Crash thoughts

When a crash happens, ask yourself the following questions:

1. If you were only allowed one more investment decision your entire life, what would it be? Buy quality stocks and sit.
2. At this point, if you were only allowed one direction to trade and hold forever, what would it be? Long.
3. In the short run, the markets are unpredictable; in the long run it is the reflection of company’s fundamentals. Earnings and growth. As long as fundamentals don’t change, no reason to trade.
4. Why you should stay away from tech: no competitive advantage lasts forever. Companies in concrete industries with good earnings do.
5. Are the companies you invest in head of the industry and make stable earnings and growth? Yes.
6. Are any companies in your portfolio speculation? 华大基因.
7. Are you holding good companies you like? Yes
8. Would you be long or short these companies in the long run (For the next 20 years)? Long
9. Cost of entry is sunk as soon as you enter and you are an owner of asset that generates dividends. You own assets.
10. Buying and selling decisions should not be made on how much money made/lost or percentage terms, it should be 1) earning potential 2) valuation. If a company does well, now it’s cheaper, that should make you buy it, not sell it. (Share price = P/E ratio \* earnings)
11. If you had 0 position and have a fresh set of eyes, would you long or short at the current level? Long, so don’t
12. Don’t buy something because it has gone up. Buy because it is an asset that has growth value and solid earnings and competitive advantage.
13. Your position should not be so big such that you worry about being wiped out and unable to hold the long term (panic).
14. You should use leverage on safe products and leverage should not be the reason for liquidation. Only earning potential change should be the reason for selling.
15. You should not liquidate because your portfolio has x% loss. Such loss cutting does not follow the principle of only looking at fundamentals/earnings growth.
16. Property is also leveraged. Most people are levered 3-5 times. Do people sell after the housing market corrects? No because you can live in it, also because it’s difficult to buy and sell so you stick with it, so you tend to hold on to it and most people make money from property.
17. Market timing is hard. Ride through the volatility and aim for long term return.
18. Why did the US go down? Vega rebalancing, too much short vol activities leading to selling futures to hedge to cover the short vega. When VIX goes up, companies will need to cover their short vega (long delta) by selling futs. When vol of vol goes up, there is more short vega and longer delta which needs to be sold. Such adjustment is inevitable. When vol of vol gets remarked higher, suddenly there is a lot more +delta to hedge. The vol of vol unwinding is self-destructive.
19. Why did China follow the US? China also greed-rallied in Jan.
20. Problem with the US market: short vega positioning. How that affects Chinese companies? None.
21. How are the economies doing? Doing fine. US economy is strong. Any company melting down? No. Any Lehman Brothers, fannie mae? No.
22. Only level matters, not direction. Valuation is determined by PE ratio and earnings. If you like a company, price going down makes it more attractive to own.
23. You should invest **not** based on the direction of the market but level (valuation) and company’s ability to generate revenue and growth – only these matter in the long run.
24. Worst case scenarios. Stock: what is your plan if market drops continuously? How much maximum loss can you take on your portfolio? What is your cutting loss strategy? Hold until end of April and see what happens. Cut leverage if markets stay bad. How to cut? Cut 1/4 of leveraged delta to 600k, 400k, 200k.
25. Worst case scenario. Futures: let Feb futures expire. Roll less into the next Month. Be less aggressive in accumulation. Cut 1/4 of position to 36 futs, then cut to 24, to 12 progressively each month. (now we have 48)
26. You should never worry about being wiped out, because it impacts your ability to hold for long term. To human beings, if there is a small probability that a position will wipe out your entire portfolio, you would want to accept loss on it in order to avoid destruction. Such behavior is risk averse and is not compensated by the market.
27. Find your optimal leverage capacity by gradually reducing position and stop at a point where you are comfortable with the daily fluctuations of the portfolio.
28. You need to prepare for the worst. Can you handle a 30% loss? What about 50%? What about 80%? What is your strategy in each case?
29. You should be able to emotionally accept the size of the fluctuation of the positions. If not, that means your size is too big and cannot handle downturns.
30. Lost/gained pnl is sunk and should not have any bearing on future investment. Only valuation and earnings potential matter.
31. No active trading below 60 DMA. Wait until things calm down and DMA flips above 60day.
32. Adjusting position size only at month end. Don’t want mtd fluctuation to affect with position sizing.
33. Going forward, adding and removing position should be done very slowly. Jan build-up was too fast on futures side. There are a lot of opportunities to add, be patient.
34. Position change from 1 month to another cannot be too great. Dec had low position and jan had huge position, make sure position changes less than 20%.
35. Next month, if things don’t stabilize, cut futs by 20% to 38 futures, stock by 10%, both reducing a bit of leverage. (20% move month on month will avoid getting hit on the top and dropping out too much on the bottom). Avoid cutting in panic / adding in greed. (January added in greed, had margin position, gladly it wasn’t too much)
36. Position changing cannot be more than 20% of entire ptf on a monthly basis. Both addition and subtraction is no more than 20%. Jan mistake: adding too much too fast. Got caught on top.
37. Keep track of entire delta on a daily basis.
38. Always draw up trading plan before open to avoid trading on emotions.
39. Continuous 20 day rally sowed the seeds for this massive drop.
40. Good practice to know how to handle crashes. In the future, be careful with leverage.
41. Anything can happen. Be aware of all kinds of situations like down 50%, up 50%. Short term market is driven by emotions, long term market is driven by one thing which is earnings.
42. In the long term, add when market liquidate. Don’t add when there is no liquidation. Liquidations happen once a few months.
43. When markets liquidate, the quicker the better.
44. Trading planning until the end of Month: hold.
45. Going forward, max lev is 2x. More than that feels uncomfortable. 2x can still hold long term without panicking.
46. 10:49 China liquidates.