S&P 500 Weekly Forecast 12/12

From: SqueezeMetrics <info@sqzme.co>
To: SqueezeMetrics <info@sqzme.co>
Subject: S&P 500 Weekly Forecast 12/12
Date: Sunday, December 12, 2021 9:00 PM
Size: 3.0 MB

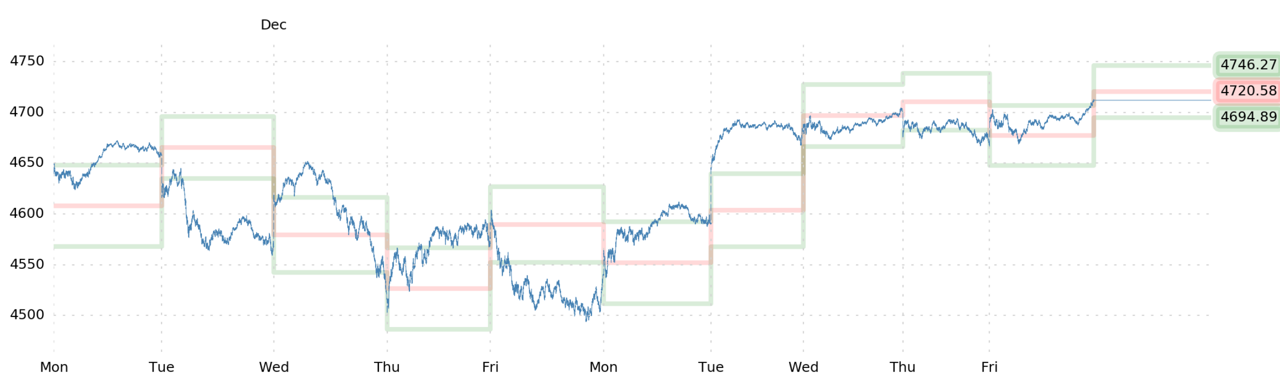
Hey everyone,

We strayed from the usual format last week, because *events* strayed from the usual format. That will be partly true this week as well—because there are important things going on.

Three things, really:

1. It was a great week *(took risk, got paid)*
2. The data is very interesting right now *(DIX versus NPD)*
3. Less Research, more Development *(big website changes incoming)*

1.
You know that we were maxed short vol (front-month VIX) last weekend. That was the whole point of the note. VIX was 30. Now VIX is under 20. SPX up 200 points. So that was nice.

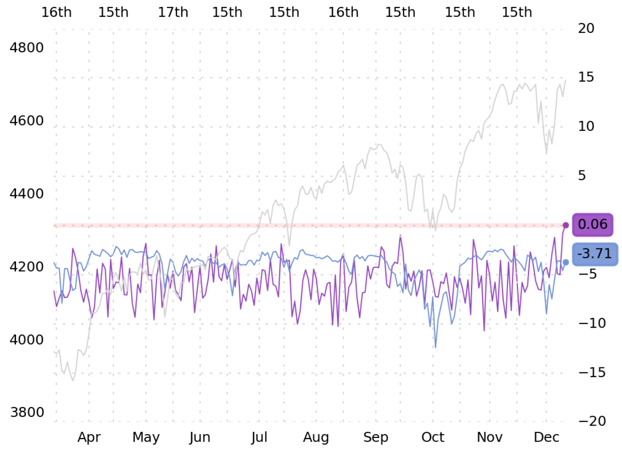


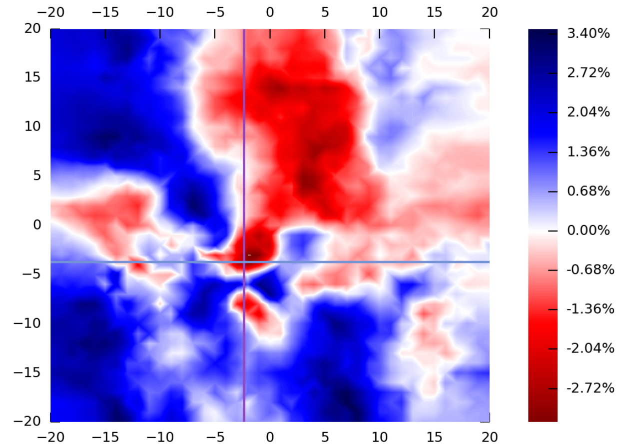
As you may recall, we are now long an ATM SPX call spread (since Thursday), with the thesis being that the left tail was suddenly a bit worrisome, but a gentle drift upward is still the most likely outcome for SPX. Not wanting that left tail exposure, we took on a bull vertical spread, because it's limited loss, and max gain occurs when there's a gentle drift up. Perfect.

And all that still applies. But the current circumstances deserve a bit more context than that.

2.
This, right now, is the most interesting data we've seen since 2020. Things are *churning* under the surface, and it is a wonder to behold.

Start with NPD/VGR.



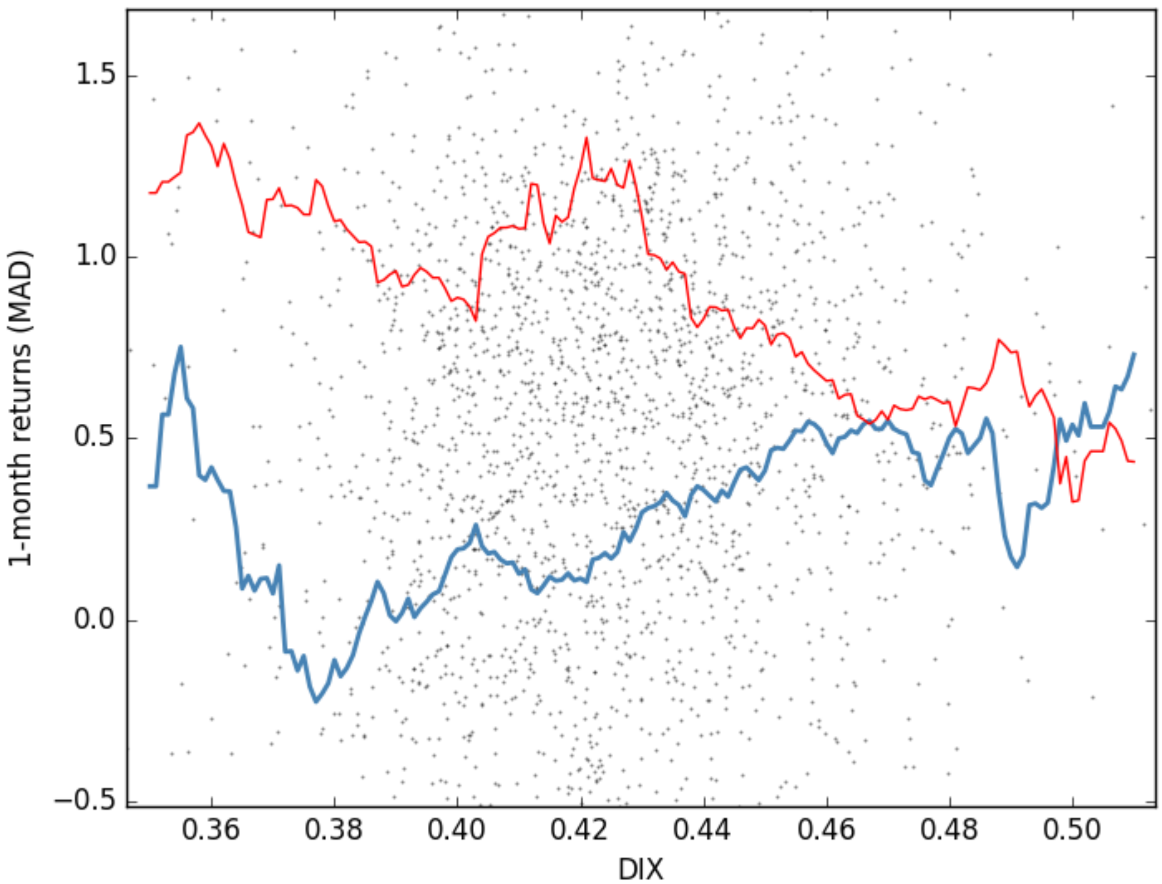


NPD was 0.06 on Friday. That means SPX puts were net *sold* (by the tiniest amount) in real dollar-delta terms. But more importantly, NPD near zero is the most reliable indicator of instability in the S&P 500 that we've ever seen. It means customers swapped deltas with each other, and that means dealers won't be expertly delta-hedging that newest crop of puts—which (by pushing the usual intermediary to the side) increases vol-of-vol, and makes liquidity less certain.

Nor was it just one bad day of NPD in isolation. Thursday was -0.79. Monday was -1.21. So in any case, there has also been a dearth of net put-buying in the market, which probably means that folks are under-hedged, and that the usual "vanna dynamics" of slowly decaying long customer put options (feeding long deltas, drip by drip, into SPX) really aren't present.

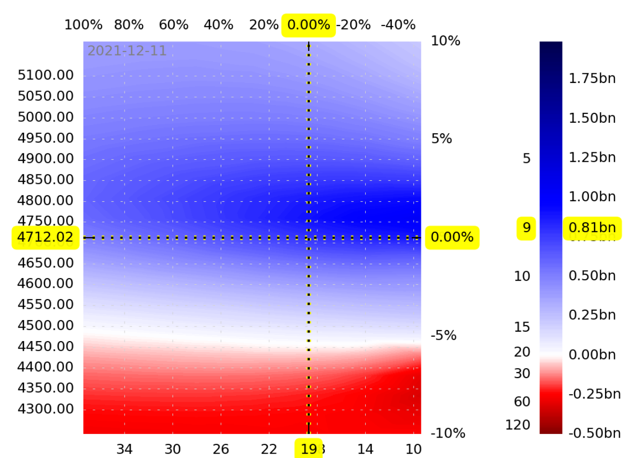
Yikes, right?

But what about DIX? *Three consecutive 45%+ prints!* That's some *hefty* buying going on in the index. Massive support. And it comes with a strong track record: Blue line is 1-month MAD return, red line is realized vol in the same terms.



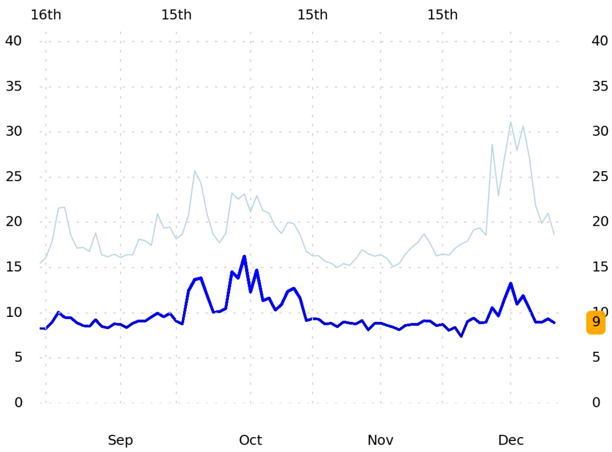
Realized gain of +0.5 MAD and realized vol of 0.5 MAD. That means, at this level of DIX, and with VIX at about 20, that SPX is expected to have a mean 1-month return of +2.30%, and realized volatility should be 10 over the period. *Solid.*

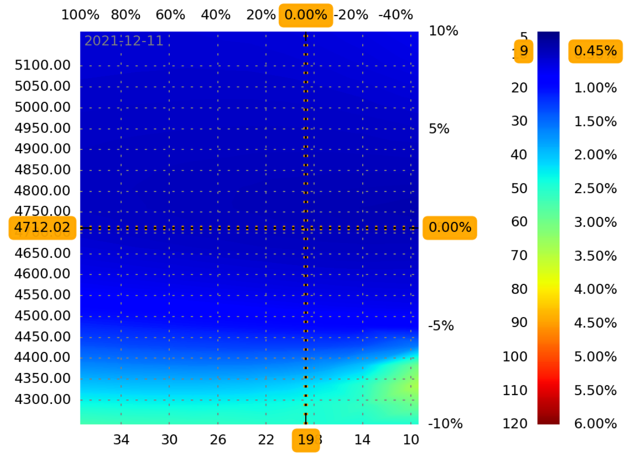
Confusing? Oh, but it gets worse.



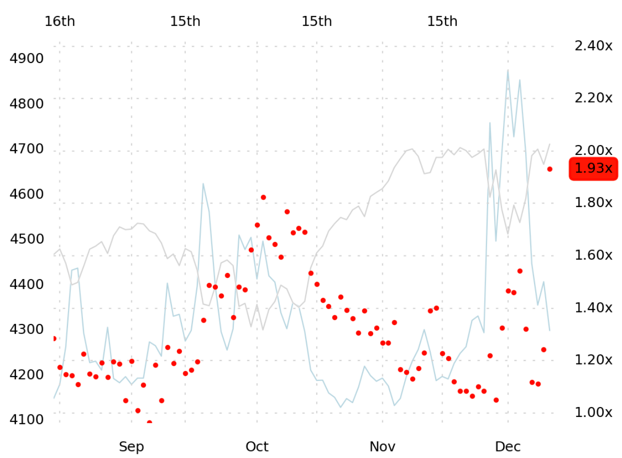
There's a solid red zone around 5% below spot where SPX dealers would stop stifling volatility and start adding to it. The red zone is where volatility self-sustains, and while it's not historically interesting to see it

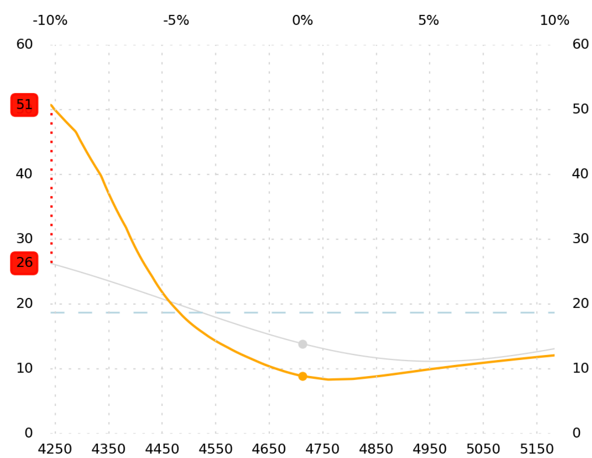
5% below spot (used to happen all the time), this map hasn't looked anything like this since before the Corona Crash.





On the GIV heatmap, you can see that a 10% decline in SPX would lead to *sustained* 50 vol (2.50% daily ranges, on average). That's the beginning of the green zone. And if we consult the *last* row of the Risk Report, we see that Crash Risk is now about 2.00x, which is closer to "normal" than we've seen—again—since March 2020, and that GIV *rapidly* rises if SPX falls below 4450.



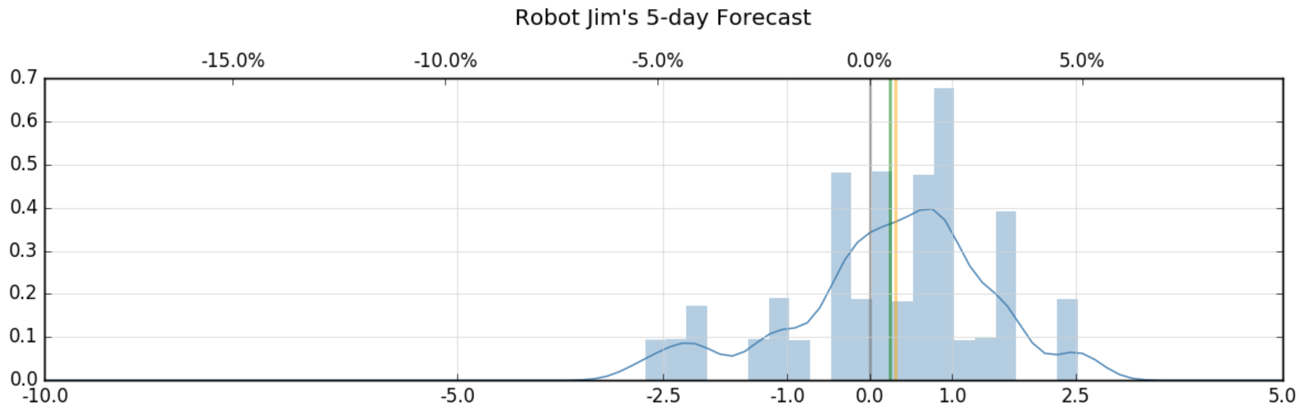


So, the Risk Report is telling us that, for the first time in a long time, some sustained tail risk has accumulated. This raises the stakes on whether it's DIX or NPD that's "right" about the current setup, because if NPD is right, there's actually the *tiniest* bit of crash risk out there.

How do we figure out "who's right," then?

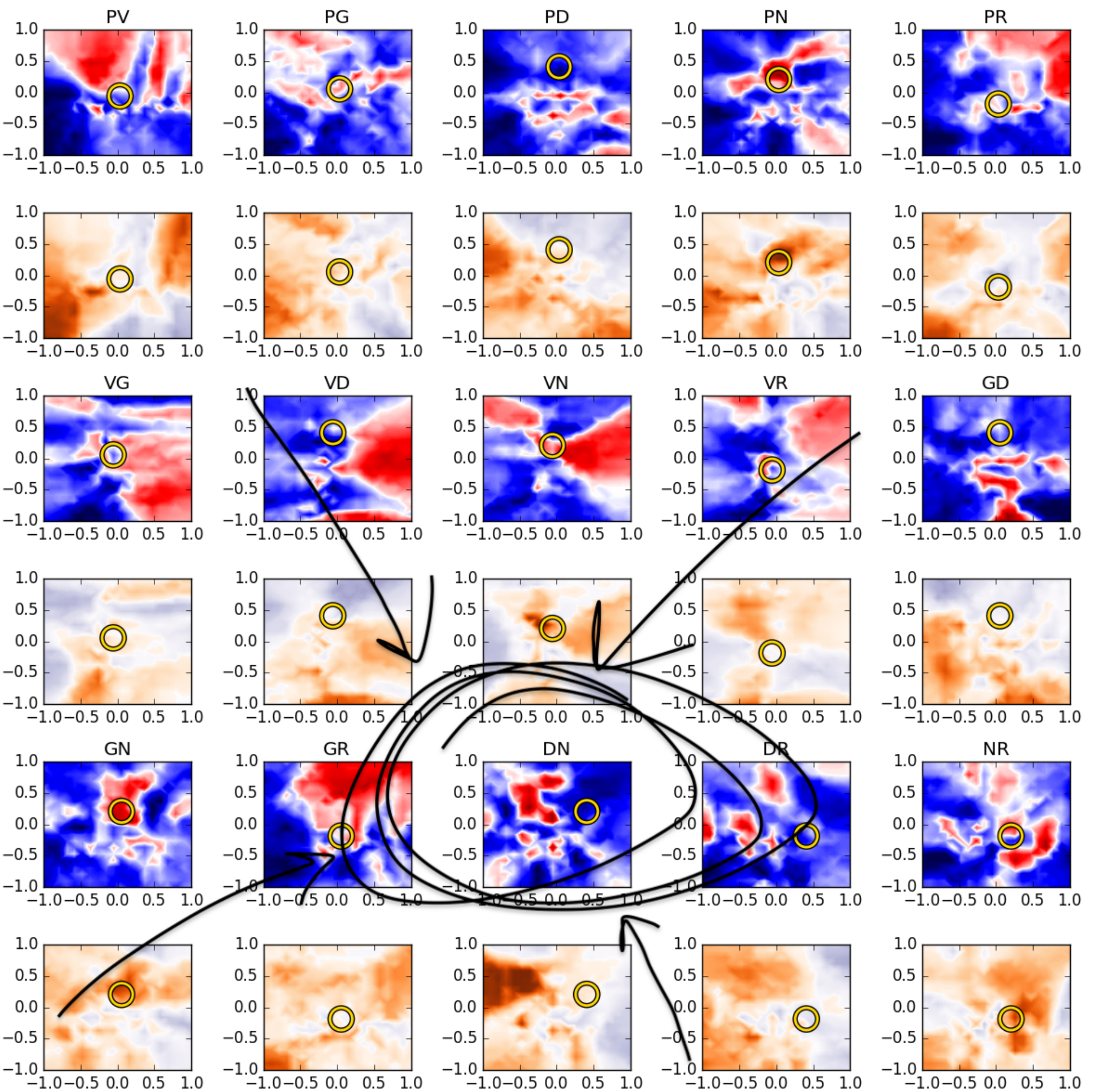
The best we can do for some context is to look at every historical event where DIX and NPD were "at odds" with each other, and GEX+ was positive, and VGR was pretty close to zero, etc. And then we can see how it worked out in the end.

This is a job for Robot Jim. What do you have for us, Jim?



That's it? Mean of +0.24 MAD, median of +0.43 MAD? The left isn't even any longer than the right tail...

So, how does Jim arrive at the conclusion that a good DIX and a bad NPD seem to mostly cancel each other out? Let's take a look at the weather maps ourselves!



The circled "DN" map is the DIX-to-NPD returns map. We're at the gold circle—deep blue. This means that, essentially, a high DIX has historically taken away the left tail risk of a near-zero NPD. If you imagine that DIX were just a bit lower (gold circle a bit further to the left), the story would be totally different—*but that's not the case right now.*

Apparently, the support from DIX is just that substantial. But perhaps you can understand why we'll be watching all of this very closely.

Still long the call spreads.

3.
Despite being distracted by this *utterly* fascinating past two weeks, and having produced no new Research—we have to admit we haven't *actually* been sitting fireside with a cup of hot chocolate. Rather, we've been

doing a bit of Development.

I.e., we've finally set in motion the plans to bring PIVT, the weather maps, and Jim, to the sqzme platform. Not only are we more convinced than ever that this is a spectacularly useful way to view our data—but really, it's about time that we finally pushed to get this out. This is the culmination of the "vol triangle" concept, married to all of our past research and made relevant for every NYSE and Nasdaq security. It's important. It's time to build it.

This means that, over the next couple weeks, the website is going to be changing. The data at the PIVT and JIM subdomains will be *replacing everything* currently on the platform. We'll be rolling out an API for programmatic access to that data. There will be spreadsheets for download, and PDF reports for every security. The charts will be replaced with something faster and lighter, to accommodate 10 years of historical data. The Research page will rank tickers by Jim's forecasts.

There's a *lot* to do, and it won't all happen at once. Nor will the legacy raw data stop updating. But expect changes to start appearing. Trust us—they'll be good.

Back to work.

Enjoy the week!

The SqueezeMetrics Team