Fed meeting window, is still in the gutter after being smashed to oblivion post CPI, even as the market is down sizably today:

And, outside of the Fed meeting it's not like the warnings haven't been out about next week/unclench, as I highlighted in last week's note:

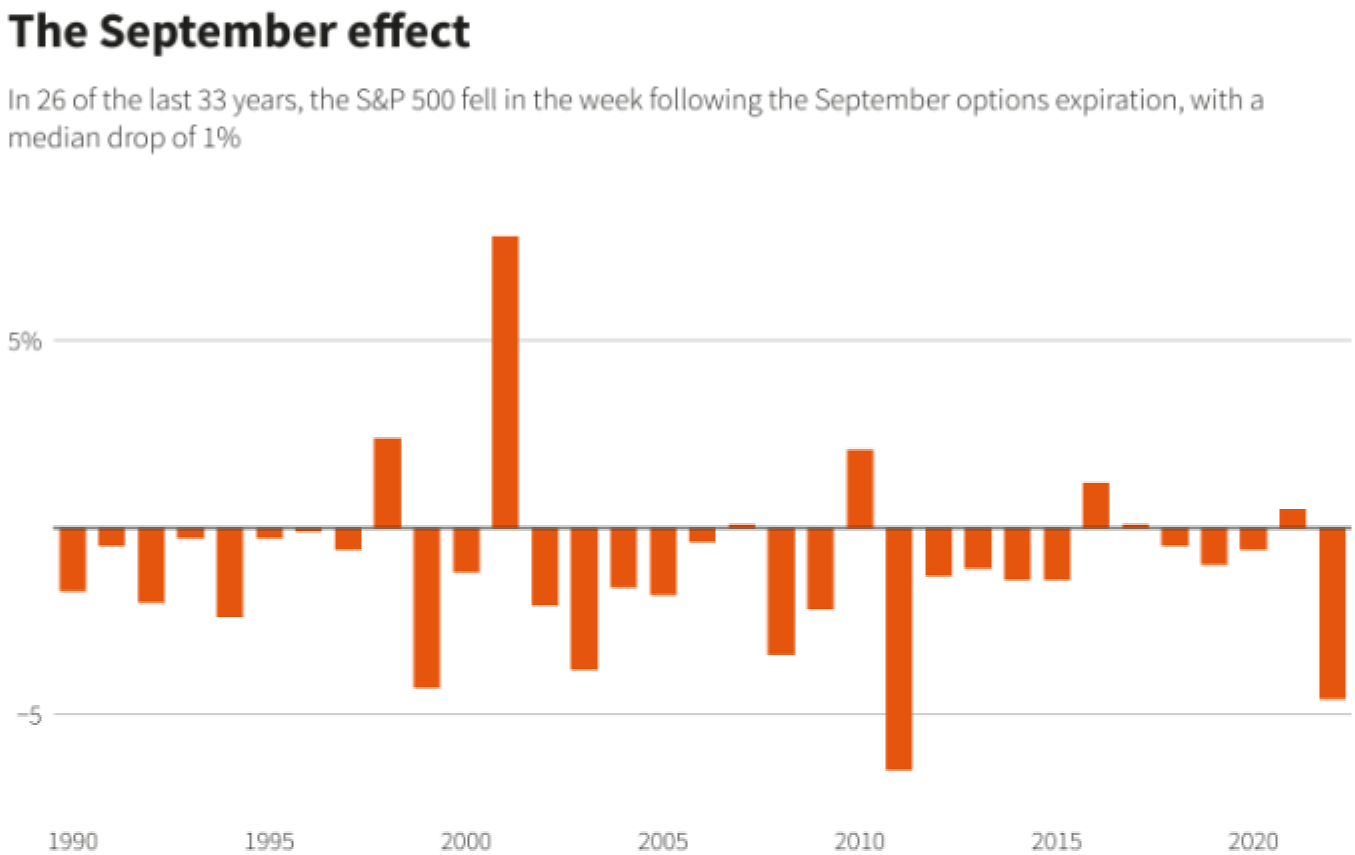
Macro Matters

Fed meeting comes during historically tough week for US stocks

By **Saqib Iqbal Ahmed**

September 12, 2023 12:51 PM EDT · Updated 3 days ago

Aa



Source: https://www.reuters.com/markets/us/fed-meeting-comes-during-historically-tough-week-us-stocks-2023-09-12/

But that didn't inspire folks to buy puts yesterday after that insane vol crush. And to boot, this pattern around quarterly opex is almost too predictable, how aren't there A.I. programs already sweeping puts at 9% IV for quant funds when it's right in front of everyone in multiple ways. Look at June's quarterly OPEX behavior:

And March quarterly OPEX:

I'm looking forward to Decembers quarterly opex week already, there is a Fed meeting on that Wednesday which will make the trades even more delightful. (re:cheap)

Well, if this is how it's going to be, if the options market is going to continue to smash event vol before the actual events arrive, for yield, and leave mega tech/index puts lying around weeks out for nickels, owning vol naked is now a thing and that is an adjustment I am making. Take what the vol surface is giving right? The smashing of the vol ironically is what helps make the names/indices more volatile, intraday anyway.

Volatility Trades:

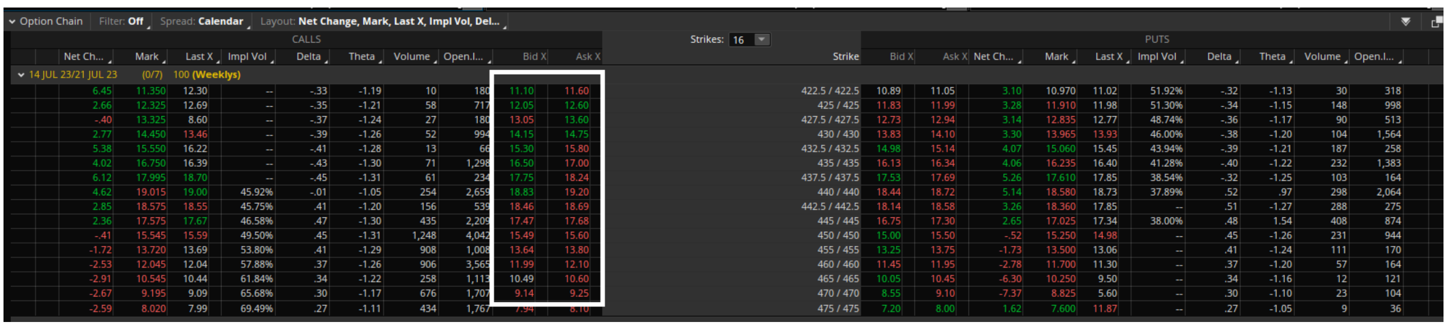
NFLX earnings week call calendar spread

Sell Oct 13th call

Buy Oct 20th call

Net debit: $7.50

How these spreads priced before earnings week in July:


Option Chain Filter: Off Spread: Calendar Layout: Net Change, Mark, Last X, Impl Vol, Del... Strikes: 16

14 JUL 23/21 JUL 23 (0/7) 100 (Weeklys)

CALLS Net Ch...	Mark	Last X	Impl Vol	Delta	Theta	Volume	Open.I...	Bid X	Ask X	Strike	PUTS Bid X	Ask X	Net Ch...	Mark	Last X	Impl Vol	Delta	Theta	Volume	Open.I...
6.45	11.350	12.30	--	-.33	-1.19	10	180	11.10	11.60	422.5 / 422.5	10.89	11.05	3.10	10.970	11.02	51.92%	-.32	-1.13	30	318
2.66	12.325	12.69	--	-.35	-1.21	58	717	12.05	12.60	425 / 425	11.83	11.99	3.28	11.910	11.98	51.30%	-.34	-1.15	148	998
-.40	13.325	8.60	--	-.37	-1.24	27	180	13.05	13.60	427.5 / 427.5	12.73	12.94	3.14	12.835	12.77	48.74%	-.36	-1.17	90	513
2.77	14.450	13.46	--	-.39	-1.26	52	994	14.15	14.75	430 / 430	13.83	14.10	3.30	13.965	13.93	46.00%	-.38	-1.20	104	1,564
5.38	15.550	16.22	--	-.41	-1.28	13	66	15.30	15.80	432.5 / 432.5	14.98	15.14	4.07	15.060	15.45	43.94%	-.39	-1.21	187	258
4.02	16.750	16.39	--	-.43	-1.30	71	1,298	16.50	17.00	435 / 435	16.13	16.34	4.06	16.235	16.40	41.28%	-.40	-1.22	232	1,383
6.12	17.995	18.70	--	-.45	-1.31	61	234	17.75	18.24	437.5 / 437.5	17.53	17.69	5.26	17.610	17.85	38.54%	-.32	-1.25	103	164
4.62	19.015	19.00	45.92%	-.01	-1.05	254	2,659	18.83	19.20	440 / 440	18.44	18.72	5.14	18.580	18.73	37.89%	.52	.97	298	2,064
2.85	18.575	18.55	45.75%	.41	-1.20	156	539	18.46	18.69	442.5 / 442.5	18.14	18.58	3.26	18.360	17.85	--	.51	-1.27	288	275
2.36	17.575	17.67	46.58%	.47	-1.30	435	2,209	17.47	17.68	445 / 445	16.75	17.30	2.65	17.025	17.34	38.00%	.48	1.54	408	874
-.41	15.545	15.59	49.50%	.45	-1.31	1,248	4,042	15.49	15.60	450 / 450	15.00	15.50	-.52	15.250	14.98	--	.45	-1.26	231	944
-1.72	13.720	13.69	53.80%	.41	-1.29	908	1,008	13.64	13.80	455 / 455	13.25	13.75	-1.73	13.500	13.06	--	.41	-1.24	111	170
-2.53	12.045	12.04	57.88%	.37	-1.26	906	3,565	11.99	12.10	460 / 460	11.45	11.95	-2.78	11.700	11.30	--	.37	-1.20	57	164
-2.91	10.545	10.44	61.84%	.34	-1.22	258	1,113	10.49	10.60	465 / 465	10.05	10.45	-6.30	10.250	9.50	--	.34	-1.16	12	121
-2.67	9.195	9.09	65.68%	.30	-1.17	676	1,707	9.14	9.25	470 / 470	8.55	9.10	-7.37	8.825	5.60	--	.30	-1.10	23	104
-2.59	8.020	7.99	69.49%	.27	-1.11	434	1,767	7.94	8.10	475 / 475	7.20	8.00	1.62	7.600	11.87	--	.27	-1.05	9	36

This stock almost always moves on earnings, that is plainly obvious, but good to be reminded how large those moves can be:

Stock Price Performance - Last 12 Quarterly Earnings				
Day of Earnings				
Earnings Move	Opening Gap	Open-to-High	Open-to-Low	Drift Open-to-Close
-8.4%	-6.5%	+0.4%	-3.3%	-2.1%
-3.2%	-3.1%	+0.7%	-2.3%	-0.1%
+8.5%	+6.5%	+2.3%	-1.1%	+1.9%
+13.1%	+10.1%	+5.4%	-0.9%	+2.7%
+7.4%	+3.3%	+4.2%	-3.9%	+3.9%
-35.1%	-29.7%	+1.5%	-13.3%	-7.7%
-21.8%	-21.3%	+2.3%	-5.0%	-0.6%
-2.2%	-2.2%	+2.0%	-1.3%	0.0%
-3.3%	-0.9%	+0.9%	-3.9%	-2.4%
-7.4%	-7.7%	+1.6%	-0.8%	+0.3%
+16.9%	+12.5%	+5.1%	-1.3%	+3.9%
-6.9%	-4.6%	+1.1%	-2.6%	-2.4%

Target, $11-13.

IWM ex-div call calendar spread

Sell Sep 25th $186 call

Buy Sep 29th $186 call

Net debit: .20-22

$IWM is going ex-div on the 26th, and it's expected to be about .80, so the back leg is pricing that in, making this spread extremely cheap. As we get closer, the spread should widen, and if it doesn't you can just own cheap calls with a full trading week into what has become typical end of month strength:


IWM - Quick Chart Main@thinkorswim [build 1978]
Quick Chart on IWM
IWM
ISHARES TRUST...
183.61
-1.94
-1.05%
B: 183.61
A: 183.62
Share
Style
Drawings
Studies
Patterns
IWM YTD 1D [NYSE]
D: 9/15/23
O: 184.79
H: 185.07
L: 182.79
C: 183.62
R: 2.28
Volume
28,316,230
June EOQ
EOM Aug
198
196
194
192
190
188
186
183.62
182
180
HistoricalVolatility (20, Annual)
0.150802
0.2
0.1508
ImpVolatility
0.1748
0.22
0.2
0.1748
6/12
6/19
6/26
7/3
7/10
7/17
7/24
7/31
8/7
8/14
8/2
8/28
9/4
9/11
9/18
9/25
Drawing set: Default

TRADE IDEAS WHILE WAITING FOR THE DATA DUMP – IS MONDAY THE NEW THURSDAY?

VOLATILITY SUMMARY

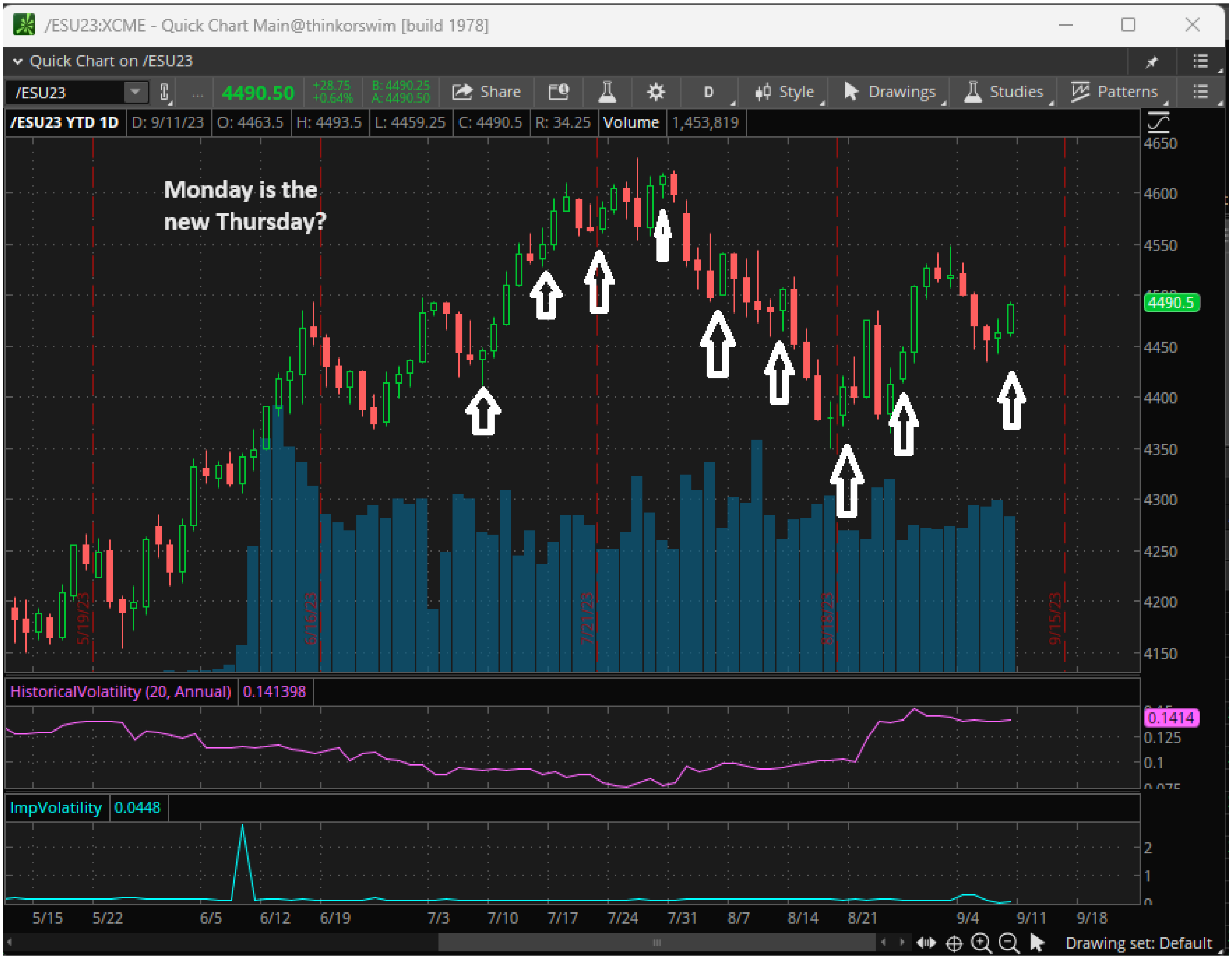
Remember when Thursdays were up almost every week continually?

May 5th note:

One fascinating and profitable pattern, to cement the point above, is this:

I've highlighted most Thursdays and Fridays year-to-date. The simple takeaway is that Thursdays are up days and if Thursday isn't up, the odds are very high that Friday will be. Today is an obvious case in point, but scrutinizing the scene of the crime, big tech options, look at how QQQ has behaved lately:

Fun times. You could buy nearest round number calls in virtually any giga tech herd stock and go to the ATM every Thursday, just like getting a Thursday payday check. Well, there seems to be a new nearly automatic QE call trend that's going brrrrr:



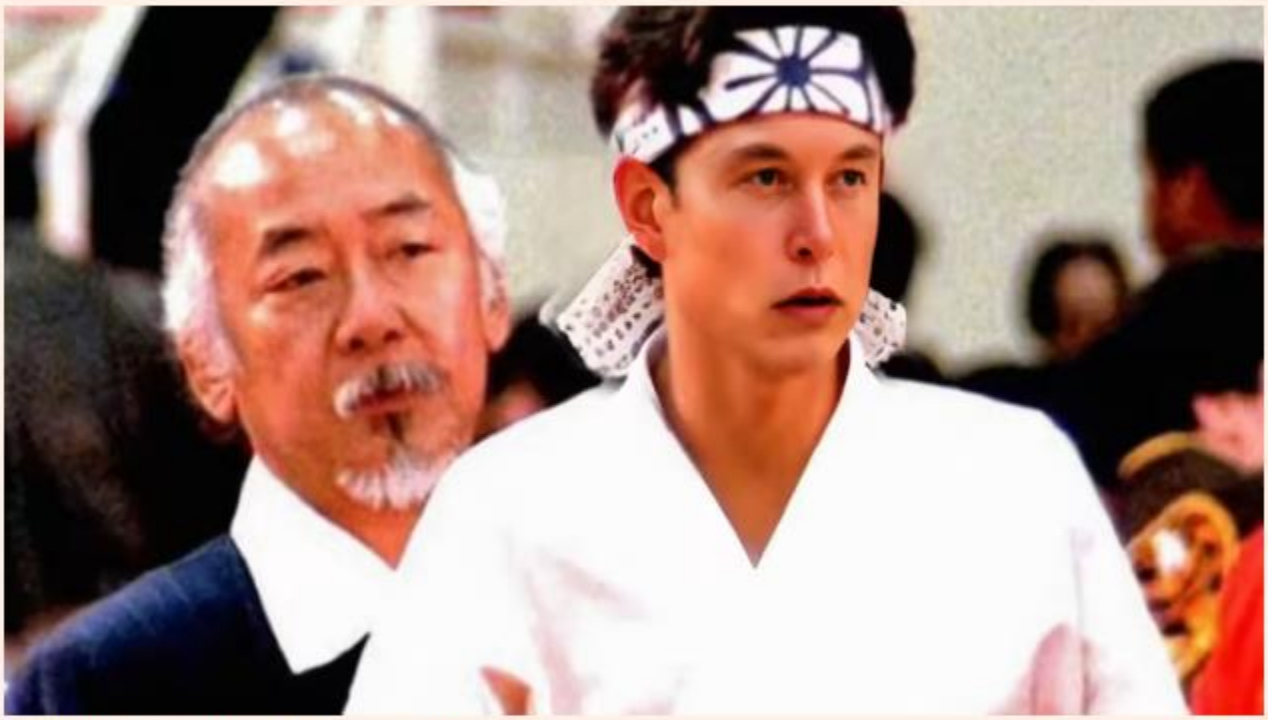
The market doesn't have a case of the Mondays, that is for sure, it's been up every time since June opex, if you can believe that. (There were a couple post-holiday Tuesdays in there to open weeks, not counting those since…well they aren't Mondays.)

And, what did they go for yesterday, yes, giga tech stocks, AMZN, TSLA, META up big. Folks blamed some A.I. 'analyst' comedic research, which is hilariously mocked in this fabulous FT column:

FT Alphaville Artificial intelligence + Add to myFT

Adam Jonas explains why Tesla will be better at being Nvidia than Nvidia

Carmaker is now AI stock, please ignore all previous communications



© FTAV montage / Columbia Pictures / Youtube

Bryce Elder YESTERDAY 41

Source: https://www.ft.com/content/d7f139d3-aebb-4932-8c0e-034c92bce963

Here's an excerpt:

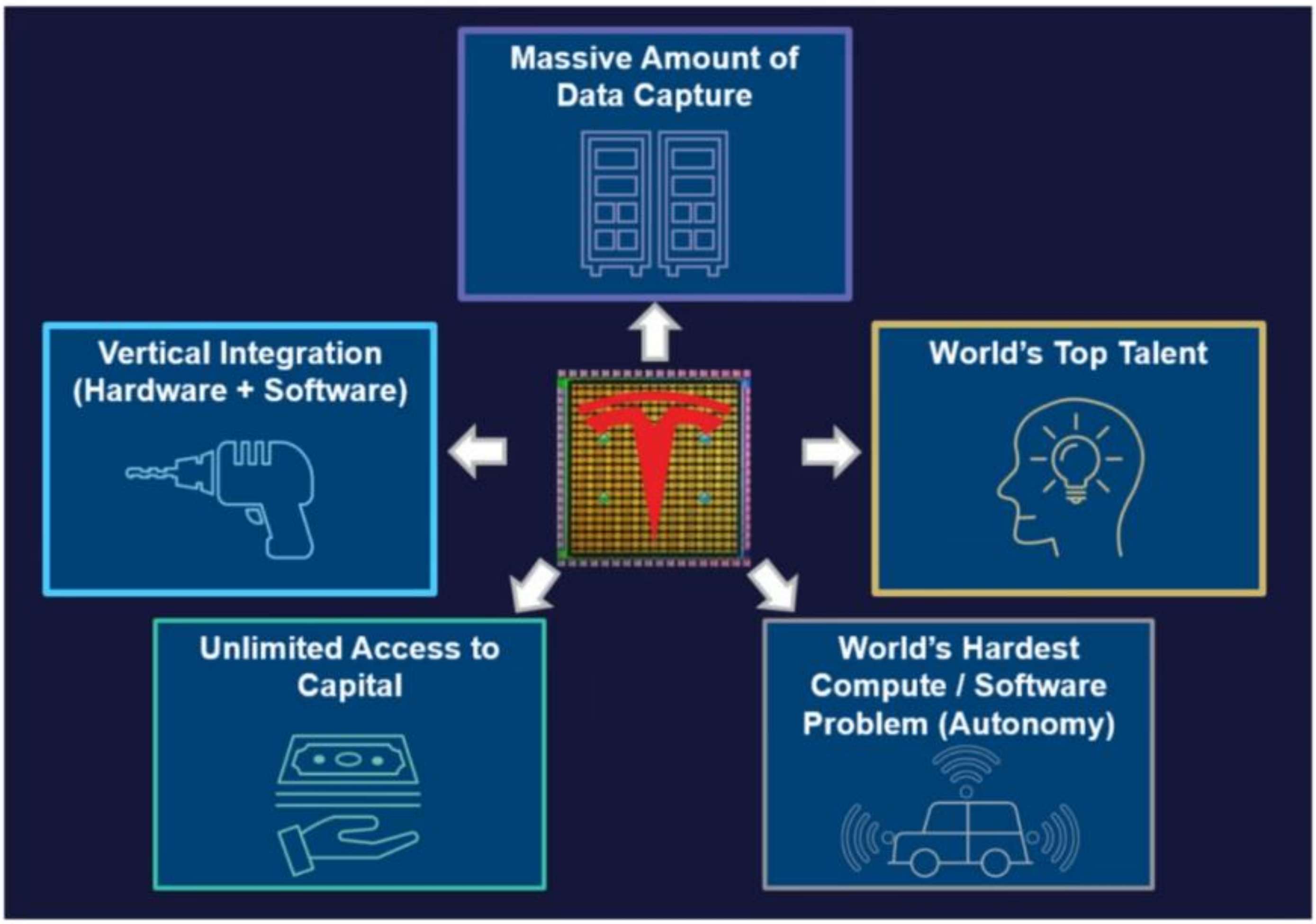
"Citing these updates, Morgan Stanley presumes the Dojo chip will deliver performance six times better than the current-but-one generation of Nvidia A100 GPU boxes, at less than the current $200k-per-unit cost of a single Nvidia box. Fewer boxes might also cut energy use because they'll need less cooling."

And Elder continues by mocking the charts for dummies segment of the 'analysis':

> Tesla is not competing to make a better chip. Tesla is optimizing for a single purpose that can in turn drive an improved total output, at greater efficiency and lower cost. NVIDIA used the demanding performance of gaming to develop the world's most powerful GPU chips. Can Tesla use the demands of autonomous cars/FSD to become a global leader in custom AI chips?

Yes! say Jonas *et al*. Yes it can! Look!

Exhibit 25: Unlocking Tesla's AI Mojo: Enter the Dojo



This is just a sliver of the stand-up the FT writer does, check it out, you will chuckle numerous times.

Anyways, the markets rallied on giga tech Monday again; keep an eye on that pattern. Just be a bit cautious, if a Monday isn't going to work, it might be this Monday. Why you say?

Well, it's a quarterly opex unclench Monday, right? These are typically not good days if the market rallies into them on opex call gamma gaming. So, we will have to see how the market digests all the data that's coming. Secondly, there's this:

Next week is the 38th week of the year. Might not mean much to you, but this is actually the worst week of the year for the **S&P 500** (SPX) going back to 1950. Yes, I just noted how **September options expiration week** (this week) tends to be strong, but it all changes next week. Now the 38th week usually takes place during the latter part of September and we all know that September is usually the worst month. Whatever the exact reason, I think this is something traders should be very aware of going into next week.

Here are the top 10 worst weeks on average. So besides the worst week next week, the 39th week is the 10th worst week. In other words, two of the 10 worst weeks are coming up over the next two weeks. Seasonality isn't doing anyone any favors here.

Worst Weeks Since 1950		
Week	Avg Return	% Higher
38	**-0.59%**	**39%**
19	-0.35%	35%
36	-0.26%	52%
53	-0.23%	45%
25	-0.22%	51%
42	-0.21%	50%
29	-0.18%	43%
32	-0.15%	55%
20	-0.11%	52%
39	-0.11%	53%

In case you're wondering (sure you are), the best week of the year is actually the last week of the year – week 52. This one is up an incredible 72% of the time for an average gain of 0.84%. Santa Claus rally indeed!

The CAGR is 1.16% while the time spent in the market is about 22%. Thus, the week after options expiration day is lower than an average week.

Does it matter which month it is?

Yes, the month matters. This is the total profits of being invested in the different months:

No.	Net Profit	Profit Factor	Avg % Profit...	% of Winners
8	21,642.18	2.92	0.69	72.41
11	18,858.86	2.02	0.66	64.29
12	22,374.82	2.44	0.75	67.86
4	13,433.24	2.21	0.52	68.00
10	9,018.92	1.41	0.34	53.57
5	7,926.05	1.51	0.28	65.52
3	8,841.52	1.36	0.35	35.71
7	3,211.62	1.14	0.14	55.17
1	-6,404.75	0.73	-0.22	53.57
2	-16,540.65	0.43	-0.59	48.28
6	-15,483.23	0.40	-0.57	31.03
9	-20,630.38	0.37	-0.80	25.00

Sep opex is the worst unclench week

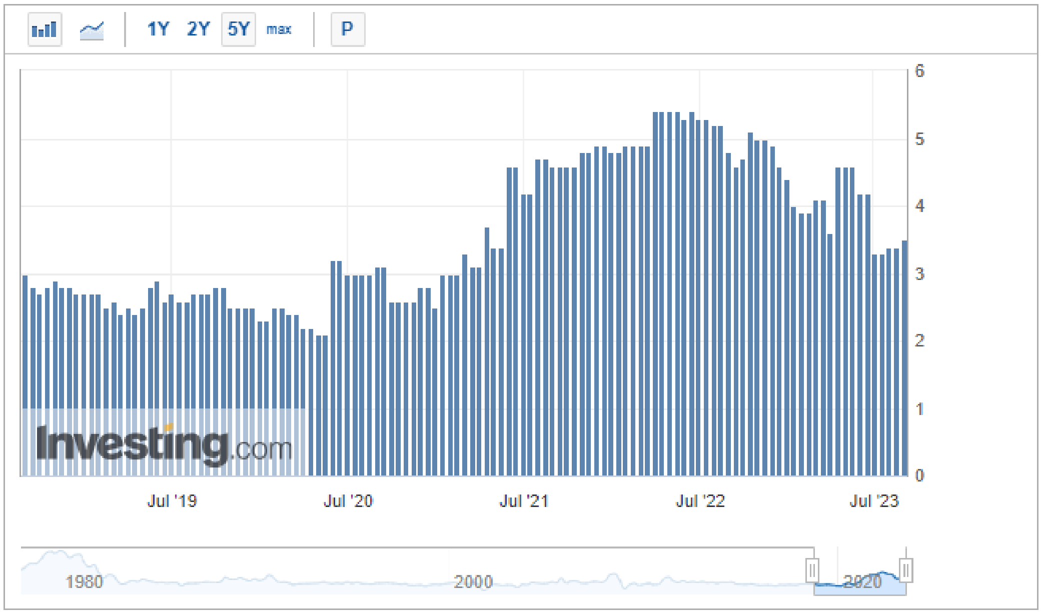
Source: https://www.quantifiedstrategies.com/trading-the-week-after-options-expiration-week/

Another thing to consider, while the markets parse through all the data and, lest we forget, an ECB rates meeting Thursday, is a sneaky data point on inflation. Now, the markets are pretty darn sanguine about CPI tomorrow, event vol has been smashed already, partly because it seems folks think that not only is the tick up in the headline number is fine, 'because it's gasoline and core will fall YOY', or something like that. From tier1apha's note yesterday:

> The September CPI on Wednesday is getting a bit of love, but it seems broadly accepted that we will see a bounce in headline (due to oil prices) and a retreat in core (due to shelter) with the Fed far more focused on the second. A positive resolution of this event is likely to take risk markets (and bonds) higher.

You see, expectations are basically, no biggie, it's just oil and the Fed is pausing anyways right. Well, here's something you probably didn't see last month, it being the Jackson Hole sideshow day and all:

U.S. Michigan Inflation Expectations



Release Date	Time	Actual	Forecast	Previous
Sep 29, 2023 (Sep)	10:00			3.3%
Sep 15, 2023 (Sep)	10:00 P			3.5%
Aug 25, 2023 (Aug)	10:00	3.5%	3.3%	3.4%
Aug 11, 2023 (Aug)	10:00 P	3.3%	3.8%	3.4%
Jul 28, 2023 (Jul)	10:00	3.4%	3.4%	3.3%
Jul 14, 2023 (Jul)	10:00 P	3.4%	3.3%	3.3%

Show more

Sizeable jump in consumer inflation expectations. And what causes that to rise? Yep, you guessed it, gasoline prices. (http://websites.umich.edu/~xqzhou/kz5.pdf) And you've heard Jay say several times, inflation psychology, that people think it could be lasting is the real battle.

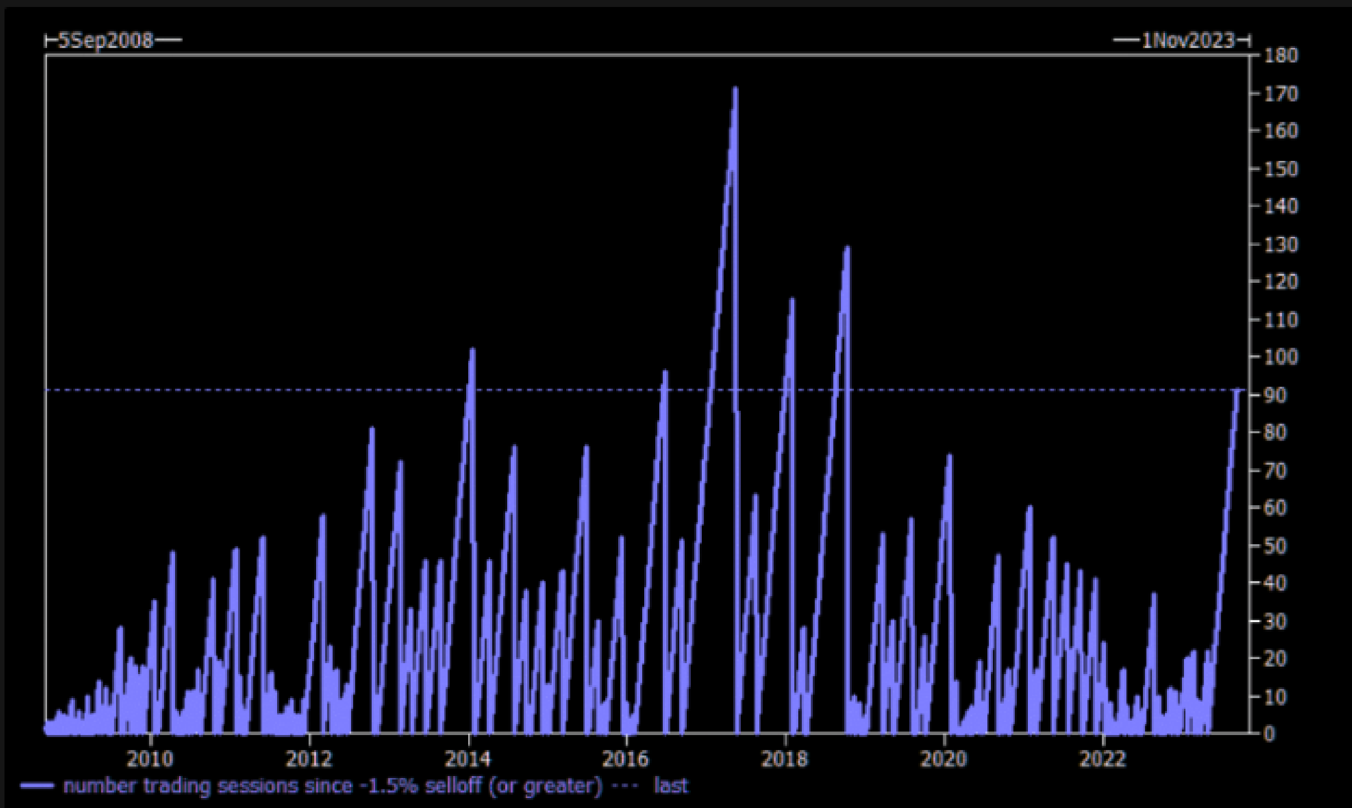
So, blowing off gasoline because it's non-core, well, it's pretty damn core to peoples' wallets, I mean, let's not retrofit real inflation to inflation hopes, that's cognitive dissonance looking to be resolved against real-world information.

And here is how the market reacted last month, before it started its typical end of month rally pattern:

But, lastly, have we really seen any legitimate non-intraday vol? Folks are smashing/offering it every down day, even when it doesn't work. And here is why they are so bold, this put-yielding Pavlovian army of premium ATM thieves, they just haven't been burned in ages:

Remember 1.5% sell-offs...?

91 is the number of trading sessions since at least a 1.5% sell off session in SPX. This length of time without a 1 day equity shock is rare ... has happened ~five times in the last 15 years.



GS trading desk

Volatility Trades:

QQQ Fed meeting put calendar spread

Sell $372 Sep 20th put

Buy $373 Sep 22nd put

Net debit: .42 (filled)

Jay comes on at 2:30pm, and vol will be sliding into the back leg as we get closer, because the release is so late in the trading day. Target, .70.

TSLA quarterly deliveries put diagonal spread:

Sell Sep 29th 262.5 put

Buy Oct 6th 260 put

Net debit: 1.90-.95

Optimism is high for deliveries in China, and as you can see above, for the TSLA Dojo to be the greatest A.I. dojo ever. Still, I expect some implied vol to slide into the Oct 6th deliveries release put leg, with folks so jazzed up, there is downside risk and that should be reflected in the spread as we get nearer. Target, $4.

ABNB SPX inclusion put diagonal spread

Sell Sep 22nd 142 put

Buy Sep 29th 141 put

Net debit: .30-.33

ABNB is going into the S&P 500, so the indexers, ETFs et al need to get some, and so the call crowd and the gap up traders and all the usual scoundrels are riding this higher into the Sep 18th inclusion. Some of this should come out as we get closer or after the event, and vol should increase. Target, .50.

VOLATILITY ANALYTICS NEWSLETTER – OCTOBER 4TH

HOLIDAY/END OF MONTH GAMES OVER AND VOL PREDICTABLY IS BACK – TRADE FOR FED DAY

VOLATILITY SUMMARY

Aug 30th note:

As vol declines into the end of the month and into the Labor Day holiday, it is once again offering the opportunity to get long volatility for very low prices. Looking at the implied volatility of the VIX, it has dropped to levels from March!

So, while the market sleeps again on the numerous/various economic risks that are about to come into play the next two months, we will start taking advantage of the low vol pricing again.

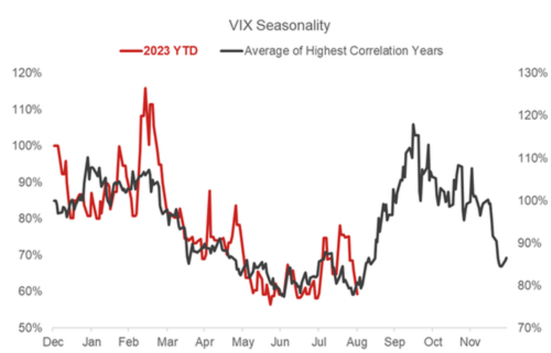
Well, that didn't take long. Holidays are often great times to get long volatility; it generally gets overly smashed to the point where the lack of premium opens up a trading range. Like a quasi-unclench perhaps.

And Charlie the celebrity quant decided to weigh in yesterday on how this vol situation was setting up for a potential vol squeeze:

Indeed, as McElligott warns there are **three strong reasons to fear a vol squeeze**:

*1) this **"low absolute level of Vol"** (VIX on Friday under 14 on the lows, which is the 7th lowest print on the first trading day of September since 1990)...*

*...and 2) into **seasonality which tends to show VIX grinding higher into mid-October,**...*



*...we have to again watch the 3) **VIX Dealer "Short Calls" dynamic** on any potential catalyst for a Vol squeeze...*

Source: https://www.zerohedge.com/markets/nomura-warns-watch-vol-squeeze-event-risk-cluster-looms

Now with ISM services for August coming in quite nicely thus markets disappointed with good economic news (feels like the Fed has permanently warped several markets' natural functionality) vol is now opening up with a host of events next week:

-CPI (base effects gone and should tick higher) 9/13

-PPI 9/14

-Retail Sales (retail companies' earnings were just a disaster with poor guidance) 9/14

-Larger Treasury auctions (*10-yr on Sep 12th the day before CPI*)

-ECB Meeting 9/14

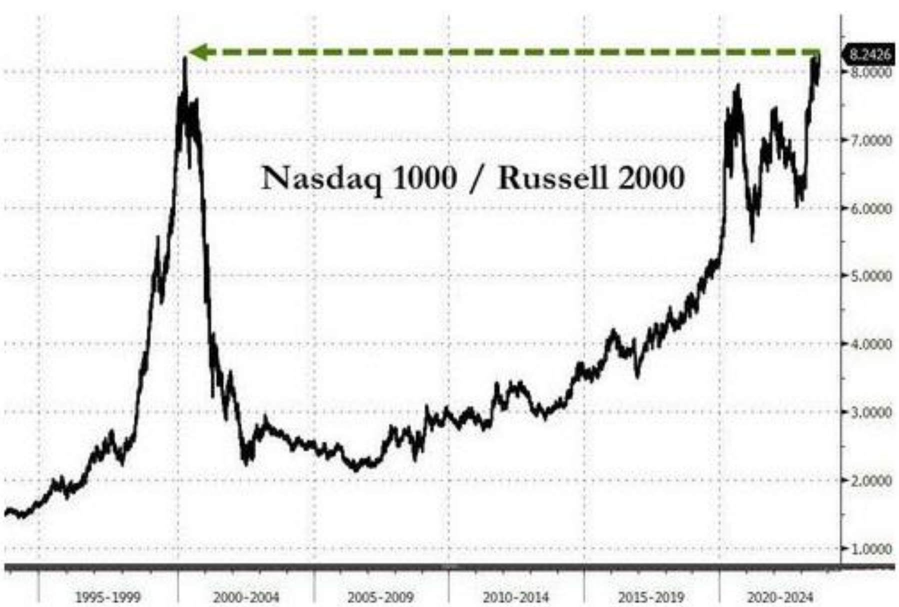
-Fed Meeting 9/20

What's interesting/comical about this level in SPX is that we have basically returned to when everyone rolled out their quarterly trades at June opex:

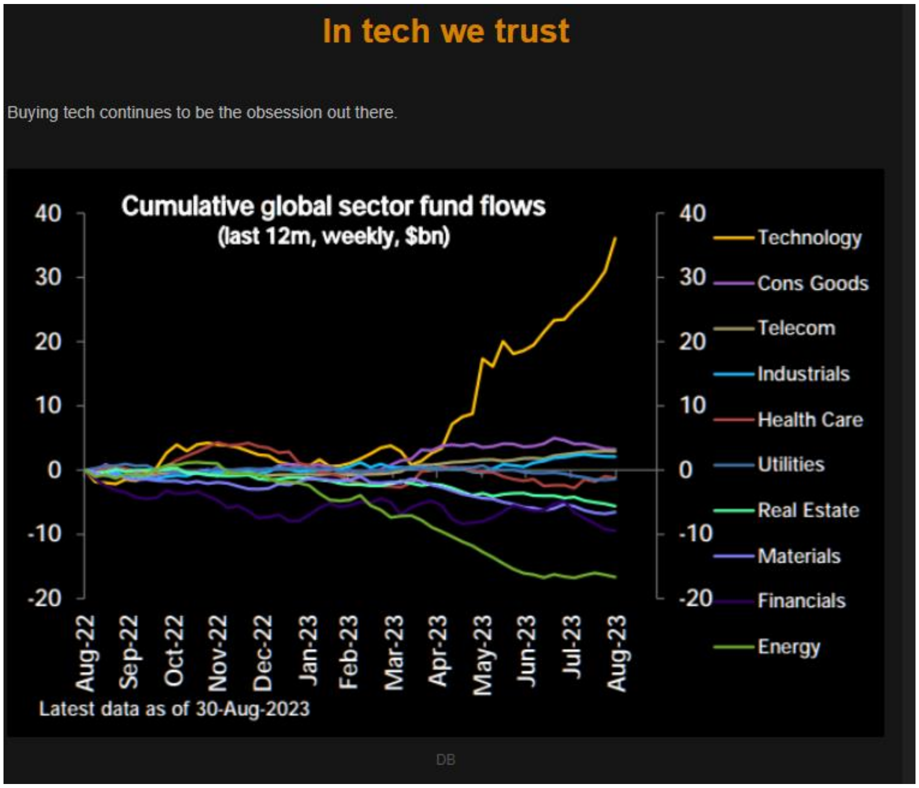
Hanging around this area ruins the sport of watching the giant JPM collar lose money, their levels not not really in play for end of this quarter:

Yesterday's divergences were comical, to the point that giga tech versus small caps was borderline absurd:

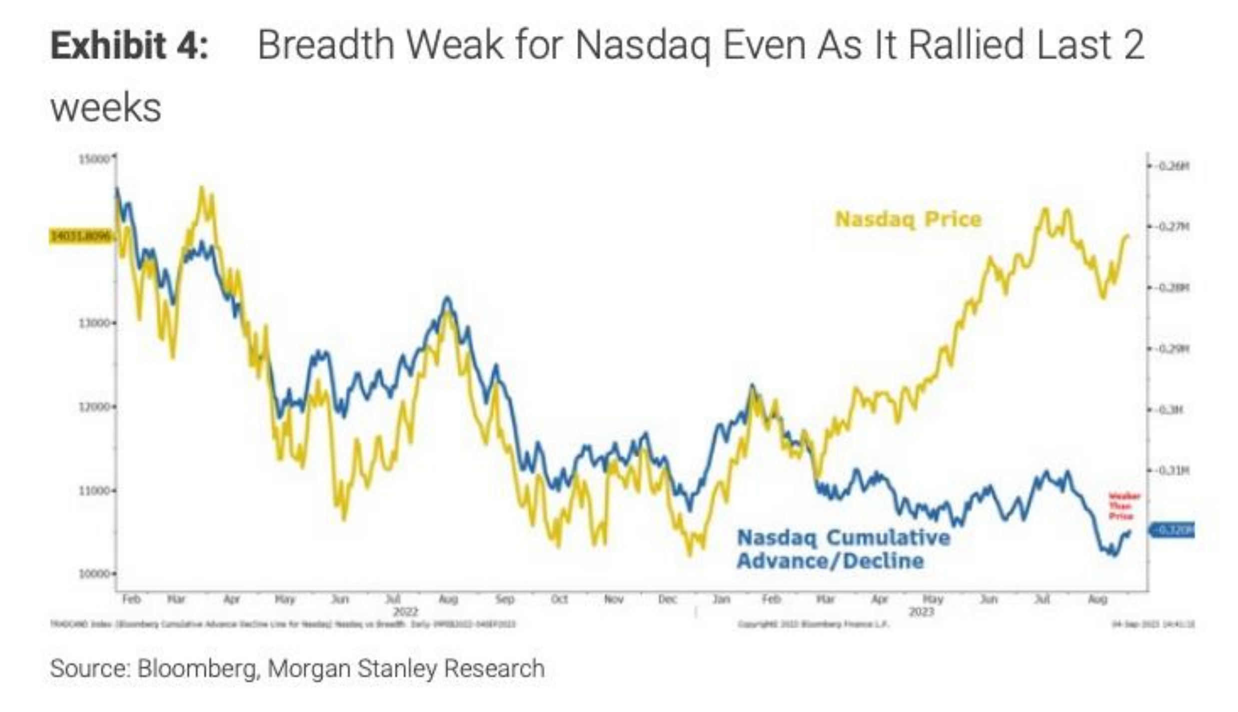
This was the Nasdaq's second best performance relative to the Russell 2000 since Nov 2021, breaking out to a new cycle high. The last time Nasdaq/Russell 2000 traded here was March 2000 - the very peak of the dotcom bubble...



You get the feeling that after witnessing the endless June/July ramp, you are going to have to pry their beloved giga tech from them with a crowbar before they report in October. And flows into the space show how full the clown car is getting; inflows into tech last week were the largest since May:



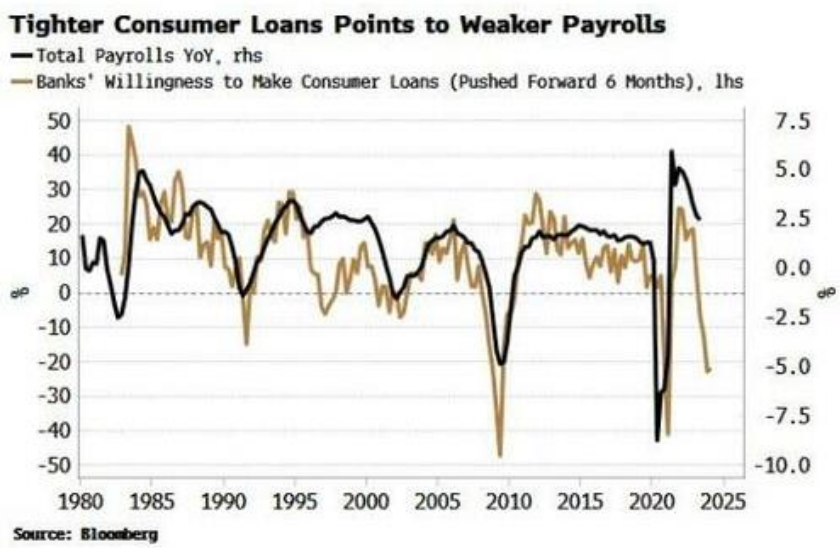
And in this chart, you can see how it's really just the top names doing all the work as their P/Es show absolutely no conscience, AI'd to oblivion:



But waiting for breadth to matter or a bubble to burst, well, feels like sitting at the RMV; the number just isn't going to come up anytime soon.

Meanwhile, still plenty of charts around that don't seem to be feeling current GDP/ISM services/soft landing scenarios:

For instance, **the sharp drop in banks' willingness to extend consumer credit is a building headwind in the coming months.**



If payrolls growth continues to decay at the rate it has over the last six months, we would get the first negative monthly change in December. However, it could come quicker if the decay rate increases (as the chart above suggests could happen).

In the meantime, when IV gets stupidly oversold, you can simply grab insanely cheap puts in giga herd stocks like AAPL. I was going to put a bearish long put spread trade of some sort in today's note for after the Iphone event. And then, it has a -3% day and I missed the trade. Look at how stupidly low priced the puts for this week were:

Oh well, I'm sure there will be more opportunities like this as folks continue to offer vol and the opex cycles/0DTE/systematic funds continue to do their thing.

Volatility Trades:

SPX Fed day put calendar spread

Sell $4450 Sep 20th put

Buy $4450 Sep 22nd put

Net debit: $2.80-3 (2.80 filled)

We did our SPX Fed put calendar trade a couple weeks ago, Sep 18-22s on a cost of $6, those are trading for $8.50 or so, and this is another classic Fed trade I like to do, selling the meeting day vol and owning the reaction days. The premise is pretty simple, by the time Jay takes the stage, it's 2:30pm, and the vol will slide into the back leg as we get closer to the event. Target $6.

ANOTHER CRASH UP HIGHLIGHTS TYPICAL END OF MONTH PRICE ACTION – VOL OF VOL IN THE BASEMENT – TRADES FOR SPY EX-DIVIDEND/QQQ FOR CPI/ECB

VOLATILITY SUMMARY

They say you can't time the markets. Those are the lazy or willfully ignorant managers; I expected this price action/end of month ramp and highlighted the tendency here a couple notes ago:

And, as the end of the month comes along with a holiday shortly after, vol burn/vanna/charm, whatever term you like is upside market fuel, and Charlie the celebrity quant makes that plainly clear, the last sentence the key:

Crucially, additional downside probably needs to materialize soon, otherwise the pullback window mentioned above will close — and reopening it will require a macro catalyst.

"Anytime you get UX1 moving up five vols in the course of five days, vol needs to be fed with movement in order to be sustained," McElligott reminded market participants. Otherwise, it'll "mean-revert under the weight of its own expectations."

BBG

The simple figure above illustrates the point.

Friday's high print for VIX futures was 19.6. The implied daily change was 1.2%, but when the dust settled, stocks were unchanged. That, Charlie remarked, "is an absolutely brutal realized vol bleeder."

https://heisenbergreport.com/2023/08/21/window-for-stock-pullback-may-close-without-more-fireworks/

Add to this the fact that the 10-yr futures options expire with a pointless exercise in Jackson Hole on Friday and the 0DTE crowd could be right back to their call sweep playbook into month end.

As usual, the opex cycle and options are the market's bosses when liquidity is low and real buyers/sellers are on vacation.

Now, it will be curious to see if we get the 3:30pm last day of the month, end of day gamma ramp that was egregious the last day of July. I highlighted that at the time:

Have you ever made 1000% in 10 minutes? Well, you could have by simply buying an at the money call at 3:50pm:

Source: Aug 2nd newsletter

VOLATILITY ANALYTICS NEWSLETTER – OCTOBER 4TH

As vol declines into the end of the month and into the Labor Day holiday, it is once again offering the opportunity to get long volatility for very low prices. Looking at the implied volatility of the VIX, it has *dropped to levels from March!*

That is pretty comical, considering we just got higher than expected inflation in Spain and Germany today, and the market events in this window include:

-CPI (base effects gone and should tick higher) 9/13

-PPI 9/14

-Retail Sales (retail companies' earnings were just a disaster with poor guidance) 9/14

-Larger Treasury auctions (*10-yr on Sep 12th the day before CPI*)

-ECB Meeting 9/14

-Fed Meeting 9/20

Let's be realistic, the news yesterday was terrible regarding job openings and consumer confidence, and the market relief rallied on rates coming in, which (at the risk of repeating myself for the third time in this note alone) had more to do with the 10-yr futures expiration than the economy or treasury supply/demand.

In fact, Bloomberg today highlighted a large seasonal arbitrage trade around 10-yr futures that occurs at the end of these cycles and had a lot of hedge funds shorting 10-yr futures which drove up yields:

Surge in Hedge-Fund Treasury Shorts Hints at Rise of Basis Trade

- Short positions in futures rose as recent bond selloff crested
- Indicates increasing leverage that raises volatility risks

By Edward Bolingbroke
August 29, 2023 at 4:46 PM EDT

Listen 3:35

A surge in short sales of US Treasury futures suggests hedge funds are expanding basis trades, a popular tactic that may be injecting leverage into a bond market whipsawed in the wake of this month's selloff.

The revival of the trade – which exploits price differences between futures and underlying bonds – was likely behind the positioning by hedge funds up to Aug. 22, when the latest Commodity Futures Trading Commission data shows their short positions swelled to over 6 million 10-year-note futures equivalents. Asset managers are net long to a similar degree.

The positioning data indicates an inrush into basis trades just as the most recent Treasury selloff was cresting, pushing 10-year yields to the highest since the before 2008 credit crisis. The proliferation of such leveraged strategies could exacerbate the market's volatility, as happened in previous cases when they were rapidly unwound.

https://www.bloomberg.com/news/articles/2023-08-29/surge-in-hedge-fund-treasury-shorts-hints-at-rise-of-basis-trade?sref=1zxv5xkq

So, while the market sleeps again on the numerous/various economic risks that are about to come into play the next two months, we will start taking advantage of the low vol pricing again.

Volatility Trades:

SPY Ex-Dividend put calendar spread

Sell Sep 12th $445 SPY put

Buy Sep 15th SPY $445 put

Net debit: .86-90 (filled)

The beauty of this trade is that the back leg holds SPY ex-dividend, and that includes 1.60 of pricing (the SPY dividend, approximately) that won't leave the back leg easily, unless we ramp hard back to the highs from here. I set these at both 445 and 450 because if it goes ITM, that dividend helps insulate the trade unlike a typical in-the-month calendar spread. It has the ex-dividend vol in the back leg. You can see it in prices from June's equivalent spreads, with the vix at 14 or so then, so the implied vols on this equivalent trade were roughly the same:

Strikes: 20

June 12/16 put calendars quoted on 6/12 3pm

	PUTS								
Strike	Bid X	Ask X	Net Chng	Delta	%Change	Impl Vol	Volume	Open.Int	Last X
424 / 424	.74	.76	-.38	-.16	-33.63%	17.73%	5,763	14,022	.75
425 / 425	.89	.91	-.44	-.19	-32.84%	16.71%	14,699	26,028	.90
426 / 426	1.07	1.09	-.51	-.22	-32.48%	15.68%	2,869	15,431	1.06
427 / 427	1.28	1.30	-.53	-.25	-28.96%	14.65%	3,029	19,176	1.30
428 / 428	1.54	1.56	-.50	-.29	-24.27%	13.64%	4,772	26,293	1.56
429 / 429	1.84	1.86	-.41	-.33	-18.06%	12.63%	4,383	16,593	1.86
430 / 430	2.19	2.21	-.18	-.38	-7.53%	11.61%	21,647	18,951	2.21
431 / 431	2.58	2.60	.21	-.40	+8.79%	11.03%	6,778	10,072	2.60
432 / 432	3.02	3.04	.62	-.40	+25.62%	10.20%	4,244	5,207	3.04
433 / 433	3.31	3.35	1.13	-.11	+51.13%	10.00%	1,345	1,748	3.34
434 / 434	3.16	3.26	1.01	.25	+45.50%	10.34%	426	564	3.23
435 / 435	2.86	3.00	.97	.37	+50.52%	--	522	140	2.89
436 / 436	2.49	2.69	.74	.32	+41.81%	--	155	51	2.51
437 / 437	2.21	2.48	.58	.28	+30.21%	--	12	1	2.50
438 / 438	1.95	2.29	1.74	.25	+122.54%	--	14	7	3.16
439 / 439	1.74	2.10	1.44	.21	+175.61%	--	1	2	2.26
440 / 440	1.59	1.91	.31	.18	+25.00%	--	4	19	1.55
441 / 441	1.46	1.82	.62	.16	+238.46%	--	0	7	.88
442 / 442	1.38	1.73	1.60	.14	+26.02%	--	0	1	7.75
443 / 443	1.31	1.66	1.85	.12	+142.31%	--	6	24	3.15

SPY was 433, and 50-100 SPX points (5-10 SPY points) ITM and the trade was still quite profitable. Target - $2+.

QQQ CPI/ECB/Retail Sales/10-yr auction put diagonal spread

Sell Sep 12th $365 QQQ put

Buy Sep 15th $364 QQQ put

Net debit: .36-.38 (.37 filled)

A bevy of risk events in the back leg, for .1% of the underlying, it's incredibly cheap. Target .75.

If we get another comical end of month gamma ramp, I'll do a quick note with an SPX put butterfly spread for September opex, since it will be even cheaper than today.