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FOMO / FOCUS: Chasing Back Into Assets on Perception of "End of Tightening"—But "Long Gamma" Opportunities Exist in 2H23 Across Rates and Equities Vol on "Higher for Longer" Accident Risk

Charlie McElligott
Managing Director
Cross-Asset Strategy
Nomura Securities International, Inc.
Charlie.McElligott@Nomura.com
O: 212-667-2210

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The US Regional Banking Crisis Changed Everything

"The" inflection in this cycle was the banks crisis, where the market's interpretation was that it pulled-forward the "end of Fed tightening cycle"— while even too signaling resumption of "The Fed Put"— in a market underpositioned for an Asset rally, which instead, was painfully positioned for an Earnings Recession…but in a world of 6-7% Nominal GDP Growth

The market's "pivot" towards the "end of the Fed tightening" cycle began thanks to the regional banks crisis (taken from mid-March into start-May)

UST CASH CURVE STEEPENING BEGAN ONCE THE REGIONAL BANK PROFITABILITY CRISIS TOOK-OFF, AS IT'S VIEWED AS FINAL CATALYST TO END THE FED TIGHTENING CYCLE

Source: Nomura Vol, Bloomberg

<u>From 2022's "Return OF Capital" to 2023's "Return ON Capital"</u>

From the banks crisis forward, the market mentality shifted out of the prior "return OF capital" mode (QT = LONG CASH / SHORT ASSETS) to "return ON capital" (QE = LONG ASSETS / SHORT CASH / SHORT VOL) regime, in a complete shift of investor risk-appetite

The 1 month since the peak of the regional banks crisis ushered in a sudden market shift in risk appetite and willingness to "Short Vol" again

SPX Daily Options PnL Summary

Cumulative PnL

	10d	20d	60d	ytd
Selling Daily ATM Straddle	3.5%	5.2%	8.9%	8.8%
Selling Daily ATM Call	1.1%	0.9%	2.8%	1.5%
Selling Daily ATM Put	2.5%	4.3%	6.0%	7.3%
Selling Daily Strangle	1.7%	2.7%	5.7%	5.3%
Selling Daily 25d Call	0.4%	0.1%	1.8%	0.7%
Selling Daily 25d Put	1.3%	2.5%	4.0%	4.6%

Sharpe Ratio

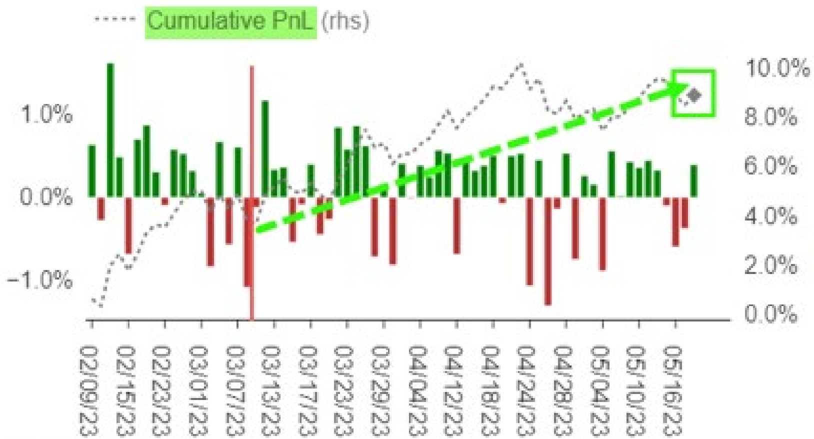
	10d	20d	60d	ytd
Selling Daily ATM Straddle	14.1	8.1	4.0	3.3
Selling Daily ATM Call	4.1	1.3	1.3	0.6
Selling Daily ATM Put	30.9	10.4	2.8	3.0
Selling Daily Strangle	11.0	6.4	4.0	3.1
Selling Daily 25d Call	2.5	0.4	1.6	0.5
Selling Daily 25d Put	64.2	23.7	3.7	3.8

APRIL 19TH MARKED THE PEAK OF THE "SHORT VOL" INSANITY, INCLUDING A 64 SHARPE RATIO OVER THE TRAILING 10D PERIOD FROM SELLING DAILY 25D PUTS

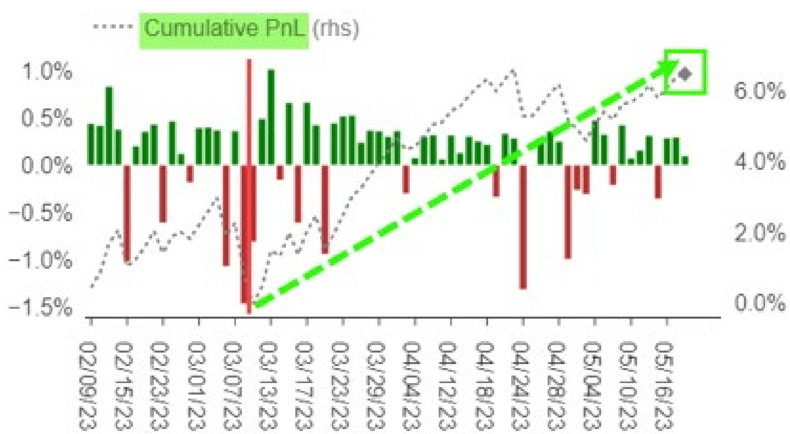
Source: Nomura Vol, Bloomberg

Short US Eq Index Vol Profitability Explodes Higher in the Two Months After the Regional Banks Crisis:

Selling SPX Daily ATM Straddle Profitability in 2023

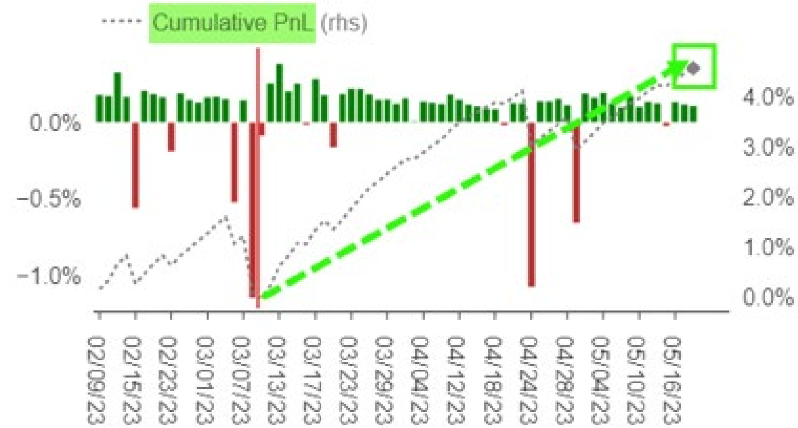


Selling SPX Daily ATM Put Profitability in 2023



Source: Nomura Vol

Selling SPX Daily 25d Put Profitability in 2023



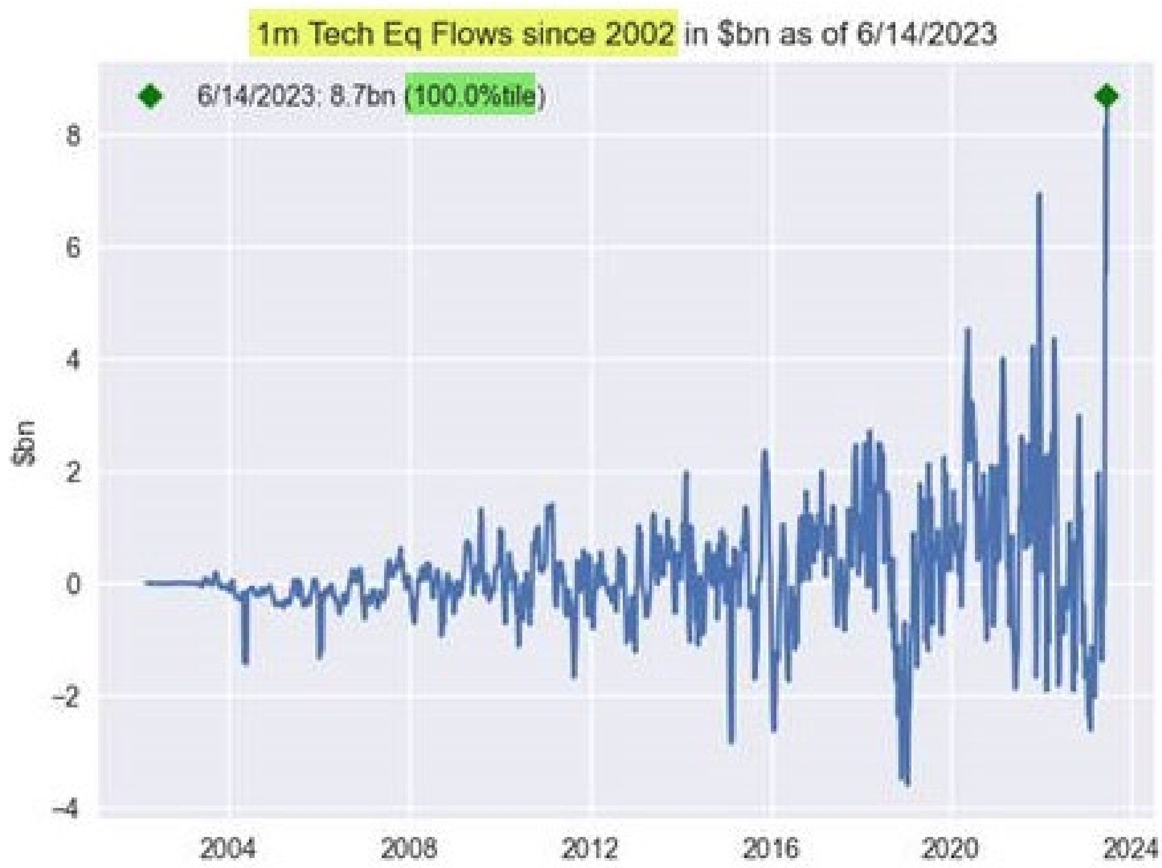
Source: Nomura Vol

Cash Now “Burning Holes in Pockets” per EPFR Fund Flow Data—Week of 6/15/23

- Global Money Markets -$37.9B 1w outflow, 6%ile
- Global Equities +$22.3B 1w inflow, 96%ile
- Global Bonds +$6.7B inflow, 86%ile; +$30.6B last 1m, 12 consecutive weeks of inflows
- DM Bonds +$6.5B inflow, 83%ile, +$32.2B last 1m, 24 consecutive weeks of inflows
- Global IG Credit +$3.1B 1w inflow, 76%Ile, +$17.1B last 1m, 11 consecutive weeks of inflows
- Tech Equities +$8.7B 1m inflow, 100%ile

Source: EPFR, Nomura Vol

1 Month Tech Equities Fund Flows — 100%ile Since 2002



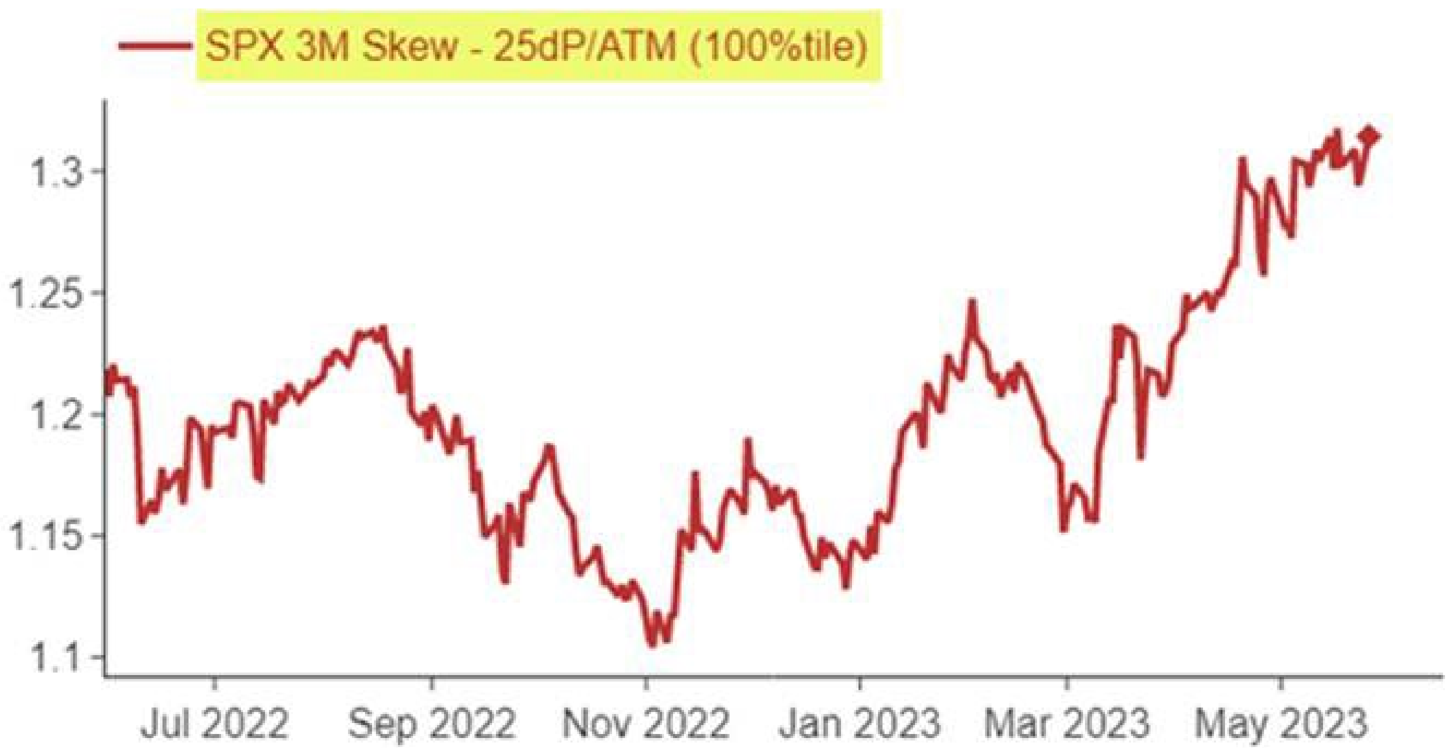
Source: EPFR, Nomura Vol

However, the perceived left-tail risks in the market at end Q1 into Q2—particularly the regional banks crisis as catalyst for accelerated credit / lending crunch into an already moderating economy off the back of lagged-and-variable tightening which has occurred since last year—then saw a new risk catalyst emerge, in the form of the debt-ceiling “x-date” default risk

These obvious “neon swans” then perversely created an extreme over-hedging into a “worst case scenario” which was over-stated, with low probability to realize

Source: EPFR, Nomura Vol

Mid May SPX 3m Skew at 100%ile



Source: Nomura Vol

But as “worst case scenario” failed to materialize and “left tails went right tails,” this created impulsive waves of hedges to be unwound, triggering an enormous shedding of risk-premia across assets from Duration / SPX Puts / VIX Calls / Gold etc which had been built into markets over the month of May…only to be violently unwound thereafter into June, propelling Stocks higher in particular, as Dealer “short futures” hedges were taken off

Source: EPFR, Nomura Vol

Mid May SPX Skew Ranks Change Versus Mid June:

SPX Skew Trends

MAY

Skew (25d)	Term	Value	5y %tile	6m Trend	6m %tile
	2w p/c	1.34	34%		94%
	1m p/c	1.50	52%		100%
	2m p/c	1.60	69%		100%
	3m p/c	1.60	66%		100%
	6m p/c	1.60	66%		100%

Put Skew (25d p/atm)	Term	Value	5y %tile	6m Trend	6m %tile
	2w p/atm	1.17	31%		94%
	1m p/atm	1.25	40%		98%
	2m p/atm	1.29	49%		96%
	3m p/atm	1.29	44%		96%
	6m p/atm	1.29	49%		96%

Call Skew (25d c/atm)	Term	Value	5y %tile	6m Trend	6m %tile
	2w c/atm	0.88	49%		6%
	1m c/atm	0.83	29%		0%
	2m c/atm	0.81	15%		0%
	3m c/atm	0.80	16%		0%
	6m c/atm	0.80	21%		0%

SPX Skew Trends

JUNE

Skew (25d)	Term	Value	5y %tile	6m Trend	6m %tile
	2w p/c	1.09	1%		2%
	1m p/c	1.24	7%		25%
	2m p/c	1.36	12%		38%
	3m p/c	1.43	17%		52%
	6m p/c	1.50	24%		65%

Put Skew (25d p/atm)	Term	Value	5y %tile	6m Trend	6m %tile
	2w p/atm	1.07	4%		13%
	1m p/atm	1.15	13%		39%
	2m p/atm	1.22	22%		60%
	3m p/atm	1.26	29%		68%
	6m p/atm	1.29	49%		74%

Call Skew (25d c/atm)	Term	Value	5y %tile	6m Trend	6m %tile
	2w c/atm	0.98	100%		99%
	1m c/atm	0.93	97%		92%
	2m c/atm	0.90	96%		88%
	3m c/atm	0.88	95%		92%
	6m c/atm	0.86	89%		80%

Source: Nomura Vol

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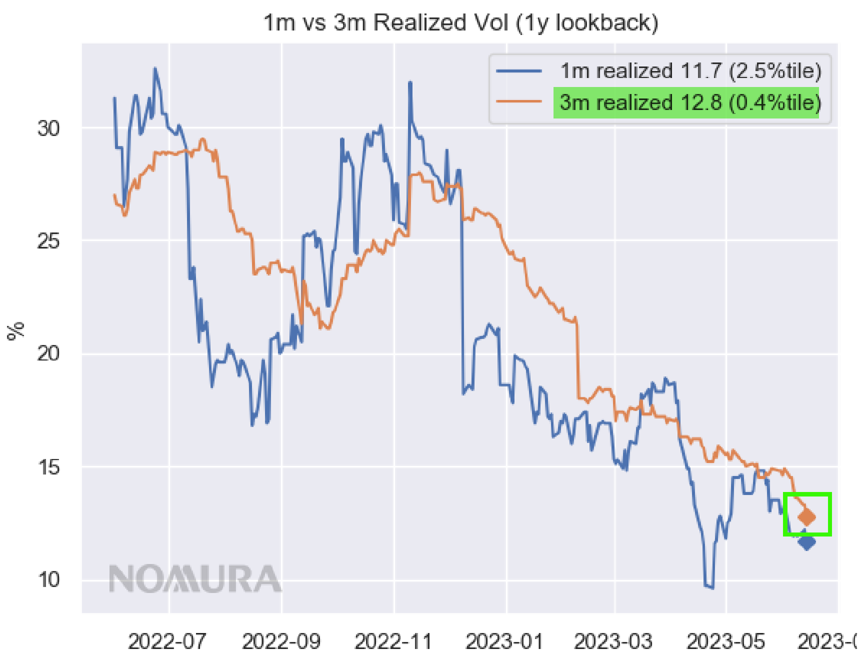
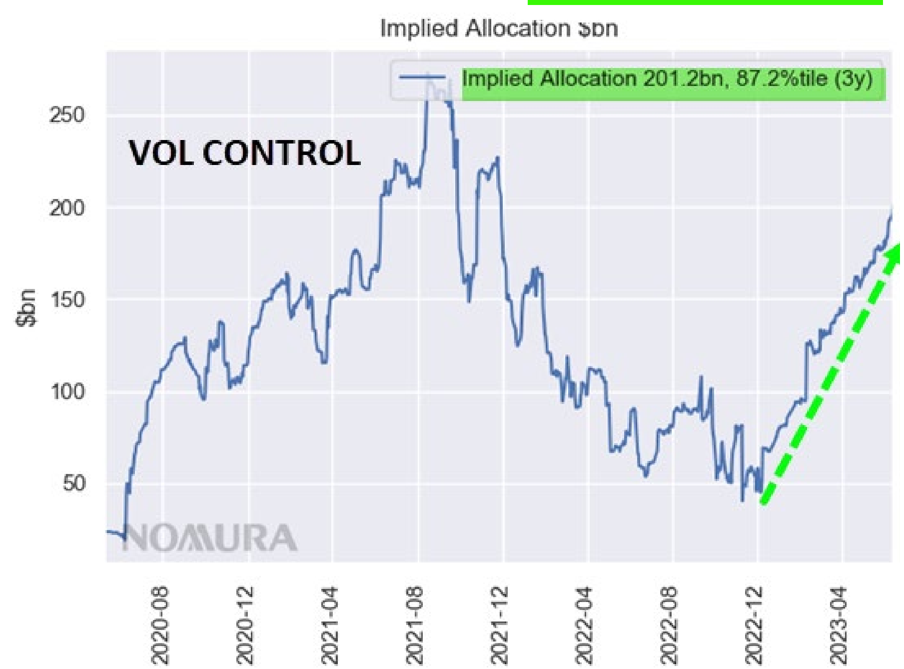
Virtuous feedback loop: realized Volatility "bleeds out" = Systematic releveraging / reallocation mechanically occurs back into Equities

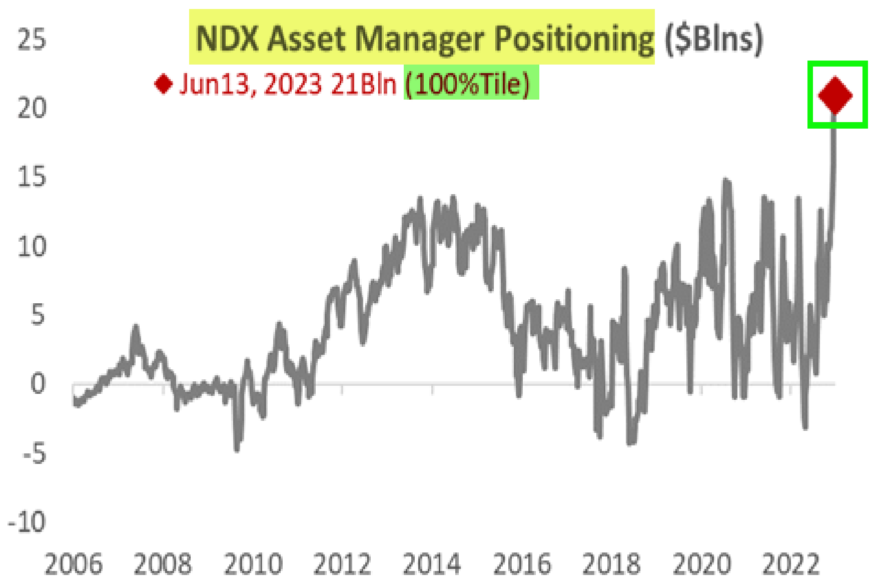


	in $bn	alloc %	%tile
Changes			
1d	2.7	1.1	80.8
2d	8.8	3.5	88.3
1w	11.1	4.5	78.6
2w	13.8	5.6	69.4
1m	25.9	10.4	66.6
3m	62.2	24.9	77.8
6m	147.5	59	95.4



Source: Nomura Vol

While Asset Manager US Equities Futures Positioning Goes “Off the Scales”—Just Another Expression of “Volatility as the Exposure Toggle”



Source: CFTC / TFF, Nomura Vol

The “Spot Up, Vol Up, Crash Up” was initially concentrated Secular Growth / Nasdaq / AI names in the wake on NVDA Earnings…

Source: Bloomberg, Nomura Vol

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<u>But beginning in June, has now shifted into a “phase two”: traders are grabbing into “the stuff that’s been left behind,” with investors panic lunging for Upside in standard “performance chasing” mode via previously “left-for-dead” stuff:</u>

Economically-Sensitives / Cyclical Value
Small Caps
Highly Leveraged Balance-Sheet
Unprofitable Tech
Retail Favorites / Meme Stocks
High Option Volume Names
Formerly “toxic” stuff like Regional Banks, Energy and even Utilities

June MTD Reversal Flows: "From Worst to First" Leadership, While Momentum, Crowding and AI / MegaCap Tech Act as "Source of Funds"

W 52: gross-down / reversal

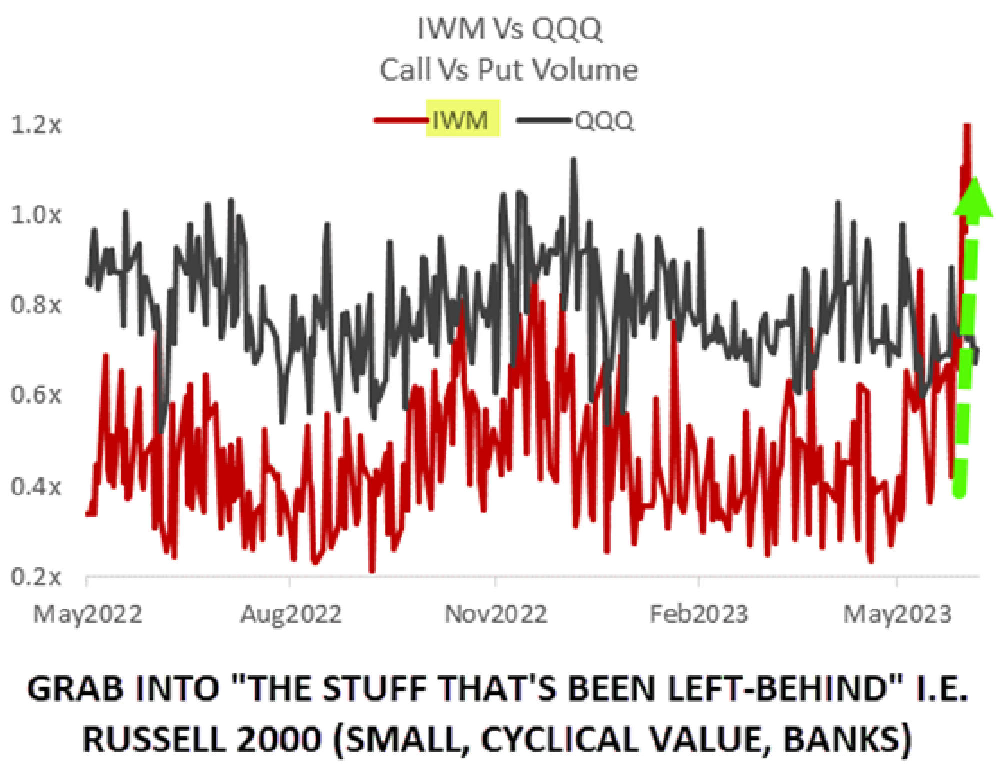
Ticker	%1D	%2D	Chg 3D Pct	%5D	%MTD ↓	Chg QTD %
Non-Profitable Tech	--	+2.49%	+2.23%	+12.10%	+20.57	+38.80%
High Short Interest	--	-1.48%	+.35%	+2.16%	+15.51	+17.96%
Regional Banks Hedge	--	+1.98%	-.76%	+1.09%	+14.52	-1.78%
Wolfe Short "Hit List"	--	+.18%	-.81%	+3.29%	+13.58	+1.03%
High Risk / Beta	--	+1.18%	-.05%	+3.73%	+12.20	+10.52%
Unprofitable Tech	--	-.90%	+2.79%	+6.01%	+11.82	+17.36%
1Y Momentum Shorts	--	+1.95%	+.15%	+3.77%	+10.99	+5.10%
Most Shorted	--	-.06%	+3.63%	+3.15%	+10.24	+11.38%
Highest Short Interest	--	+1.07%	+.08%	+3.24%	+10.19	+5.67%
Retail / Squeeze Alert	--	+.86%	+.70%	+3.60%	+10.07	+16.32%
ARKK US	--	+.56%	+2.91%	+4.36%	+10.00	+10.41%
Low Profitability R2K	--	-.55%	+2.66%	+3.10%	+9.61%	+10.72%
NYFANG	--	+2.54%	+3.46%	+6.32%	+9.49%	+26.79%
Passively Held Short	--	+.56%	+2.14%	+3.21%	+8.67%	+8.97%
E&P Hedge	--	+2.39%	+.87%	+.07%	+8.38%	-2.26%
Energy Hedge	--	+1.74%	+.64%	+.33%	+7.91%	-1.26%
Recent IPOs	--	+1.01%	-.58%	+3.31%	+7.87%	+11.31%
Cyclicals Basket	--	+1.10%	+.64%	+2.09%	+7.81%	+3.49%
Retail Favorites	--	+1.35%	+2.28%	+4.20%	+7.54%	+11.61%
High Options Volume Basket	--	+1.69%	+2.51%	+4.37%	+7.34%	+9.46%
Secular Growth	--	+1.27%	+1.81%	+4.63%	+7.14%	+13.81%
Crowded Longs	--	+1.28%	+.62%	+2.55%	+6.79%	+6.81%
HF Least Crowded	--	+.95%	+.02%	+.91%	+6.56%	+.26%
1Y Momentum Longs	--	+.69%	+.19%	+1.47%	+6.28%	+4.39%
High Realized Vol	--	-1.55%	+.45%	+1.31%	+6.07%	+11.49%
SPY US	--	+1.36%	+2.03%	+3.14%	+5.92%	+8.11%
VIP Shorts	--	+1.44%	+2.21%	+2.88%	+5.91%	+1.68%
SPX	--	+1.30%	+2.00%	+3.07%	+5.89%	+7.70%
10Y Yield Sensitive Factor	--	+.65%	-.62%	-1.66%	+5.81%	-5.68%
Momentum Longs	--	-.03%	+.80%	+1.69%	+5.73%	+3.82%

W 52: gross-down / reversal

Ticker	%1D	%2D	Chg 3D Pct	%5D	%MTD ↓	Chg QTD %
Low Vol	--	+1.39%	+1.73%	+2.24%	+3.47%	+1.62%
1M Reversal Factor	--	+.05%	-.45%	+1.05%	+2.38%	-.43%
GDP Nowcast Factor	--	+.65%	-.39%	-2.00%	+1.59%	-6.86%
Mutual Fund OW vs UW	--	-.07%	+.11%	+.34%	+.43%	+1.25%
WTI Crude Sensitive Factor	--	+.62%	--	-2.81%	+.25%	-7.43%
HF Crowding Factor	--	+.33%	+.60%	+1.62%	+.22%	+6.54%
Share Buyback Factor	--	-.32%	-1.02%	-1.47%	-.42%	-5.60%
AI long/short	--	+1.33%	+.88%	+2.65%	-2.02%	+22.91%
Nomura HF "Crowd L/Most S" M/N	--	+.21%	+.54%	-.67%	-3.09%	+1.08%
1Y Momentum Factor	--	-1.24%	+.05%	-2.22%	-4.24%	-.68%
HF VIP vs Most Shorted	--	+1.49%	-1.55%	+.12%	-4.27%	-1.39%
MegaCap Tech / Unprofitable Tech	--	+3.46%	+.64%	-.45%	-4.78%	+7.84%
High Beta Momentum	--	-.42%	-1.80%	-.95%	-5.10%	+3.50%
Quality	--	+.35%	-.81%	-1.19%	-5.86%	-7.73%

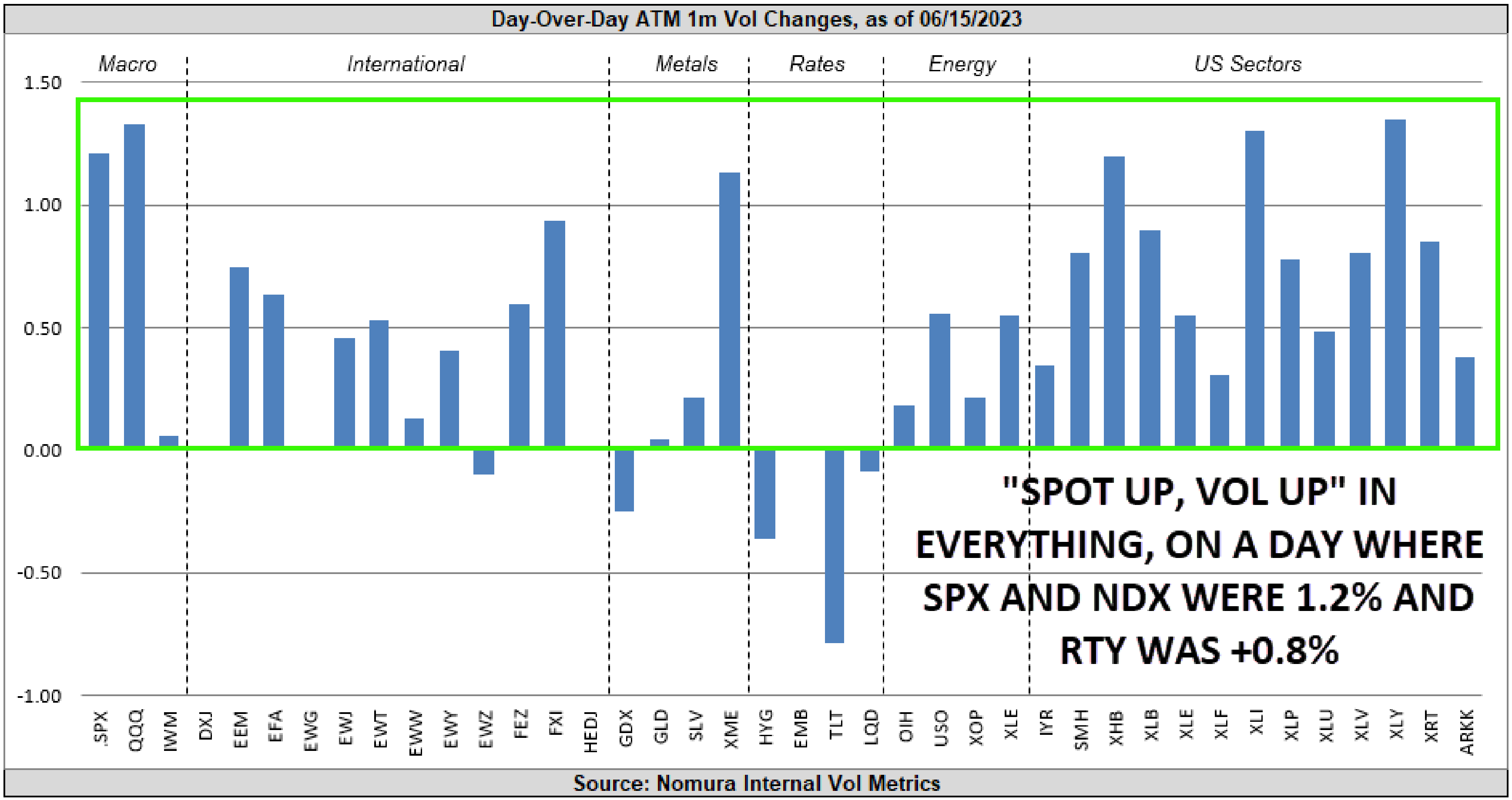
Source: Bloomberg, Nomura Vol

Previously un-loved Russell (Small Caps, Economically Sensitive, large Regional Banks / Energy weights) now seeing Call vs Put volume ratio now even more extreme that Mega Cap Tech QQQ's



Source: Bloomberg, Nomura Vol

Now "Spot Up, Vol Up" in EVERYTHING:



Source: Bloomberg, Nomura Vol

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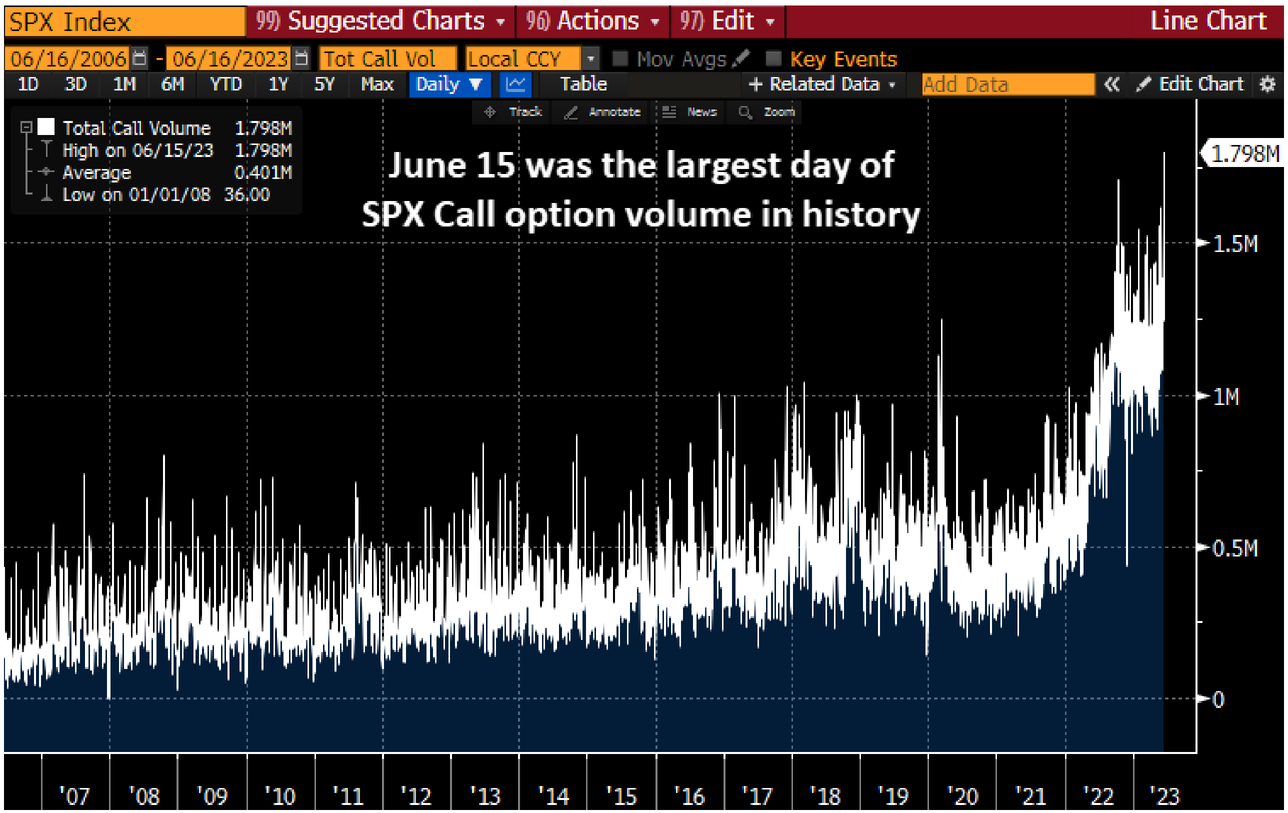
Exotic Products Contributing to this "Upside Vol Squeeze": Legacy "Double No Touch" Structured Products—along with various other Equities Notes—were getting Dealers "Short Vega" as we rallied, so they were having to buy Upside Vol into the Spot market breakout

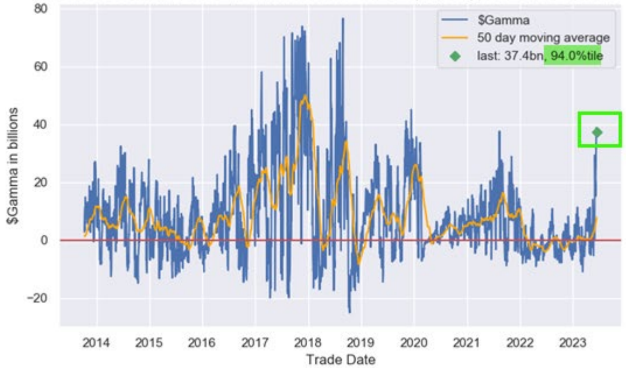
So besides just "chasing" due to underperformance / underexposure, this Dealer Exotic Desk "Short Vega" / Vanna issue was a big reason that June 15th was the largest day of SPX Call option volume in history:



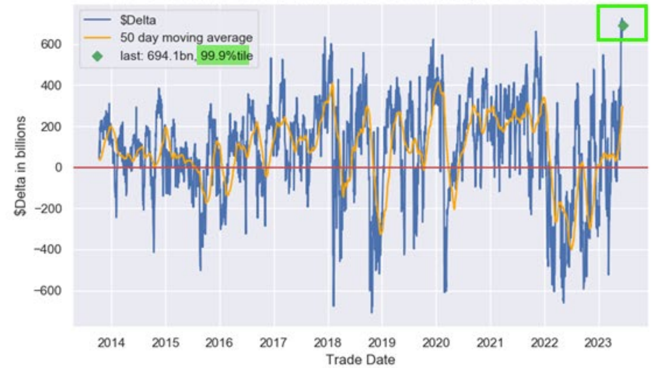
Source: Bloomberg, Nomura Vol

And as US Equities have impulsively rallied on said "Crash Up" grab into Calls, we have begun to ignite yet-another mechanical "forced" buy flows out of Overwriters, who are now being forced to cover previously OTM Calls they sold for income, but have now rallied to ITM—so they are forced to buy-back their "short strikes"

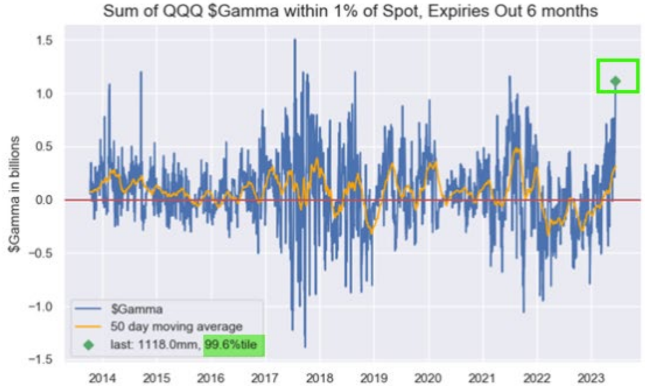
Sum of SPX and SPY $Gamma within 1% of Spot, Expiries Out 6 months



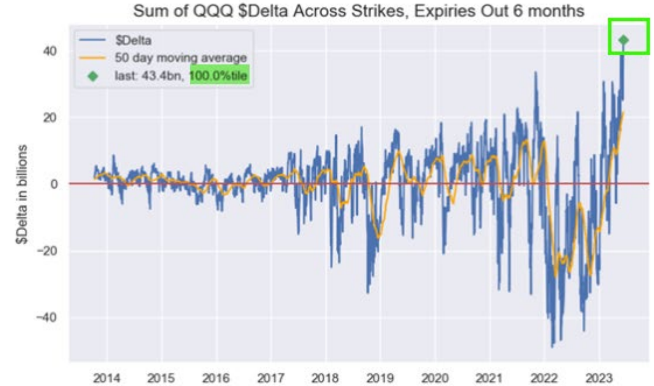
Sum of SPX and SPY $Delta Across Strikes, Expiries Out 6 months



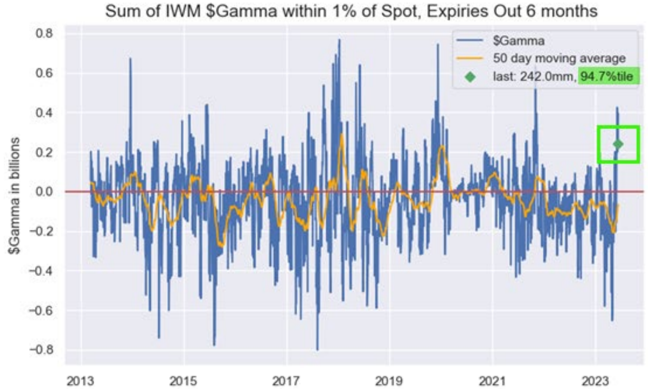
Sum of QQQ $Gamma within 1% of Spot, Expiries Out 6 months



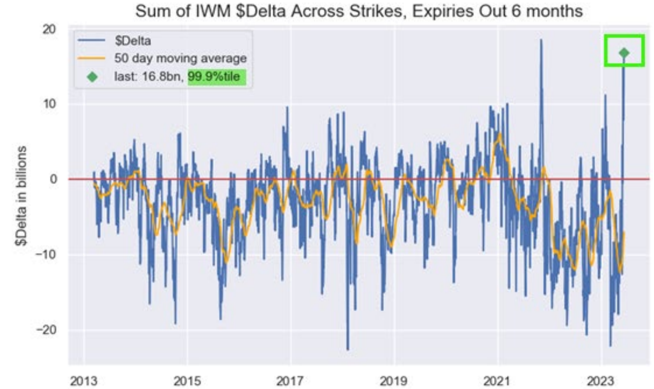
Sum of QQQ $Delta Across Strikes, Expiries Out 6 months



Sum of IWM $Gamma within 1% of Spot, Expiries Out 6 months

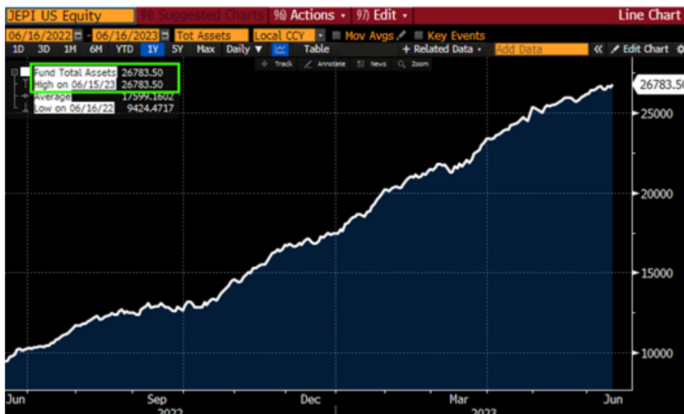


Sum of IWM $Delta Across Strikes, Expiries Out 6 months



Source: Bloomberg, Nomura Vol

Overwriter total AUM to new all-time record highs (after all, the Fed was telling you to "sell Calls" all last year!), proving that the shift from last year's Cash / "return of capital" is now pivoting to a current market focus on "capital appreciation"—but also too part of the "Crash-Up" problem, as the Calls they sold get rallied through and force-covered!



3 LARGE U.S. EQUITIES OVERWRITE FUNDS / ETF'S ALL MAKE NEW TOTAL AUM HIGHS JUNE 15, 2023--WHICH SPEAKS TO MARKET SHIFT FROM CASH / "RETURN OF CAPITAL" TO NEW, "RETURN ON CAPITAL" / CAPITAL APPRECIATION

Source: Bloomberg, Nomura Vol

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This "crash-up, grind-down (if at all!)" Equities dynamic has created a very challenged performance dynamic for systematic Call sellers versus Put sellers—where a strategy selling SPX daily ATM Calls (-4.5% YTD, -1.1 Sharpe) would have underperformed one selling daily ATM Puts (+11.7% YTD, +3.4 Sharpe) by a whopping -16.2% YTD

SPX Daily Options PnL Summary

Cumulative PnL

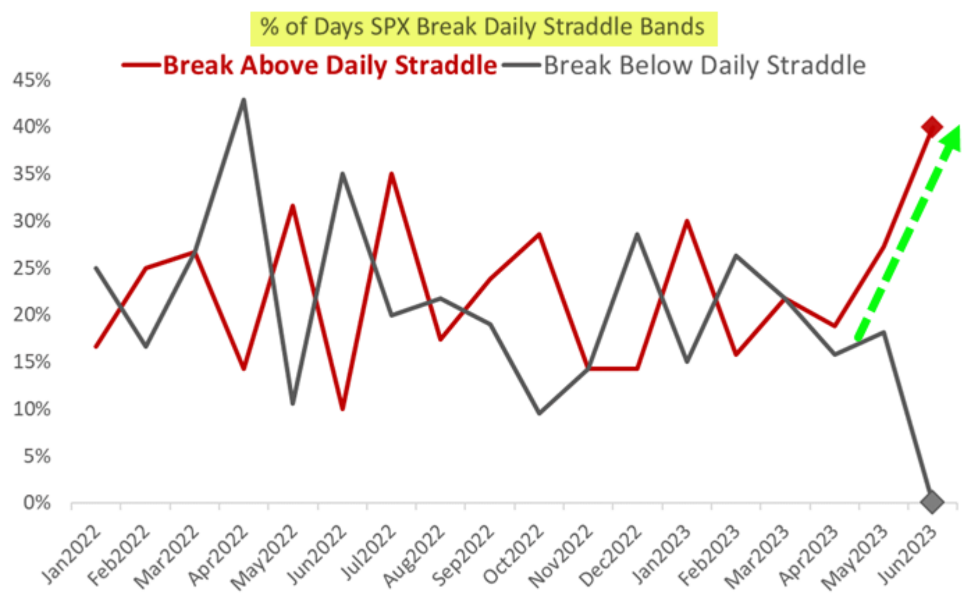
	1d	10d	20d	60d	ytd
Selling Daily ATM Straddle	-0.5%	0.0%	-1.7%	2.9%	7.2%
Selling Daily ATM Call	-0.9%	-2.3%	-4.3%	-4.2%	-4.5%
Selling Daily ATM Put	0.4%	2.4%	2.6%	7.0%	11.7%
Selling Daily Strangle	-0.5%	-0.4%	-1.3%	1.1%	4.4%
Selling Daily 25d Call	-0.6%	-1.4%	-2.8%	-3.4%	-3.1%
Selling Daily 25d Put	0.1%	1.0%	1.4%	4.6%	7.6%
Selling Daily Straddle, Long Strangle	-0.1%	0.4%	-0.3%	1.8%	2.8%

Sharpe Ratio

	10d	20d	60d	ytd
Selling Daily ATM Straddle	0.2	-3.0	1.5	1.8
Selling Daily ATM Call	-6.9	-6.4	-2.0	-1.1
Selling Daily ATM Put	20.1	6.3	4.7	3.4
Selling Daily Strangle	-1.7	-3.4	0.8	1.7
Selling Daily 25d Call	-6.2	-7.0	-2.7	-1.4
Selling Daily 25d Put	42.4	8.0	5.8	4.4
Selling Daily Straddle, Long Strangle	3.5	-1.4	2.2	1.5

Source: Nomura Vol

“Crash-Up” as 1) grab into Upside from both those who are underpositioned for risk-rally, AND 2) Dealers getting “Shorter (Upside) Vega” into the Spot-Up, Vol-Up” rally AND 3) those who are systematically short Calls (Overwriters) sees us blowing through the upper band of the daily implied straddle — in start contrast to the majority of 2023, which HAD BEEN a grinding range-bound, compressed Vol environment, e.g. previously perfect for “Short Straddles”—but no longer the case now, as we keep blowing-through Upside barriers



"CRASH-UP" AS GRAB INTO CALLS DRIVES "SPOT-UP, VOL-UP" AND WE BLOW THROUGH UPPER STRADDLE BAND

Source: Nomura Vol

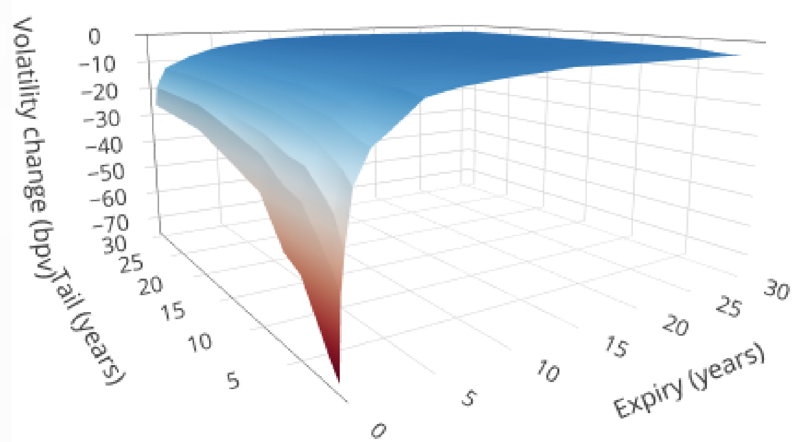
Post- the debt-ceiling deal and Fed "Pause," an absolute melt-down in USD Rate Vol, as the market has priced-out both Fed –cuts and –hikes in the past 3 weeks—de facto SELLING STRADDLES

Field	Currency	Start date	End date
Swaption: Implied volat:	USD	26-May-2023	16-Jun-2023

Refresh

USD volatility change (bpv) from 26-May-2023 to 16-Ju

	1y	2y	3y	5y	7y	10y	15y	20y	30y
1m	-74.3	-69.7	-64.3	-53.6	-50.6	-37.8	-32.7	-27.9	-25.7
3m	-52.6	-47.1	-43	-34.9	-33.2	-27.4	-23.6	-20.1	-19.2
6m	-42.3	-34.5	-31.4	-26	-25.2	-21.8	-19.5	-17.4	-16.7
1y	-27.6	-24.1	-22.4	-19.4	-17.8	-15.7	-14.2	-12.8	-12.3
18m	-23.4	-21.2	-19.7	-17	-15.8	-14	-12.8	-11.6	-11.2
2y	-19.1	-18.2	-17.2	-14.7	-13.8	-12.4	-11.4	-10.5	-10.2
3y	-15.9	-15.4	-14.2	-11.8	-11	-9.8	-9.1	-8.5	-8.2
5y	-8.9	-8.2	-7.7	-7.4	-7.2	-7	-6.3	-5.7	-5.4
7y	-7.1	-7.4	-6.9	-5.6	-5.6	-5.5	-4.9	-4.3	-4
10y	-5.7	-5.3	-4.9	-4.2	-4.1	-3.8	-3.3	-2.7	-2.6
15y	-4.2	-4.1	-3.6	-2.7	-2.6	-2.6	-2.3	-2	-2
20y	-4.4	-4	-3.6	-2.8	-2.7	-2.5	-2.3	-2.1	-2.3
30y	-4.1	-4.2	-3.9	-2.9	-2.9	-2.7	-2.7	-2.6	-2.6



Source: Nomura Vol, Nomura International Plc. Qstrat team

But the trillion dollar question is then

"How much lower can Vol go from here?"

(famous last words)…

especially when the economic "left tail" remains so fat

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“Fat Left Tail” risk looking underpriced relative to uncertainty--from Jia Cong Lim in USD Rate Vol (June 15):

The FOMC was somewhat of a surprise with the 2 additional hikes in 2023 in the dots but clearly this was not considered credible by the market and the muted rates reaction makes it tempting to sell vol.

What does the market actually think of the FOMC dots though?

We have about 10bps priced in for Dec 2023 which is 40bps away from the Fed, so if we believe that the base case is that the Fed will realise their dots, this means there is maybe a 10% chance of a catastrophic event by the end of the year which would justify a 400bps or so cut.

This seems like quite a lot of uncertainty for this vol to be down at 105bpv.

To buy the Straddle / buy Gamma now is again starting to feel like the right call as "stretched" as the market moves are getting (both UST / Rate selloff AND Equities rally feeling increasingly "unstable"), **as the longer that the Fed holds above 5% due to "still too high inflation and too tight labor markets," we perversely have even more certainty of an even harder landing….ESPECIALLY into tightening Bank lending / credit conditions and the diminishing liquidity profile with pervasive mention of Bill issuance and "crowding-out" risk, all while rest of world CB's re-escalate hikes *(RBA, BoC, BoE and ECB)***

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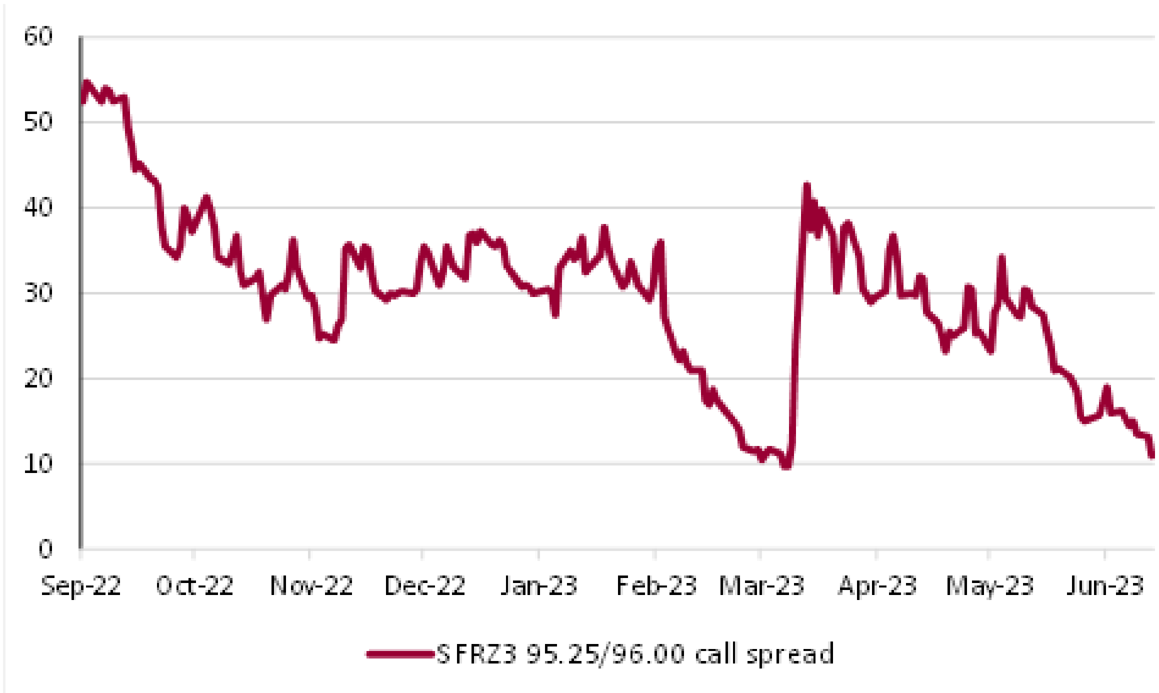
Just as we are seeing in US Equities Index / ETF Options on the “Crash-UP,” Call Skew remains rich in SOFR Options as well—so we agree that SOFR Call Spreads set up nicely, especially on the entry cost



Source: Bloomberg, Nomura

Source: Nomura Vol, Bloomberg

I am firmly in the camp that believes when we get that first “YIKES” NFP print or mega “base-effect” decline in CPI / Core PCE in the US, that Duration / Bonds will “go” and rally almost “without offer,” as the asymmetry grows towards BIGGER CUTS the longer policy holds higher and from such elevated levels off the zero bound

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Similar to these exact same points above on SOFR Call Spreads as attractive "higher for longer" left-tail trades, this is also why VIX Call Spreads look so attractive, with 2m, 3m and 6m VIX 25d / ATM Call Skew at 99%ile, 100%ile and 100%ile, respectively

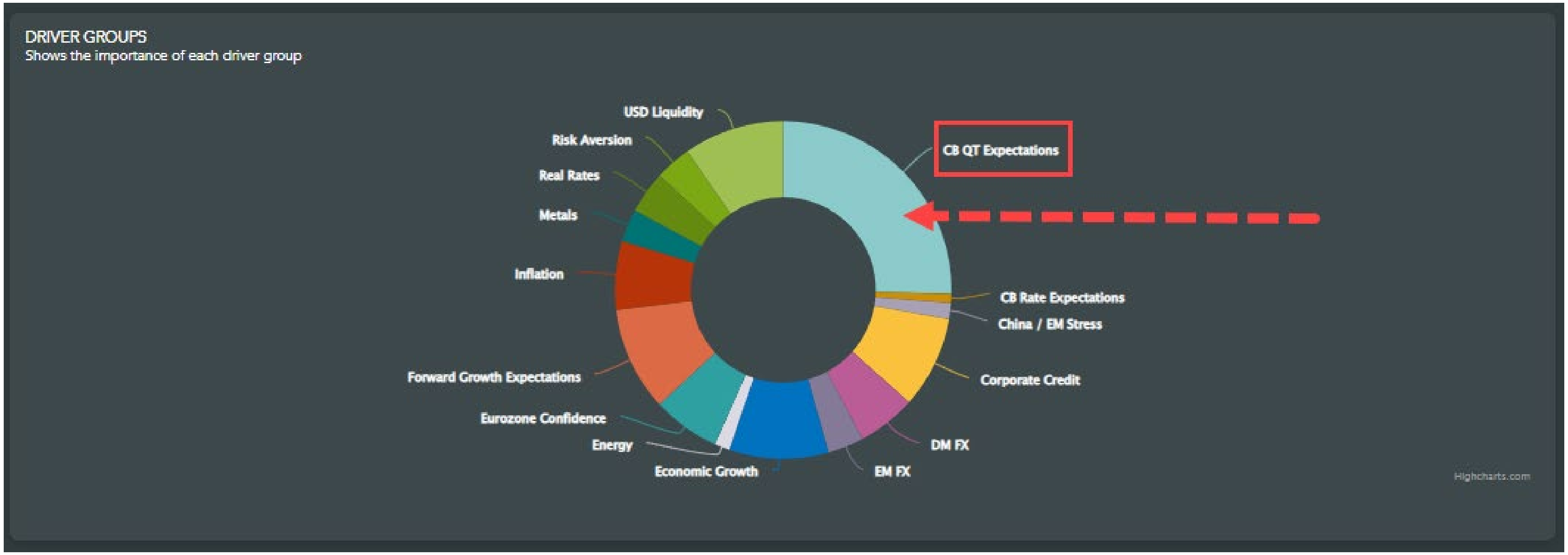
VIX 1m2m3m6m atm and upside with upside call skew

upside

Index	Strike (delta)	Maturity	Current	Percentile	Min	Max
VIX	0.25	1m	90.3	13.4%	66.6	235.2
VIX	0	1m	69.3	7.4%	50.2	214.4
Implied ratio			130.3%	75.3%	77.2%	264.4%
VIX	0.25	2m	87.4	24.7%	56.2	170.5
VIX	0	2m	64.9	8.4%	43.0	180.0
Implied ratio			134.7%	98.7%	74.1%	176.6%
VIX	0.25	3m	79.5	27.5%	55.1	141.8
VIX	0	3m	59.7	8.3%	47.8	148.7
Implied ratio			133.1%	99.9%	78.0%	133.4%
VIX	0.25	6m	65.9	23.3%	48.2	121.9
VIX	0	6m	51.4	5.2%	44.6	112.2
Implied ratio			128.0%	99.9%	97.2%	162.7%

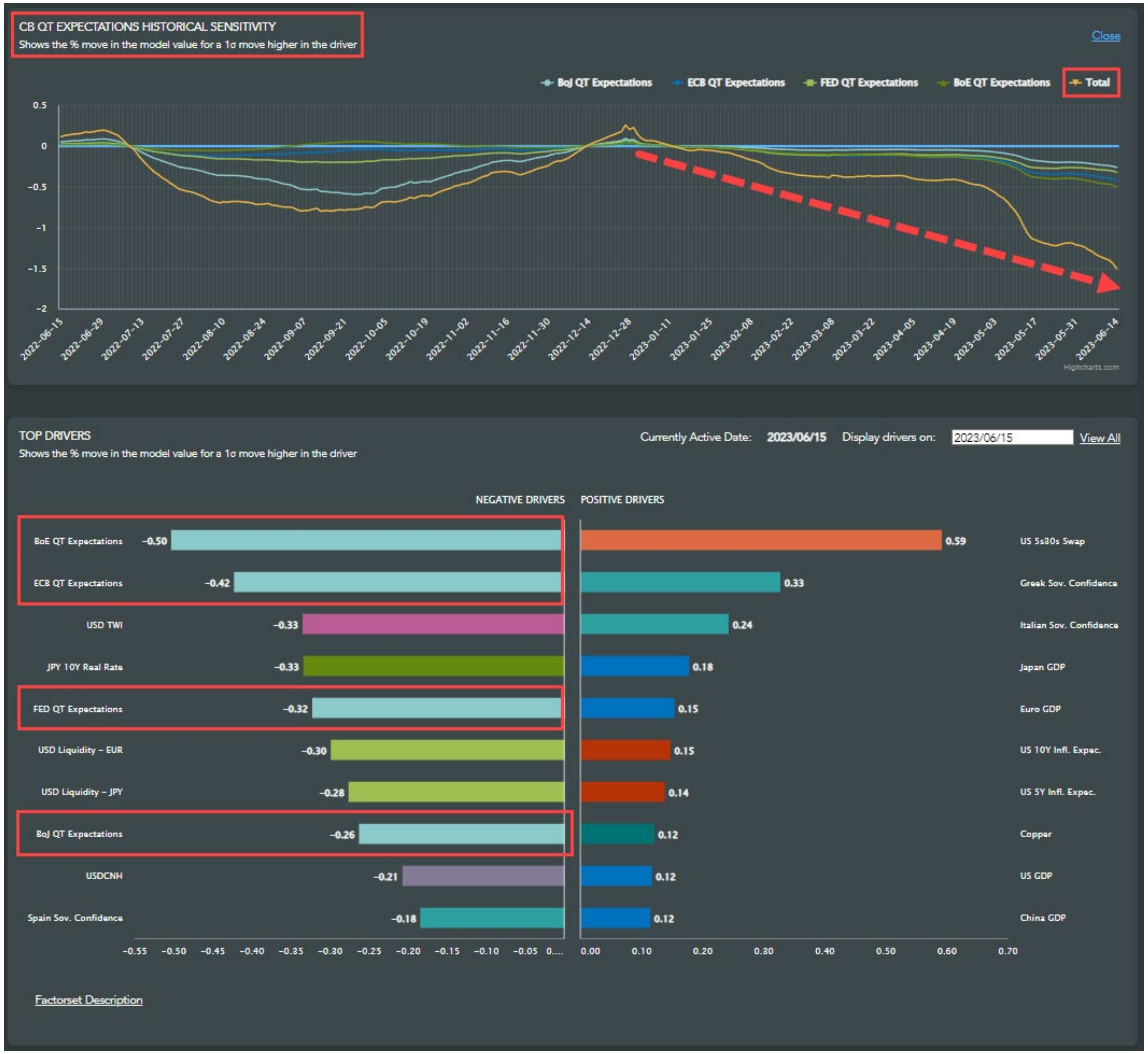
Source: Nomura Vol

And the VIX Upside / Gamma isn't simply just a spurious *"when recession hits, Equities will go lower"* narrative thing…as Quant-Insight PCA tool shows that "Central Bank QT Expectations" is "THE" S&P 500's largest singular (negative) macro factor price driver for the index



Source: Quant-Insight, Nomura Vol

VIX Upside Gamma for “Higher for Longer” Left-Tail Hedge



Source: Quant-Insight, Nomura Vol

And take a look at the historic VIX seasonality "fit" analog with the current path 2023 YTD:

Source: Nomura Vol

Point-being, despite a local Vol suppressing outcome from the Fed last week, a "Higher for Longer" message only increases the attractiveness of left tail "Hard-Landing" trades in both -SOFR and -VIX Call Spreads in coming months

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What Market Scenarios Would Hurt the Most in 2H23?

- **A Bear-Steepening in USTs** *(any number of possibilities: AHE / inflation stickiness, housing reacceleration, coupon sizes continuing to go up, R* higher…while Fed stays "nowhere" and remains on pause, due to ongoing "financial stability" concerns, waiting for lagged-and-variable tightening impacts to continue bleeding things out)*

- **A Cyclical Value (NOT Secular Growth) -led Equities rally** *(i.e. the current "grab into upside" and even the Call wing on the aforementioned "stuff that's been left behind" which we've seen MTD then extending)*

- **Dollar higher** *(folks slipping back into "Short Dollar" / Carry trades on "end of Fed tightening cycle" meme)*

- **MBS wider while IG tightens further** *(while the whole Street is pushing the opposite trade: IG wider while MBS tightens)*

- **US Equities Vol LOWER with Rate Vol HIGHER** *(seems impossible that we could see catalyst for higher Rate Vol—i.e. Fed forced to take terminal higher again scenario on still-too-firm data—at the same time that Equities could continue grinding higher on their merry way, without a Vol-event, due to so much over-positioning now being built)*

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The following is a brief summary of certain considerations which each NGFP or NIP OTC Derivative or Swap counterparty should take into account in deciding whether to participate in transactions involving OTC Derivatives or Swaps. This document is not meant to be all-inclusive; rather, it is intended to highlight certain of the more significant factors and special risks relating to OTC Derivatives and Swaps:

1. Credit Risk. NGFP, NIP (or an affiliate thereof) will be the writer of any OTC Derivative or Swap purchased by you. Consequently, any such purchase from NGFP, NIP or its affiliate will be an obligation of NGFP, NIP or the affiliate, as the case may be (as opposed to an obligation of a central clearing organization as in the case of exchange-traded options), so you must evaluate the credit of NGFP, NIP or its affiliate.

2 . Market Risk. Market risk is the risk that the value of a transaction will be adversely affected by fluctuations in the level or volatility of, or correlation or relationship between, one or more market prices, rates or indices or other market factors, or by illiquidity in the market for the relevant transaction or in a related market. As the purchaser of an OTC Derivative or Swap you generally will be exposed to market risk, and it may be difficult or impossible to sell or unwind your position as a way to reduce market exposure or to gain liquidity.

3. Funding Risk. Funding risk is the risk that, as a result of mismatches or delays in the timing of cash flows due from or to you or your counterparty in OTC Derivative or Swap transactions or related hedging, trading, collateral or other transactions, you or your counterparty may not have adequate cash available to fund current obligations.

4 . Operational Risk. Operational risk is the risk of loss to you arising from inadequacies in, or failures of system and controls for, monitoring and quantifying the risks and contractual obligations associated with OTC Derivative or Swap transactions, for recording and valuing OTC Derivative or Swap transactions and related OTC transactions, or for detecting human error or systems failures.

5 . Restrictions on Transfer; Non-Marketability. The OTC Derivatives or Swaps will not be registered under the U.S. Securities Act of 1933, as amended (the "Securities Act"), or under applicable state securities laws and, therefore, the transfer of OTC Derivatives or Swaps may be prohibited or restricted by such laws. OTC Derivatives or Swaps will be sold to or bought from you by NGFP, NIP (or an affiliate thereof) in transactions exempt from registration under the Securities Act by virtue of Section 4(a)(2) of the Securities Act and/or Regulation D thereunder. There will be no public market for the OTC Derivatives or Swaps. You also will be required to represent that you are entering into OTC Derivative or Swap transaction for investment purposes only and not with a view to resale or distribute. OTC Derivatives or Swaps which you enter into with NGFP,NIP (or an affiliate thereof) generally cannot be assigned or transferred without the prior written consent of NGFP, NIP or such affiliate. The limits on transferability of OTC Derivatives or Swaps make such transactions a relatively illiquid investment.

Because of the restrictions noted above, it may be extremely difficult for you to transfer any OTC Derivative or Swap entered into with you other than to NGFP, NIP or an affiliate thereof. NGFP, NIP or an affiliate thereof may, but is not obligated to, repurchase or otherwise resell an OTC Derivative or Swap originally entered into with you. If the OTC Option is an American-style option (as described in Section 10 below), you may exercise it in accordance with its terms and realize any intrinsic value it may then have. However, if it is a European-style option (also described in Section 10 below), it may be exercised only at its date of expiration and you will not be able to realize any intrinsic value the OTC Option might have at any earlier date unless it is repurchased by NGFP, NIP or an affiliate. Similarly, if it is a Bermuda-style option (described in Section 10 below), it may be exercised only on certain specific dates and thus you will not be able to realize any intrinsic value the OTC Option might have on any other dates unless it is repurchased by NGFP, NIP or an affiliate.

OTC Derivatives or Swaps are privately negotiated and are not listed on any exchange. Therefore, if you write and sell an OTC Derivative or Swap to (or buy an OTC Derivative or Swap from) NGFP AND NIP (or an affiliate thereof) to offset an OTC Derivative or Swap you bought from (or sold to) another dealer or counterparty, there will not be an automatic close-out as would be the case with listed options. You will, in addition to being a holder of an OTC Derivative or Swap , continue to be obligated as the writer of an OTC Derivative or Swap unless and until it is exercised or is sold back to you by NGFP AND NIP (or such other dealer or counterparty).

6. Pricing and Other Terms. The price and characteristics of an OTC Derivative or Swap are individually negotiated between NGFP, NIP or its affiliate and you and there is no central source to obtain prices from other dealers. Accordingly, neither NGFP, NIP nor its affiliates represent or warrant to you that the prices at which they offer OTC Derivatives or Swaps are the best prices available in the marketplace. Similarly, while marketmakers and dealers generally quote prices or terms for entering into or terminating OTC Derivative or Swap transactions and provide indicative prices or mid-market valuations with respect to outstanding OTC Derivative or Swap transactions, NGFP, NIP and its affiliates are not contractually obligated to do so. You may wish to seek representative quotations from other participants in the OTC Derivative or Swap markets to determine the intrinsic or current market value of a particular OTC Derivative or Swap. Consequently, it also may be difficult for you to establish an independent market value for an outstanding OTC Derivative or Swap. You should not regard the valuation or representative quotation that is provided by NGFP, NIP or its affiliate at your request to be an offer to enter into or terminate the relevant transaction at that value or price, unless the value or price is identified by NGFP, NIP or its affiliate as firm or binding with respect to a specific quantity of the security.

7 . Potential Loss of Investment. As a purchaser of an OTC Derivative or Swap you may lose your entire investment in a relatively short period of time. This risk reflects the nature of an OTC Derivative or Swap as an asset which tends to decline in value over time. If the OTC Derivative is a call option, it may not be in-the-money or at-the-money before it expires; if it is a put option, it may not be in-the-money at the time of its expiration. Therefore, a long OTC Derivative or Swap is not intended to be the sole asset held by an investor, and long OTC Derivatives or Swaps should be only one portion of an investor's portfolio, which should be diversified by holding other types of asset.

8 . Position and Exercise Limit Requirements. The position limit and exercise limit rules of the Financial Industry Regulatory Authority, Inc., Rule 2360, may apply to OTC Options. As a result, you may be required to aggregate all options on listed equity securities and all OTC Derivatives held by you at any given time to determine whether you have complied with such limitations, thereby potentially limiting your positions in OTC Derivatives or Options.

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9. Option Style. The style of an option refers generally to when an option is exercisable.

An American-style option may be exercised at any time (i.e., on any business day) during the specified exercise period prior to the time of expiration.

A European-style option may be exercised only on the specified exercise date (or expiration date).

A Bermuda-style option may be exercised only on certain specified dates prior to the expiration time.

An Asian-style option is a variant of the European-style option. The Asian-style option may be made available by NGFP, NIP or its affiliates to certain counterparties under appropriate circumstances. Alternatively referred to as an "average price" option, in an Asian-style option the reference price in relation to the underlying securities is derived from an agreed upon calculation, which, by way of example, may be based upon an average of the underlying securities' market prices at predetermined dates occurring during a specified "averaging period," with the exercise date (assuming the counterparty is the option buyer or holder) occurring at the end of such averaging period. An Asian-style option can have the effect of reducing the risk, inherent in a standard European-style option, of establishing the value of an OTC Option on a single trading day, and hence can protect the option holder from fluctuations in underlying securities prices which might otherwise occur as a Europeanstyle option nears the single expiration date. An Asian-style option's payoff is therefore based upon the difference between the average reference price of the underlying securities and the option strike price.

10. Additional Considerations. There may be other significant risks which you should consider based upon the terms of a specific OTC Derivative or Swap transaction. Highly customized OTC Derivative or Swap transactions in particular may increase liquidity risk and introduce other significant risk factors of a complex character. For example, highly leveraged transactions are subject to significant changes in value as a result of relatively small changes in the value or level of an underlying or related market factor.

Before entering into an OTC Derivative or Swap transaction, you should understand fully the terms of the transaction, the relevant risk factors, the nature and extent of your risk of loss and the nature of the contractual relationship into which you are entering. You also should evaluate carefully whether the transaction is appropriate for you in light of your investing experience, financial objectives and needs, financial resources, and other relevant circumstances and whether you have the operational resources in place to monitor the associated risks and contractual obligations over the term of the transaction. If you are acting as a financial adviser or agent, you should evaluate these considerations in light of the circumstances applicable to your principal and the scope of your authority.

In entering into OTC Derivative or Swap transactions you should also understand that NGFP, NIP or its affiliates are acting solely in the capacity of an arm's length contractual counterparty to you in connection with the transaction and not in the capacity of your financial adviser or fiduciary, unless NGFP, NIP or its affiliates have expressly so agreed in writing, and then only to the extent so agreed. Accordingly, unless NGFP, NIP or its affiliates have agreed in writing to act as your advisor, you should not regard any transaction proposals, suggested investment strategies or other written or marketing materials or other oral communications from NGFP, NIP or its affiliates as investment recommendations or advice or as expressing NGFP, NIP or its affiliates' view as to whether a particular transaction is suitable for you or meets your financial objectives.

In evaluating the risks and contractual obligations associated with a particular OTC Derivative or Swap transaction, you should also consider that an OTC Derivative or Swap transaction may be terminated, modified or offset only pursuant to the terms of the relevant OTC Derivative or Swap Agreement or confirmation or by the mutual consent of the parties to the transaction. Accordingly, it may not be possible for you to terminate your obligations or your exposure to the risks associated with a particular transaction by terminating the transaction prior to its scheduled termination date or by entering into an offsetting transaction.

Furthermore, you should be aware that NGFP, NIP and its affiliates may from time to time have substantial long or short positions in, and may make a market in or otherwise buy or sell instruments identical or economically related to, OTC Derivative or Swap transactions entered into with you. NGFP, NIP or its affiliates also may undertake proprietary trading activities, including hedging transactions related to the initiation or termination of an OTC Derivative or Swap transaction with you, which may adversely affect the market price, rate, index or other market factors underlying an OTC Derivative or Swap transaction entered into with you and, consequently, the value of such transaction.

THIS BRIEF DISCLOSURE STATEMENT DOES NOT PURPORT TO DISCLOSE ALL OF THE RISKS OR OTHER RELEVANT CONSIDERATIONS ASSOCIATED WITH ENTERING INT O OTC DERIVATIVE OR SWAP TRANSACTIONS. YOU SHOULD NOT CONSTRUE THIS DISCLOSURE STATEMENT AS BUSINESS, LEGAL, TAX OR ACCOUNTING ADVICE. YOU SHOULD CONSULT YOUR OWN BUSINESS, LEGAL, TAX AND ACCOUNTING ADVISERS WITH RESPECT TO PROPOSED OTC DERIVATIVE OR SWA P TRANSACTIONS AND YOU SHOULD REFRAIN FROM ENTERING INTO ANY OTC DERIVATIVE OR SWAP TRANSACTION UNLESS YOU HAVE FULLY UNDERSTOOD THE ASSOCIATED RISKS AND HAVE INDEPENDENTLY DETERMINED THAT THE TRANSACTION IS APPROPRIATE FOR YOU.

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