S&P 500 Weekly Forecast 1/26

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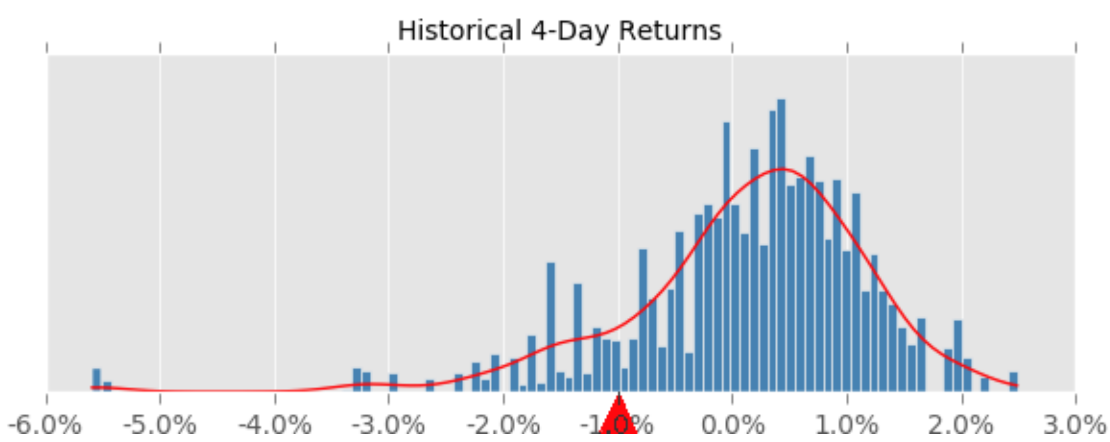
Hey guys,

Last weekend, we *finally* started souring on the S&P 500's future prospects. The assumption was that if GEX can't get any higher than $1.36bn, then the GEX floor is going to stay weaker. And if *half* of the prior week's 2% gain was nothing more than a squeeze, then we're no longer in a position of strength, and ought to get more defensive.

> With that said, remember that GEX is still high, and that DIX is supportive of prices not far below where we are right now. Yes, it might be time to slow down. No, there will be no Volpocalypse. [...] We just think that we should start tempering the most bullish of those expectations.

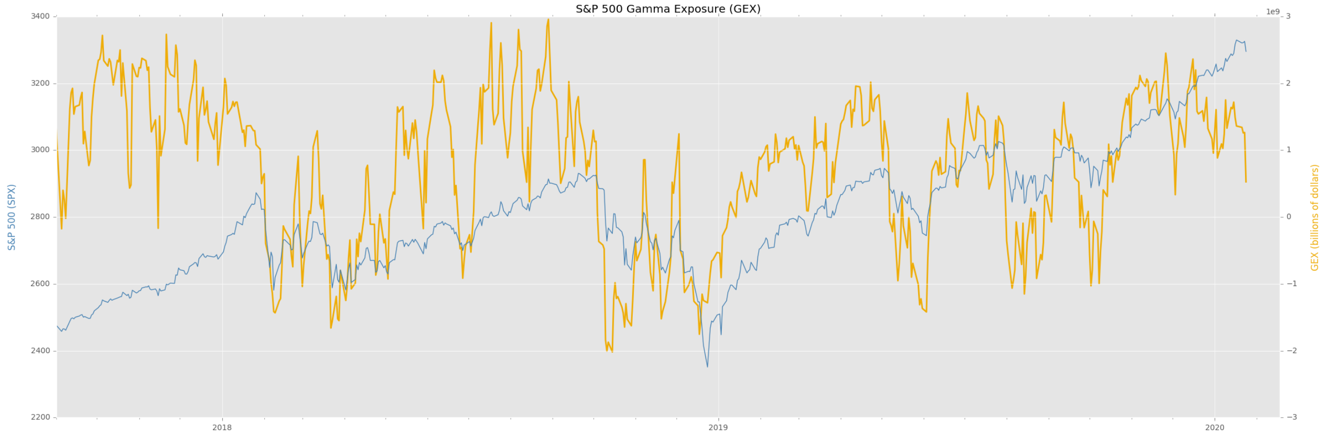
Well, the index retraced the **1%** that it squeezed. No more, no less.

And on its own, that's neither surprising nor interesting.



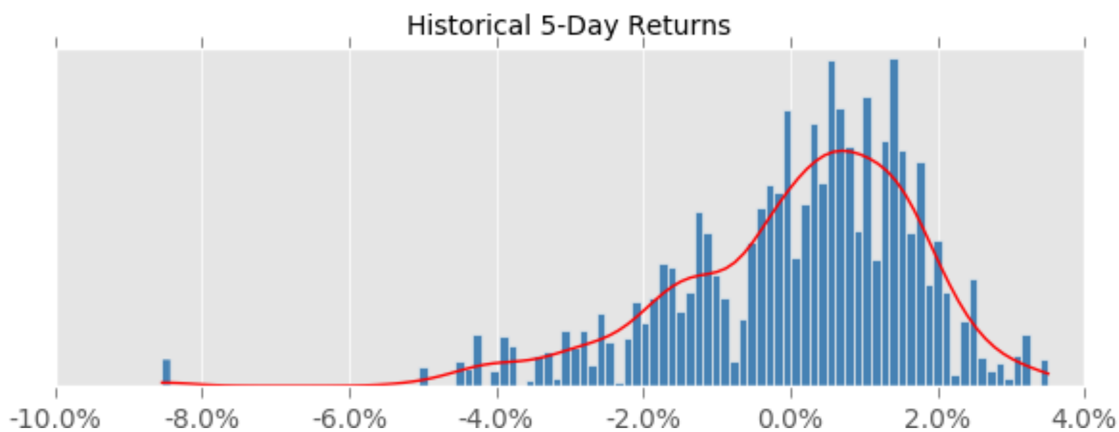
But what *is* interesting is that this 1% loss means quite a lot for SPX GEX. Because with the SPX monthly expiration gone, there's less long gamma on dealers' books, and lower GEX overall. For this reason, a 1% loss in SPX brought GEX all the way down to $526mm.

GEX hasn't been that low since the very beginning of December.



And with a GEX in the $0.5bn range, the forecast changes. With fewer restraints on motion, a more serious left tail arises (although the median gain rises to compensate for that extra risk -- upside volatility and downside volatility *usually* come together). Basically, everything gets a bit more dramatic, with threats of zero GEX in sight for the first time in a long time.

Even if you don't want to think in terms of the extreme tails, it's notable that the probability of a ~1.75% weekly loss is reasonably high. This has *not* been the case for a very long time. In other words, this distribution actually has *some* risk. Fancy that.



In numbers, this 5-day return forecast has a mean gain of **0.07%**, a median of **0.40%**, and a standard deviation of **1.68%**. In volatility terms, that's a 1-week vol of **11.89%** -- quite a bit higher than what you've grown accustomed to in the last three months. Meanwhile on a 1-month timeframe, we forecast vol at **12.28%**. With VIX hanging around 15, there's still an apparent variance risk premium to be harvested, but really, it's not all that great.

Speaking of "not all that great," the entirety of last week was not great from the perspective of SPX/SPY option trades. We didn't place a single trade -- there wasn't enough edge to justify it. The GXV skew plots began the week mostly lining up with the market's skews, and that persisted. Even now, when we look at the vertical skew charts at the bottom of the attached PDF, we see little edge. Note how closely GXV- and market-derived IVs track each other on the 5-DTE plot. There is no low-hanging fruit here, and so we're *still* on the sidelines.

For the long SVXY / short VXX trade, though, GXV1D being below VIX is the only requirement. And that barrier has yet to be breached. This is suggestive, again, of what we said last week: Yes, there's more risk now that the GEX floor has weakened, but no, there's no risk of a Volpolcalypse. When GXV is 20 and VIX is 13 -- that's when you get scared. That's not happening here.

Two other things demand examination: Viruses and DIX.

Wuhan Coronavirus is gaining steam as a fear *du jour.* Last time there was a big geopolitical scare, it was with regard to an imminent war with Iran. We cavalierly brushed this off at the time because GEX was so high that pretty much nothing could break the floor. The feedback from this event was that "Iran doesn't matter," despite the fact that if GEX were below $1bn when that scare started, the market would have sold off significantly. But with his virus, GEX is a mere $500mm. As a result, there is some potential for people to take "pandemic risk" seriously -- simply because they may see that the market takes this more seriously than Iran (and it already has).

But how serious can it get? That takes us to point two: The Dark Index (DIX). On Friday, DIX printed 46%, which is above our "bullish" level. This predicts good returns over the course of the next three months. It does not, however, necessarily predict good returns over the next week. DIX is telling us that there is real, passive buying demand in stocks (for whatever reason), and that this will likely manifest itself in higher prices over time. But with the combination of a weak GEX floor and a global fear that might actually gain traction, we can't expect DIX to save us *right away*.

So, be cautious. Some losses seem quite possible (finally). But a true correction seems unlikely just yet.

Fresh Picks

The 100 low-GEX picks have a mean 20-day projected return of **1.56%** and a standard deviation of **8.02%**. The 13 high-GEX picks have a mean 20-day projected return of **0.91%** and a standard deviation of **6.01%**. Snippets of charts are attached, as always. With a tiny shakeup at the end of the week, there's a bit more opportunity in single stocks, and despite the fact that there aren't a lot of high-GEX candidates, last Friday's OpEx opened up a lot of low-GEX stuff.

This is probably played out, and we've exited:

> The only stock that fits this bill is **Booking Holdings** (BKNG). Its GEX was recently >200k, which is easily more than *half* of daily volume. This kept things pretty tight. And now, after Friday, GEX is close to zero. Options, meanwhile, haven't gotten any more expensive. Worth a shot? We think so -- how about a tiny OTM put position?

But.... if you're interested, it would be worth trying to play BKNG again, in the other direction.

Otherwise, another low-GEX candidate would be **Bank of America** (BAC). This one is an old standby. Its options are liquid, and they're still pretty cheap right now. *And* its GEX is around zero. Since BAC has recently had many days with GEX in the 2bn-share range, a GEX around zero is a potentially nice opportunity to buy calls OTM, betting on a relief bounce. Nothing too sophisticated. Just something that has often worked in the past, thanks to GEX dynamics.

Last weekend, we told you to "stay safe out there!" That's worth reiterating.

So, stay safe out there.

The SqueezeMetrics Team

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