S&P 500 Weekly Forecast 2/23

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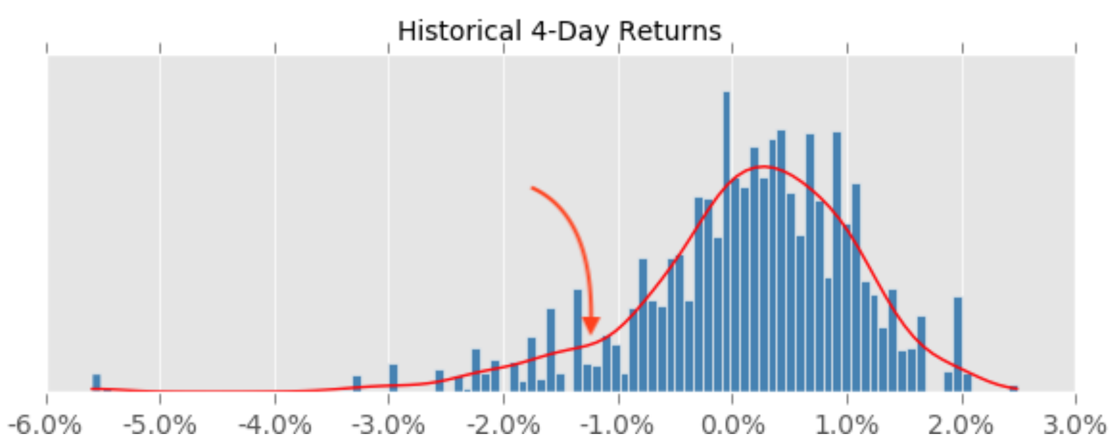
Hey guys,

So, Tuesday and Wednesday were typical high-GEX days: Intraday mean-reversion and low-volatility upside drift. Nice! This promised to continue through to the end of the week, after which the monthly option expiration would bring GEX back to around $1bn, which is where we draw the line between "high" and "middling" GEX.

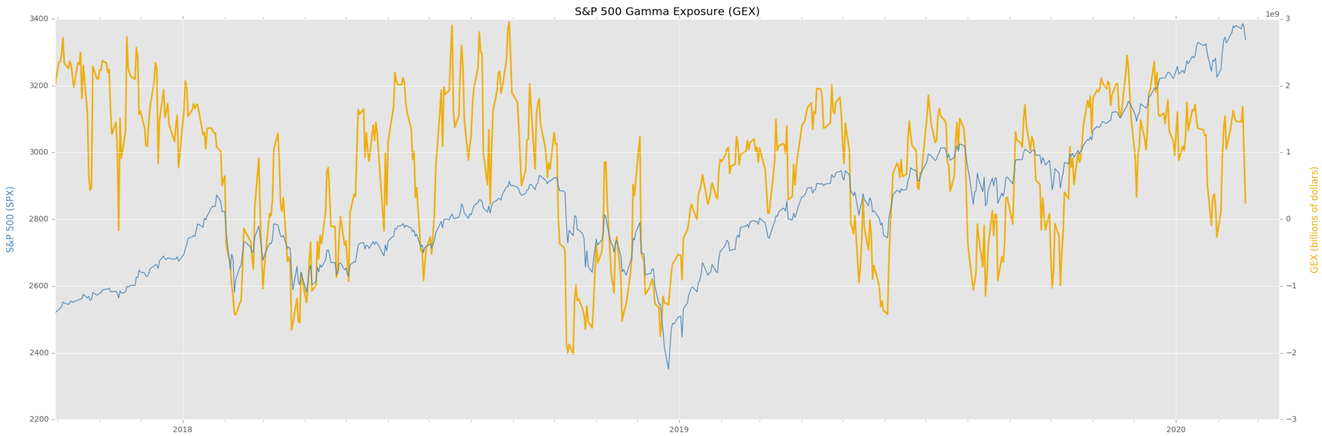
But then something happened on Thursday, and whatever it was (let's ignore that), it was pretty dramatic, because getting SPX to fall 1.2% on a high GEX day requires a lot of bearish volume, and all at once. As is typical in high-GEX scenarios, though, once dealers' re-hedging started, the rest of the day reverted to the mean. Thank you, GEX floor.

On Friday morning, the big monthly OpEx had already begun (SPXAM expired), bringing GEX down a peg by default, and by Friday at the close -- following a bit more bearishness -- the index was down **1.2%** on the week and GEX was a whole lot lower.



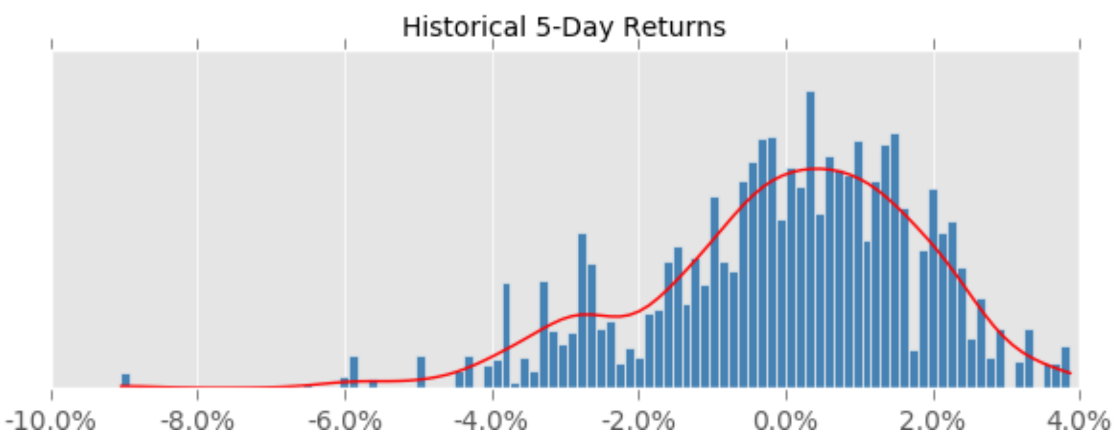
For a week with a forecasted standard deviation of 0.99%, maybe a 1.2% loss doesn't sound that crazy, but you can tell from the probability density above that any loss over 1.00% is pretty unusual for a week starting with GEX at $1.5bn. This gives you a sense of how dramatic Thursday's action really was -- that must have been some very persistent selling to put such a dent in the GEX floor.

But enough about last week. What's *really* interesting about last week is the awkward position it leaves us in for *next* week. GEX, after two days of being battered by SPX price action and one monthly expiration, closed on Friday at a mere $0.25bn. Down from the $1.5bn that it started the week with.



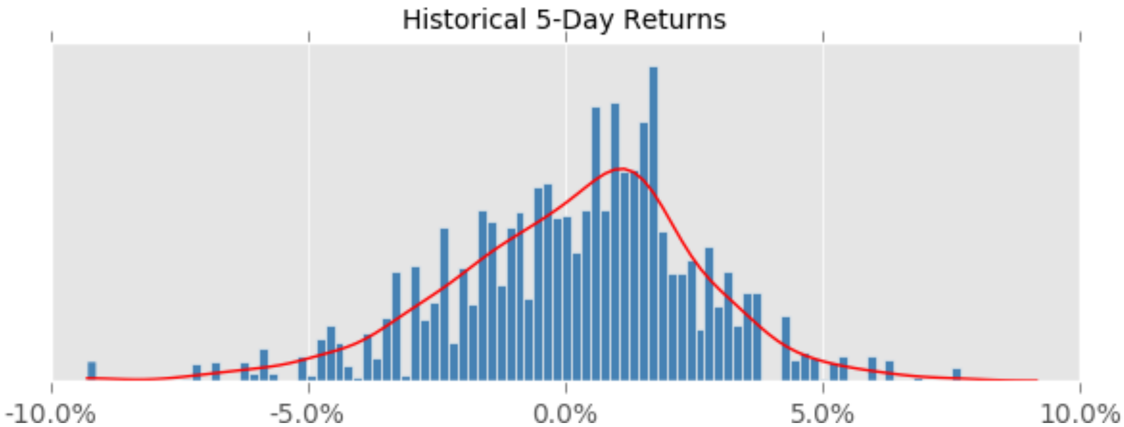
Obviously, $0.25bn is a lot closer to zero than it is to the safe-zone of $1bn, but you really have to take a look at the 'GXV by S&P 500' plot on the attached PDF to get a sense for *why* low-positive GEX numbers make us uneasy. See how steep the slope of GXV is right here? That means that volatility is *itself* volatile here. I.e., a small move up in SPX will decrease realized vol, whereas a small move down will increase realized vol. This little dance always occurs when the market is in the middle of making a decision between staying in positive GEX land or dipping into negative.

At the close on Friday, we were straddling that risk. Indeed, the left tail of the forecasted distribution below is long enough to make the mean of the whole distribution *negative* (also something that only happens near zero GEX), and with the benefit of seeing the E-minis open tonight, the fear of a weekly return landing in that clump around -3% seems legitimate indeed.



In numbers, the above 5-day distribution has a mean return of **-0.03%**, a median of **0.19%**, and a standard deviation of **1.86%**. In volatility terms, that's a 1-week vol of **13.2%**. Further out in time, we see a 1-month volatility of **12.5%**.

Given that futures are currently threatening an SPX open below 3320 (which is around where GEX = 0), let's also look at a distribution that would reflect lower GEX.



Notice how the distribution is quite different (vol of vol!). Instead of a volatility of 13.2%, it's **17.16%**. The mean is positive, and while the left tail is pronounced, the right tail offsets it. A median gain of **0.46%** is a distinguishing feature -- absent other forces, lower GEX tells of a higher probability of near-term gains. The mean, too, is positive, at **0.17%**.

Right now, the market is straddling these two worlds.

For the long SVXY / short VXX practitioner, this is the toughest time to trade. It's likely that GXV will rise into the low 20s, but it's also likely that VIX will follow. We'll be following it on an intraday basis (https://squeezemetrics.com/monitor/v/gxv), and getting out of the trade if GXV rises above VIX -- as planned.

For the SPX/SPY option geeks, it's likelier than not that if SPX opens around 3300, the best trade will be long (OTM) calls, as is usually the case when GEX falls to or below zero and IVs are relatively cheap. But then it would be good to spread or monetize those calls pretty quickly. As you can see from the attached PDF, when SPX closed at 3337, the favored trade was still to be short options. Again -- vol of vol!

Another option trade that tends to perform well here is short skew with a bit of short delta, which may or may not be something you'd enjoy doing.

In any case, it may be that the "laundry list of geopolitical risks" that we referenced last weekend is finally having an effect. But more interesting to us than geopolitical risk *per se* is the way the S&P 500 reflects that risk and crystallizes what "we," collectively, believe is "real" geopolitical risk. Since GEX is now around zero, risk-awareness will be amplified, and the Narrative Machine will be focusing a lot on coronavirus, et al., in the next few days as SPX volatility brings it into focus.

Fresh Picks

The 139 low-GEX picks have a mean 20-day projected return of **1.63%** and a standard deviation of **7.26%**. The 9 (all gone!) high-GEX picks have a mean 20-day projected return of **0.60%** and a standard deviation of **6.25%**. Now that Gamma Week is over, very few high-GEX candidates remain. Snippets of charts are attached, as always.

We're not going to highlight any picks in particular this week, since none are *particularly* interesting to us. But it's worth mentioning that any trade that you want to be long -- now's a decent time to get long convexity (buy a call). Same goes for something you'd be interested in shorting (buy a put). Now is the right time to be taking advantage of single-stocks' collectively low GEX. That is, if you're not too distracted by the excitement in the index itself (which we are!).

Enjoy!

The SqueezeMetrics Team

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