

S&P 500 Weekly Forecast 5/9

From: SqueezeMetrics <info@sqzme.co>
To: SqueezeMetrics <info@sqzme.co>
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Hey everyone,

We've been slowly piecing together a "tension model" to describe the relationship between the S&P 500 and its volatility. So far, we've determined that "*past implied volatility*" (*PIV*) is indeed, as we hypothesized, the angle from which one really needs to view the progression of spot price, realized volatility (RV), and implied volatility (IV) -- if one wants to have an internally consistent view of the vol market. It's the key to understanding volatility, as a whole.

Early on, we saw this in the form of our "vol triangle." When the relationship between PIV, IV, and RV was approximately equal (a "tense" 60-60-60 triangle), that was invariably when the greatest S&P 500 volatility commenced. Then, when we added spot price dynamics, we saw that the signal is enhanced by waiting for a market that's rolling over (as recent SPX returns approach zero).

These are all things that trading veterans would understand, and even be able to express -- but they're *not* things that are ever consistently expressed *quantitatively*.

And so, expressing this "tension" in a tidy, quantitative way is what we've been working on for a couple months now, and the closer we get, the more convinced we are that it's worth more digging. So today, let's push off some data onto you, dear reader, so that you can have a peek and ponder it yourself -- and so you can tell us what you see.

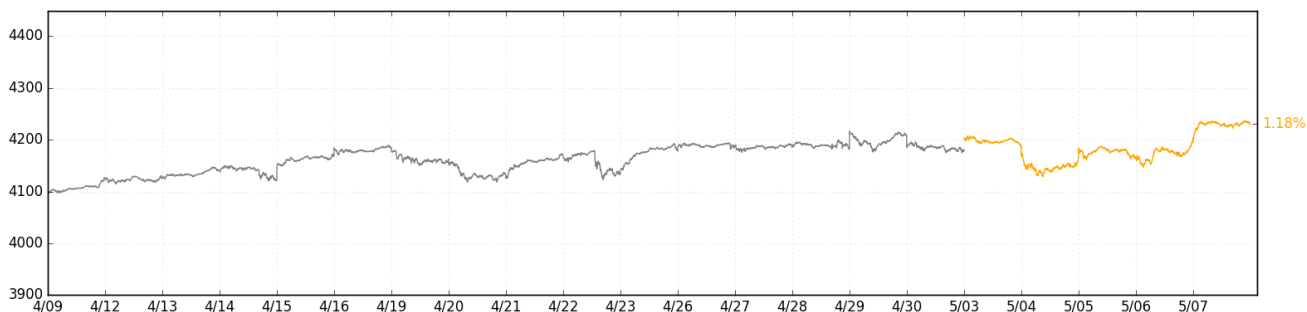
But first...

1. All pain, no gain
2. The pump
3. The dump

All pain, no gain

We started the week off with some OTM calls. The usual tiny position, which we've been rolling for a while. But then on Tuesday, a bit of unexpected data showed up -- a second shallow NPD print (-1.82): Perhaps an indication that put-buying had significantly slowed! And by extension, a suggestion that investors had given up on buying insurance. Exciting!

And so we spent the next two days long a 1-month SPX put, betting that the sudden lack of insurance-buying, coupled with the high sensitivity of customers to shifts in IV (a persistently shallow negative VGR), could spike vols. And, well, maybe it did, and maybe we were right -- on Tuesday, VIX immediately spiked over 3 points, to levels not seen since March! But... it was short-lived.

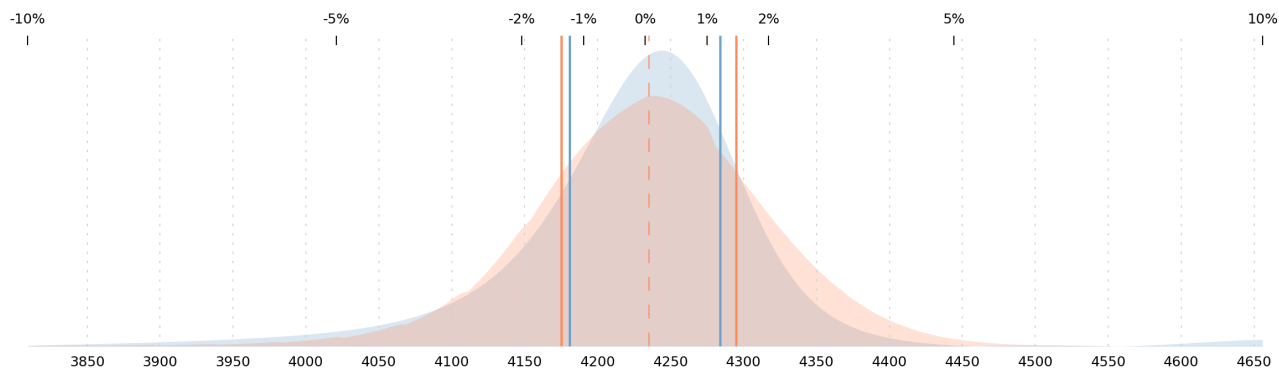


The put got nearly halved before we confirmed that NPD prints were staying pretty neutral and gave up. The call expired worthless.

After an altogether lovely YTD performance for all things GEX-, NPD-, and VGR-related (and SuMo too!), this past month has been a slow bleed. Luckily, one of the greatest motivations for understanding the market is losing money. So let's harness our resentment and move on.

The pump

We've been making very low-probability bets for the past month. That's the "reason" that we've been slowly bleeding chips. We maintain that they're the right bets, though. And as if to goad us further, the market continues to offer the same bet. Our resolve is being tested.



So yes, we already bought a starter OTM call position for Friday (at EOD, after IVs had gotten crushed), and we will likely add more, at and above SPX 4300.

If the market insists on being stubborn, so will we.

Monday SuMo:

4217.09	4240.36	4263.62
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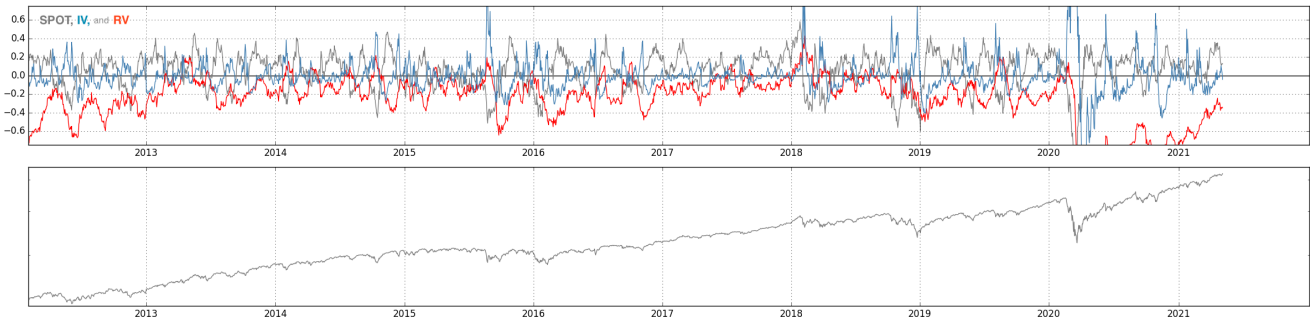
The dump

We said we'd supply a data dump. It is attached.

Columns are DATE, SPOT, RV, and IV. Each field is based on a 1-month historical moving window of data, and is denominated in a normalized percent. Everything is normalized to past implied volatility (PIV). E.g., "SPOT" is the average daily S&P 500 percent gains over the past month, normalized to the implied daily moves of PIV. "RV" is the difference between day-to-day realized volatility and PIV's implied ranges. "IV" is the

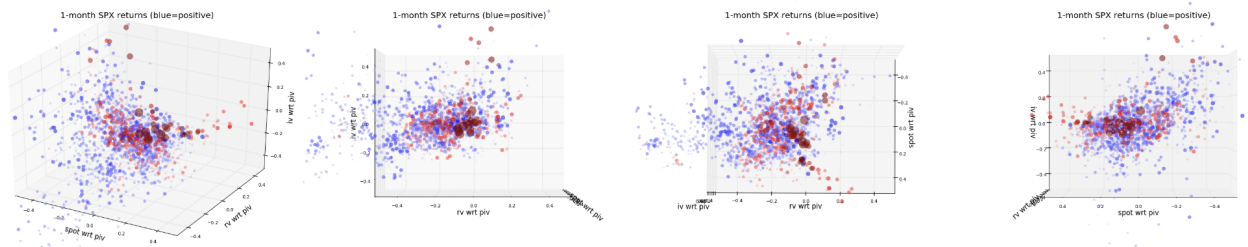
difference between current implied volatility and 1-month PIV.

Just as with the angles of the "vol triangle," all of these numbers "oscillate." Except instead of oscillating around 60 degrees, they oscillate around 0.0% (but the meaning is very similar).



When "SPOT" is above 0%, that means long SPX has "worked" in the last month. When "RV" is above 0%, that means long gamma has "worked" in the past month. When "IV" is above 0%, that means long vega has "worked" in the past month. Anything below 0%, of course, means the trade *hasn't* worked in the past month. Get the idea?

And when SPOT, RV, and IV are all close to zero, that's when you oughta buckle up, because that's the same thing as the equilateral 60-60-60 vol triangle combined with a market that's rolling over. Note that the big red dots below tend to cluster where SPOT is *just above* 0%, and RV and IV are *just below* 0%. A precipice, of sorts.



Notice *also* that when... er... well, OK, let's stop. We'll let you have a look at the data and charts, and maybe draw some of your own conclusions before we go on bloviating about what it all might mean. Lots more to think about and test.

But we can't help ourselves from mentioning one thing that we find... very exciting. Especially now that the method seems to be showing us something useful: *This analysis could be done on any security, asset, or index with an option or vol market.*

Yeah. That's cool.

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By the way, while you're looking at the data this week, we're finally going to create some kind of "Sentiment Sheet PDF" to go along with the Risk Report and Probability Page. We're tired of downloading the whole GEX+ spreadsheet every morning when all we want is to see the new NPD, VGR, and SuMo numbers.

Enjoy another horrible, awful, no-good week.

The SqueezeMetrics Team

tension.csv 140 KB