From: Richard Kahn <richardkahn12@gmail.com>
To: "jeffrey E." <jeevacation@gmail.com>
Subject: Fwd: Derivatives not priced for a bond-equity melt up or tantrum, making hedging cheap
Date: Tue, 19 Jul 2016 16:29:42 +0000
Inline-Images: image001gif01D1E1A4D4978140.gif; image009jpg01D1E147FE917C10.jpg; image012jpg01D1E147FE917C10.jpg; image016jpg01D1E147FE917C10.jpg; image028png01D1E147FE917C10.png; image004png01D1E18AFACCFE90.png

---

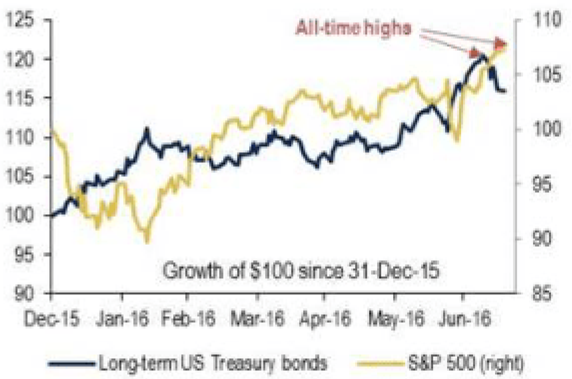
in process of setting up account with amanda ens at investment bank now
would you like to see these emails or shall i just have amanda send trade ideas?
please advise
thank you

Richard Kahn
HBRK Associates Inc.
575 Lexington Avenue 4th Floor
New York, NY 10022
tel [redacted]
fax
cel

Begin forwarded message:

From: "Ens, Amanda" <[redacted]
Subject: Derivatives not priced for a bond-equity melt up or tantrum, making hedging cheap
Date: July 19, 2016 at 10:07:27 AM EDT
To: "Rich Kahn"<[redacted]
Reply-To: "Ens, Amanda[redacted]

Highlights from this week's Global Equity Volatility Insights



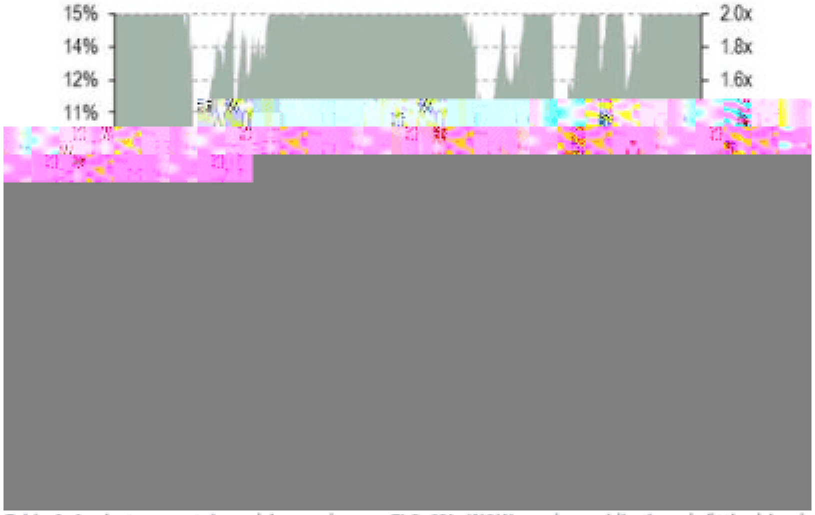
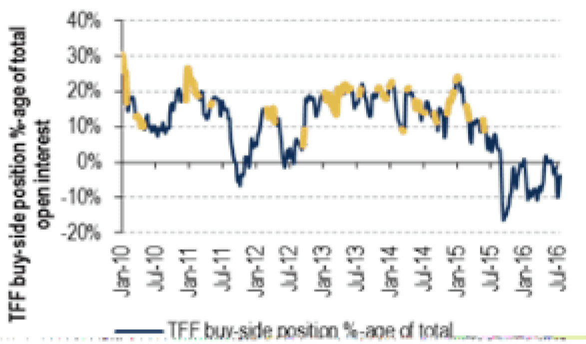


Table 1: Analysts expect downside surprises on TLS, CSL, WOW earnings while there is little risk pricedin in the option market vs. historical earnings moves

Symbol	Name	Expected Report Date	Aug Vol	Sep Vol	Option Implied Move	Past 4 Earnings Avg Moves	30-day Realized Vol	BofAML Rating	Analyst Expected Surprise	Scope for Surprise
RIO AU	RIO TINTO LTD	03/08/2016	31.4%	30.6%	2.7%	1.5%	35.3%	Underperform	Upside	Renewed focus on cost
CBA AU	COMMONW BK	10/08/2016	19.8%	19.5%	1.0%	0.8%	21.0%	Buy		
AGL AU	AGL ENERGY	10/08/2016	20.0%	19.4%	2.5%	1.8%	16.9%	Neutral		
TLS AU	**TELSTRA**	**11/08/2016**	**14.6%**	**14.3%**	**0.4%**	**1.5%**	**15.8%**	**Buy**	**Downside**	**Higher cost re-investment**
NCM AU	**NEWCREST**	**15/08/2016**	**46.0%**	**45.6%**	**2.8%**	**4.6%**	**45.3%**	**Buy**	**Upside**	**Upside to FY16 Production**
BHP AU	**BHP BILLITON**	**16/08/2016**	**35.8%**	**36.8%**	**--**	**2.2%**	**43.3%**	**Buy**	**Upside**	**Upside on Petroleum Production**
CSL AU	**CSL**	**17/08/2016**	**20.9%**	**20.5%**	**1.6%**	**3.6%**	**20.5%**	**Neutral**	**Downside**	**Margin pressure from lower US demand**
QBE AU	QBE	17/08/2016	30.5%	27.5%	5.1%	2.3%	35.8%	Underperform		
ASX AU	ASX	18/08/2016	18.5%	18.4%	0.4%	1.1%	18.0%	Underperform		
WPL AU	WOODSIDE	19/08/2016	28.3%	27.0%	3.4%	1.5%	28.7%	Buy		
STO AU	SANTOS	19/08/2016	40.4%	39.3%	3.4%	2.7%	51.1%	Buy	Upside	Aggressive cost reduction
FMG AU	FORTESCUE	22/08/2016	59.2%	57.3%	4.8%	6.4%	61.4%	Underperform	Upside	Potential further reduction in Cost
WES AU	WESFARMERS	24/08/2016	21.2%	20.7%	1.7%	1.8%	18.6%	Underperform	Downside	Dividend pullback
WFD AU	WESTFIELD	24/08/2016	23.2%	22.4%	2.0%	0.6%	23.3%	Underperform	Downside	Guidance impacted by weak GBP

Source: BofA Merrill Lynch Global Research



Click for full report

US: Derivatives not priced for a bond-equity melt up or tantrum, making hedging cheap

- Both US equities and long-dated US Treasuries recently touched all-time highs, with the S&P 500 +7% YTD and TLT (US 20+ Year Treasury Bonds) up 16% on a total return basis [Chart 1]
- Despite this, bond-equity realized correlation remains strongly negative and is near 3yr lows, creating attractive entry points for directional long correlation trades [Chart 2]
- For example, a 6M ATM best-of put on SPX & TLT costs ~0.8% (82.5% discount to the average vanilla put) and could serve as a cheap hedge against an inflation shock or hawkish reversal in Fed rate hike expectations, both potentially amplified by risk parity unwinds from max leverage
- Alternatively, equity investors who anticipate continued bond outperformance can substantially cheapen longer-dated equity calls via 1Y ATM worst-of calls on SPX & TLT (~0.9%, 83.5% cheaper than a vanilla SPX 1Y ATM call)

Both US equities and long-dated Treasuries recently hit all-time highs, with YTD total returns of 7% for the S&P and 16% for TLT

Source: BofA Merrill Lynch Global Research. Daily data from 31-Dec-15 through 18-Jul-16. Total returns of TLT and SPX.

However, bond-equity realized correlation has fallen to near 3yr lows as Treasuries have diversified equities well this year

Source: BofA Merrill Lynch Global Research. Daily data from 15-Jul-13 through 18-Jul-16. US 20+ Year Treasuries are represented by TLT.

Volatility of risk parity portfolios has come in this year as cross-asset performance has been diversified YTD—as a result, risk parity leverage has remained elevated

Source: BofA Merrill Lynch Global Research. Daily data from 15-Jul-15 to 18-Jul-16.

Source: BofA Merrill Lynch Global Research. Daily data from 15-Jul-15 to 18-Jul-16.

Europe: Cheap upside in laggard stocks with bearish positioning

Buy Oct16 ~110%F calls on VIE FP, STAN LN, AI FP, IBE SQ and MUV2 GY for an average price of 2.37% (ref €19.39, €96.03, €6.02, £6.087 and €148.7 respectively):

- The 5 names screen as the most attractive candidates based on (table):
  - **Stock underperformance relative to their sector since the Brexit vote**: they have lagged their sectors in the post-Brexit vote rebound from 27-Jun through 15-Jul
  - **Cheap calls**: YTD percentile of 3M 25d call prices (as of 15-Jul) is low
  - **Bearish stock positioning**: short open interest is high vs. other stocks in our list, suggesting the stocks may outperform in a potential market squeeze higher.
- Air Liquide (AI FP) screens inexpensive in our earnings implied move ranking (table in next section)
- **Light exotic implementation**: Oct16 110%F call on an equally wt basket (qEUR) costs 0.81% indic. (correl = 64%), 66% discount vs. avg single stock calls

Top 20 candidates for inexpensive upside potential: Veolia (VIE FP), Standard Chartered (STAN LN), Air Liquid (AI FP), Iberdrola (IBE SQ) and Munich Re (MUV2 GY) stand out

Ticker	Sector	Stock performance (since 27-Jun)	Sector performance (since 27-Jun)	Out(+)/Under(-) performance	Short open interest*	3M 25d call price	3M 25d call price (YTD percentile)	Underperformance rank	Short Open interest rank	Option price rank	Overall rank**
VIE FP	Utilities (SX6P)	7.1%	11.3%	-4.1%	1.3%	1.5%	2.7%	7	38	16	**1**
STAN LN	Banks (SX7P)	13.1%	10.6%	2.5%	4.5%	2.4%	0.2%	55	8	5	**2**
AI FP	Chemicals (SX4P)	8.1%	8.8%	-0.7%	1.7%	1.4%	0.2%	35	28	5	**3**
IBE SQ	Utilities (SX6P)	7.7%	11.3%	-3.6%	1.3%	1.3%	3.9%	8	39	21	**4**
MUV2 GY	Insurance (SXIP)	3.1%	8.0%	-4.9%	1.6%	1.4%	14.1%	5	31	37	**5**
ABBN VX	Industrials (SXNP)	3.5%	10.2%	-6.7%	1.2%	1.4%	13.9%	3	41	36	6
SAND SS	Industrials (SXNP)	11.9%	10.2%	1.7%	5.6%	1.7%	7.1%	52	4	24	7
ASML NA	Technology (SX8P)	10.2%	10.6%	-0.4%	1.5%	1.7%	0.4%	37	34	9	8
ITX SQ	Retail (SXRP)	8.1%	9.5%	-1.4%	0.9%	1.5%	0.0%	29	57	1	9
TSCO LN	Retail (SXRP)	7.5%	9.5%	-2.1%	6.0%	2.2%	47.5%	18	2	67	10
BMW GY	Autos (SXAP)	13.7%	9.7%	4.0%	3.1%	1.8%	0.6%	61	15	12	11
AAL LN	Basic Resources (SXPP)	32.1%	20.2%	11.9%	5.8%	3.3%	0.4%	77	3	9	12
AGN NA	Insurance (SXIP)	-4.2%	8.0%	-12.2%	3.4%	2.7%	75.0%	1	13	75	13
RDSA NA	Oil & Gas (SXEP)	7.7%	10.7%	-3.0%	0.6%	1.4%	0.6%	11	66	12	14
HMB SS	Retail (SXRP)	9.7%	9.5%	0.2%	4.9%	1.5%	16.1%	42	6	41	15
SAN FP	Health Care (SXDP)	7.4%	7.9%	-0.5%	1.4%	1.5%	3.2%	36	36	18	16
AIR FP	Industrials (SXNP)	5.4%	10.2%	-4.8%	1.4%	2.0%	19.4%	6	37	47	17
IFX GY	Technology (SX8P)	9.8%	10.6%	-0.9%	4.4%	2.2%	19.9%	33	9	48	18
DBK GY	Banks (SX7P)	3.8%	10.6%	-6.8%	3.1%	2.9%	73.0%	2	16	73	19
KPN NA	Telecom (SXKP)	7.8%	9.4%	-1.7%	4.3%	1.9%	35.8%	23	10	58	20

Source: BofA Merrill Lynch Global Research, Markit. Stock and sector performance data from 27-Jun to 15-Jul. 3M 25d call prices as of 15-Jul (percentile using data since 4-Jan-16). **Overall rank based on an (equally weighted) average of Underperformance rank, Short open interest rank and Option price rank. *Short open interest is an average of net stock lending by brokers as a percentage of free float market cap calculated by Markit. This is a screen and not a recommended list either individually or as a group of stocks. Investors should consider the fundamentals of the companies and their own individual circumstances / objectives before making any investment decisions.

Asia Pacific: Screen for AU stock options to capture earnings surprises

- Buy TLS, CSL Aug-16 puts to hedge potential earning downside surprise
- Buy NCM, BHP Aug-16 call spreads to hedge potential earnings upside surprises
- Indicative pricing (As of 18-Jul-16):
  - Buy Telstra 25-Aug-16 95% puts: 1.05% (iv: 17.1%, -31d)
  - Buy CSL 25-Aug-16 95% puts: 1.09% (iv: 23.3%, -23d)
  - Buy Newcrest 25-Aug-16 105/115% call spreads: 2.64% (iv: 46.2%/44.6%, 21d)
  - Buy BHP 25-Aug-16 105/115% call spreads: 2.22% (iv: 35.2%/32.7%, 26d)

Week in Review: US equity vol has declined towards its 1yr lows as the S&P made new highs

- SPX 1M straddles are currently the most attractive in terms of break-even probability among many global major indices, breaking even 79% of the time over the past 3 yrs at current pricing **[Chart 1]**
- The current net 'buy-side' positioning as a %-age of net positioning is the most bearish as inferred by e-mini futures since 2010 for which the S&P500 hit a relative and/or all-time high at **[Chart 2]**
- Last week, the front end of the VIX futures term structure steepened last week to near its 4yr steepest levels partly due to net vega in VIX ETP products grew $34.5 mn over the week **[Chart 3]**
- The recent post-Brexit rally in US equities coincided with the sharpest flattening in SPX 3m 90-110 skew ever recorded over the past 10 yrs with the move uniquely driven by call skew **[Chart 4]**

1M ATM straddles on the S&P500 screen the most attractive among major indices globally, as they would have broken even 92% of the time over the past year at current pricing

			Break-even probability		
Index	1M straddle cost	IV	Last 1Y	Last 2Y	Last 3Y
SPX	2.3%	9.8%	91.8%	81.5%	79.0%
HSCEI	5.1%	21.1%	87.9%	76.3%	71.9%
AS51	3.2%	13.8%	84.4%	70.8%	61.6%
HSI	4.2%	17.7%	83.6%	69.2%	64.0%
TWSE	3.4%	13.2%	83.3%	69.7%	60.5%
KOSPI2	2.8%	11.9%	78.1%	71.1%	71.6%
NIFTY	3.4%	14.0%	72.6%	71.6%	73.6%
NKY	6.2%	26.2%	71.8%	50.3%	47.0%

S&P500 at all-time highs but net 'buy-side' positioning still looks bearish