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October 26, 2022

Nasdaq

Another October Bottom?

Kevin Davitt

Head of Index Options

Content

Nasdaq

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Another October Bottom? When Will the “Bear Market” End?

Interactive Brokers

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Nasdaq

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Before transacting in VOLQ options, market participants should fully inform themselves about the Nasdaq-100 Volatility Index and the characteristics and risks of VOLQ Options. Market participants also should make sure they understand the product specifications for VOLQ Options and the methodologies for calculating and settling the Nasdaq-100 Volatility Index.



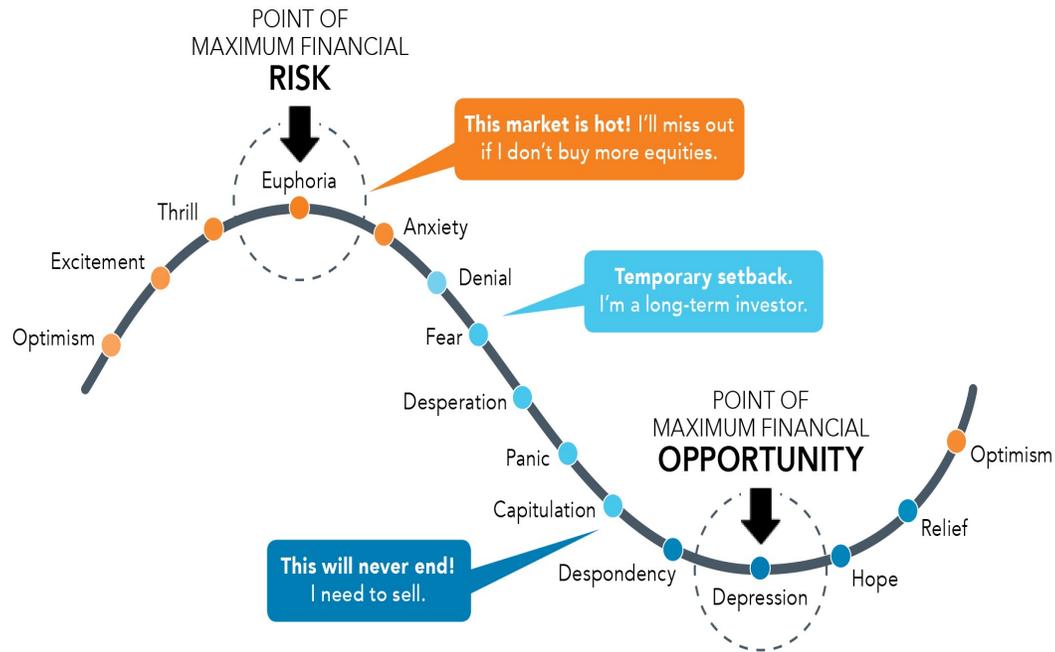
October Bottom?

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October Bottom?

Where Are We Now?



Source: CDSPI

"Waiting for the bottom is folly. What, then should be the investor's criteria? The answer is simple: if something is cheap – based on the relationship between price and intrinsic value – you should buy, and if it cheapens further, you should buy more"

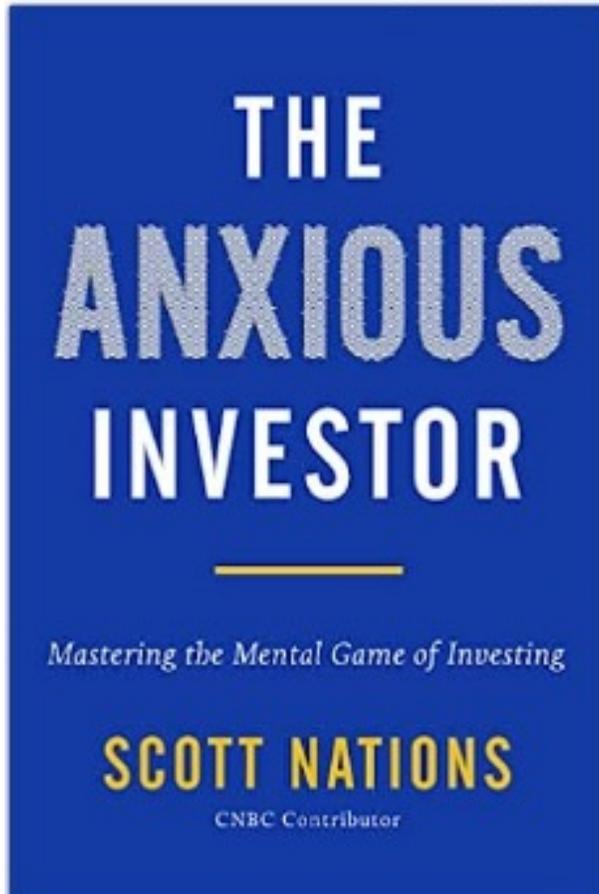


- Howard Marks

- Bull Markets “Climb a Wall of Worry”
 - Countless obstacles overcome since 2009/2011:
 - Greece/End of QE, Ebola, Brexit, Chinese devaluation, North Korea, Trade war, etc.
- Bear Markets “Slide down a Slope of Hope”
 - Current hopes:
 - Corporate earnings stronger
 - Inflation measures fall
 - FOMC “pivot”
 - Russia/Ukraine resolution

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Where Are We Now?



Source: Scott Nations

“The best thing to do in the midst of market turmoil like this is to take a deep breath and embrace an adage that generally associated with the practice of medicine, ‘First do no harm’. Regardless of how long it’s been since we’ve had some sort of gut-wrenching, insomnia inducing market turmoil, one thing will remain constant: when it comes to your portfolio, the most dangerous element during the next stock market crash is likely to be you.”

- **Scott Nations**

On Capitulation: “I’ve always had two conflicting opinions. One, it’s like Potter Stewart’s definition of pornography: ‘I can’t define it, but I know when I see it’. And two, it’s only obvious in retrospect.”

- **Scott Nations**



October Bottom?

The Strength of the U.S. Dollar: A Real Concern

Exhibit 3: US Dollar Y/Y Change Is at a Level That Usually Leads to Financial/Economic Stress



Source: Bloomberg, Morgan Stanley Research

- U.S. is arguably the “cleanest shirt in the laundry”
 - U.S. economy is strong relative to European/Asian/EM economies.
 - The Federal Reserve raising rates more/quickly than other central banks.
 - USD is the global reserve currency.
- In 2008/2009 & 2020 (Q1) U.S. equity markets bounced as USD reached its zenith
- G20 Meeting Nov. 15/16
 - Relative strength of USD likely topic of discussion.

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Past Performance is Not Indicative of Future Results!

October 13th NDX Made Lower Lows

When the Nasdaq is Down 30% or Worse Since 1971

Peak	Trough	% Decline	+1 Year	+3 Years	+5 Years	+10 Years
1/11/1973	10/3/1974	-59.9%	29.1%	80.2%	170.6%	438.7%
6/24/1983	7/25/1984	-31.5%	25.6%	87.1%	99.6%	246.0%
8/26/1987	10/28/1987	-35.9%	20.7%	8.5%	104.5%	454.8%
10/9/1989	10/16/1990	-33.0%	67.1%	144.8%	230.1%	992.4%
3/10/2000	10/9/2002	-77.9%	-44.7%	-60.8%	-48.1%	-32.9%
10/31/2007	3/9/2009	-55.6%	-1.2%	14.5%	85.2%	318.7%
2/19/2020	3/23/2020	-30.1%	73.4%	???	???	???
1/3/2022	9/30/2022	-34.1%	???	???	???	???
Averages		-44.8%	24.3%	45.7%	107.0%	403.0%

?



October Bottom?

Past Performance is Not Indicative of Future Results!

Generally – U.S. Equities Higher During “Holiday Season”



Source: Zerohedge



October Bottom?

(2010 – 2021) NDX Oct Avg: +2.79%; NOV +2.04%; Dec +0.50%
 2018: Outlier Following Chinese Deval (Global Deflation)

^NDX Monthly Returns Heatmap

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2022	-9.12%	-4.64%	4.22%	-13.37%	-1.65%	-9.00%	12.55%	-5.22%	-10.60%	-1.69%		
2021	0.29%	-0.12%	1.41%	5.88%	-1.26%	6.34%	2.78%	4.16%	-5.73%	7.90%	1.80%	1.82%
2020	2.96%	-5.89%	-7.66%	15.19%	6.17%	6.29%	7.37%	11.05%	-5.72%	-3.20%	11.00%	5.05%
2019	9.11%	2.76%	3.96%	5.46%	-8.40%	7.62%	2.32%	-2.01%	0.76%	4.31%	3.96%	3.92%
2018	8.65%	-1.38%	-3.99%	0.37%	5.48%	1.05%	2.72%	5.84%	-0.35%	-8.66%	-0.26%	-8.91%
2017	5.20%	4.17%	1.99%	2.71%	3.68%	-2.45%	4.13%	1.84%	-0.16%	4.50%	1.87%	0.48%
2016	-6.84%	-1.82%	6.73%	-3.17%	4.21%	-2.35%	7.07%	0.86%	2.19%	-1.53%	0.20%	1.10%
2015	-2.07%	7.04%	-2.41%	1.86%	2.13%	-2.47%	4.37%	-6.85%	-2.19%	11.19%	0.34%	-1.53%
2014	-1.95%	4.95%	-2.72%	-0.38%	4.32%	3.01%	1.12%	4.88%	-0.81%	2.69%	4.32%	-2.34%
2013	2.65%	0.26%	2.93%	2.44%	3.27%	-2.42%	6.21%	-0.53%	4.70%	4.96%	3.26%	2.99%
2012	8.35%	6.29%	5.04%	-1.15%	-7.30%	3.60%	1.02%	4.91%	0.97%	-5.40%	1.13%	-0.63%
2011	2.89%	3.03%	-0.51%	2.78%	-1.31%	-2.00%	1.62%	-5.15%	-4.54%	10.33%	-2.75%	-0.76%
2010	-7.72%	4.46%	7.68%	2.16%	-7.41%	-6.11%	7.18%	-5.18%	13.05%	6.33%	-0.34%	4.75%

USD STRENGTH



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The Strength of the U.S. Dollar: A Real Concern

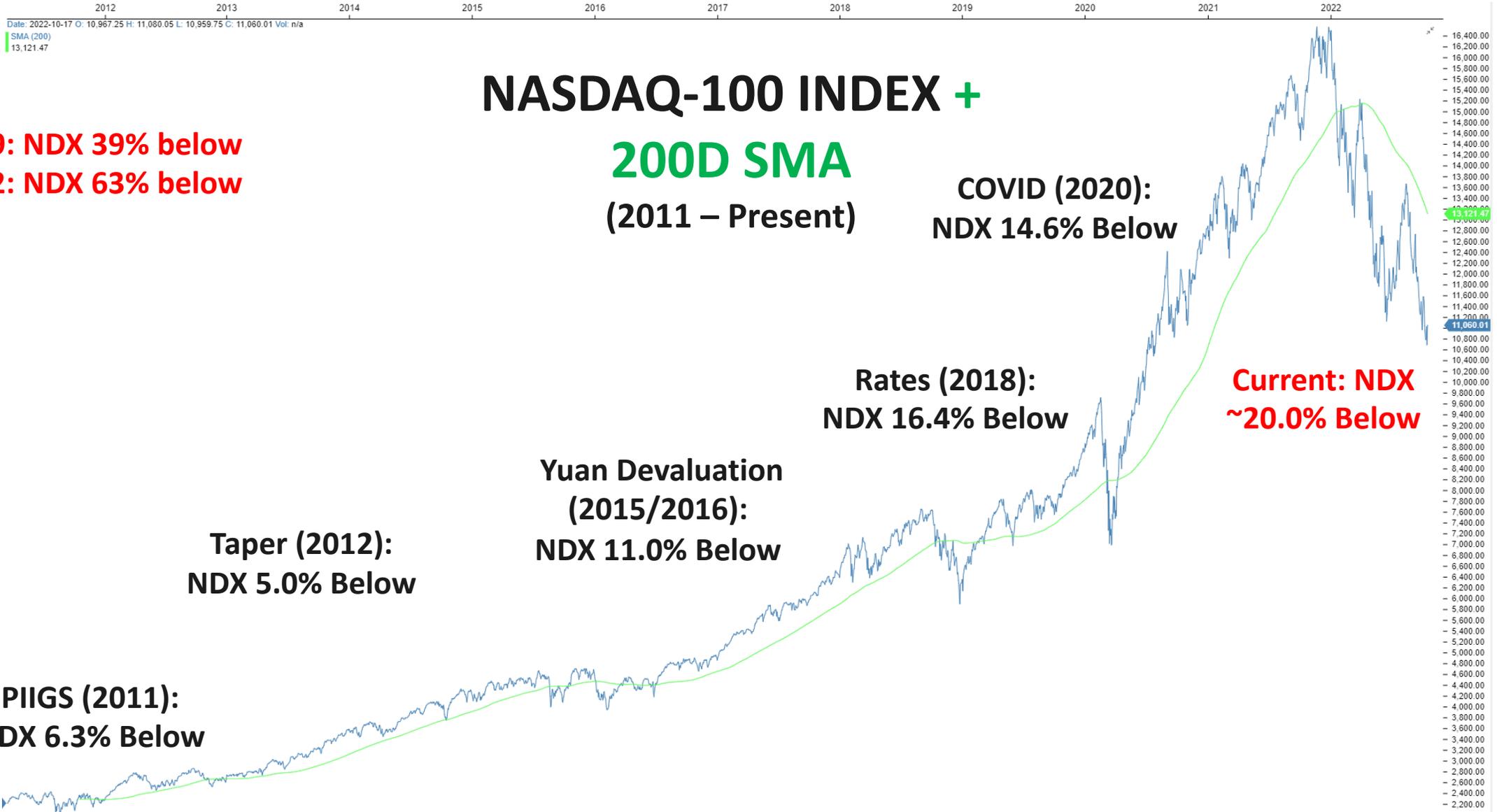


- Mid October ~15% of S&P 500 Index components are above their 200D SMA.
 - Long-term trends broken lower.
- Since GFC – rare to see readings this low.
 - AAPL: ~13% below
 - MSFT: ~19% below
 - AMZN: ~21% below
 - TSLA: ~28% below
 - GOOG: ~22% below
 - META: ~37% below
 - NVDA: ~43% below
 - PEP: ~4.7% below (pre-earnings)
 - COST: ~12% below

Source: Trading View



October Bottom?



2009: NDX 39% below
2002: NDX 63% below

NASDAQ-100 INDEX +
200D SMA
(2011 – Present)

COVID (2020):
NDX 14.6% Below

Rates (2018):
NDX 16.4% Below

Current: NDX
~20.0% Below

Yuan Devaluation
(2015/2016):
NDX 11.0% Below

Taper (2012):
NDX 5.0% Below

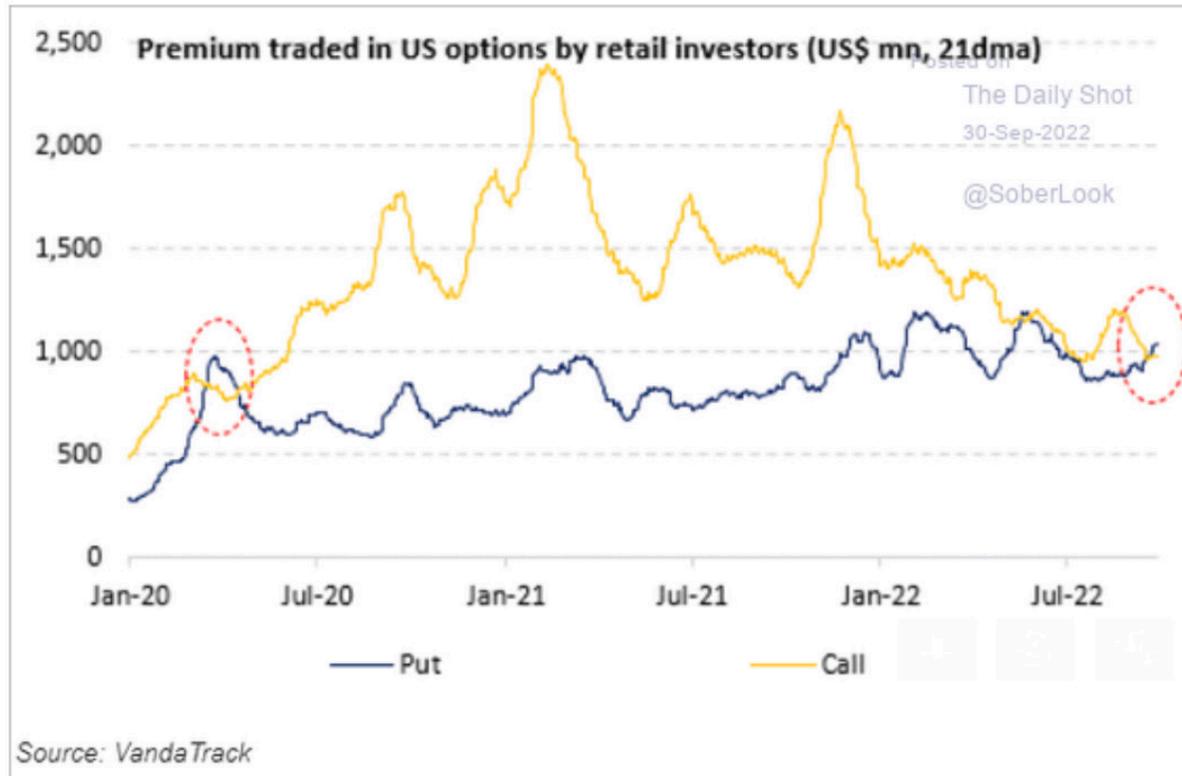
PIIGS (2011):
NDX 6.3% Below



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Put Premiums > Call Premiums Lately

Retail investors' put options have now exceeded calls, as they did in early 2020.



Source: [Vanda Research](#)

- Options volume have grown exponentially over the past three years.
 - 40+ million in ADV YTD
 - 2022 likely to be highest options volume in history
- Ratio of call premium relative to put premium declined over past year.
 - Don't make too much of single data points
 - The options data from past 3 years arguably has no comparison
 - Single stock option volumes have declined in 2022
 - Index (including EFT) option volumes have increased in 2022

Source: Vanda & The Daily Shot



October Bottom?

Put Premiums in “Perspective”



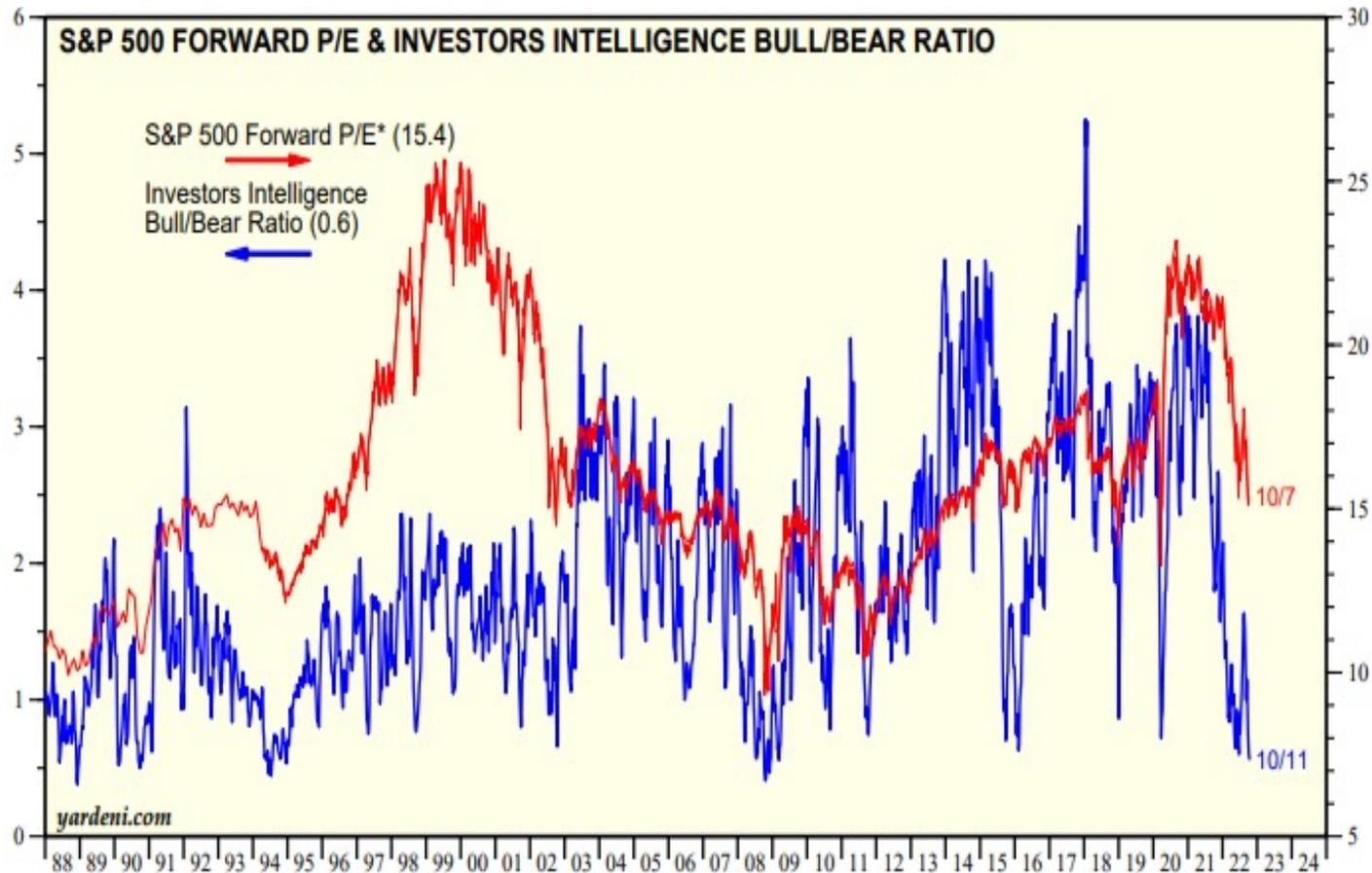
Source: Sentiment Trader

- When volatility (realized and implied) increases, option premiums increase (all else equal).
 - IV + impacts calls and puts in the same direction
- VOLQ Index is a measure of forward volatility expectations based on at-the-money NDX options.
 - Arguably more focused Volatility metric (not impacted by SKEW).
 - There are tradeable VOLQ futures (VLQ) and options (VOLQ) with a 3-month term structure



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Bearish Sentiment + Improved Valuations



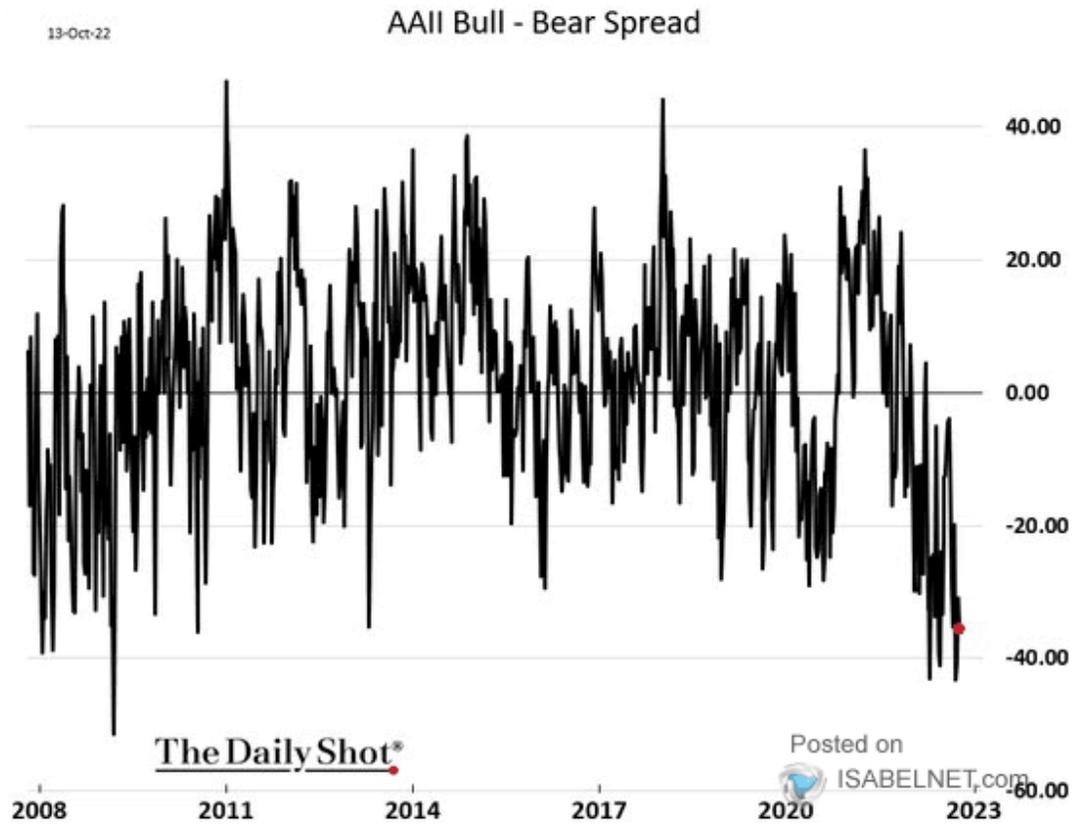
- IF forward earnings estimates are correct...
 - Then US equity valuations are much closer to longer-term trend again
 - However, earnings estimates could suffer
- Bull/Bear ratio near extremes
 - Data comes from weekly AAI survey data
 - Rarely does the ratio fall below 1.0
 - Recently near 2008/2009 lows

Source: Yardeni Research

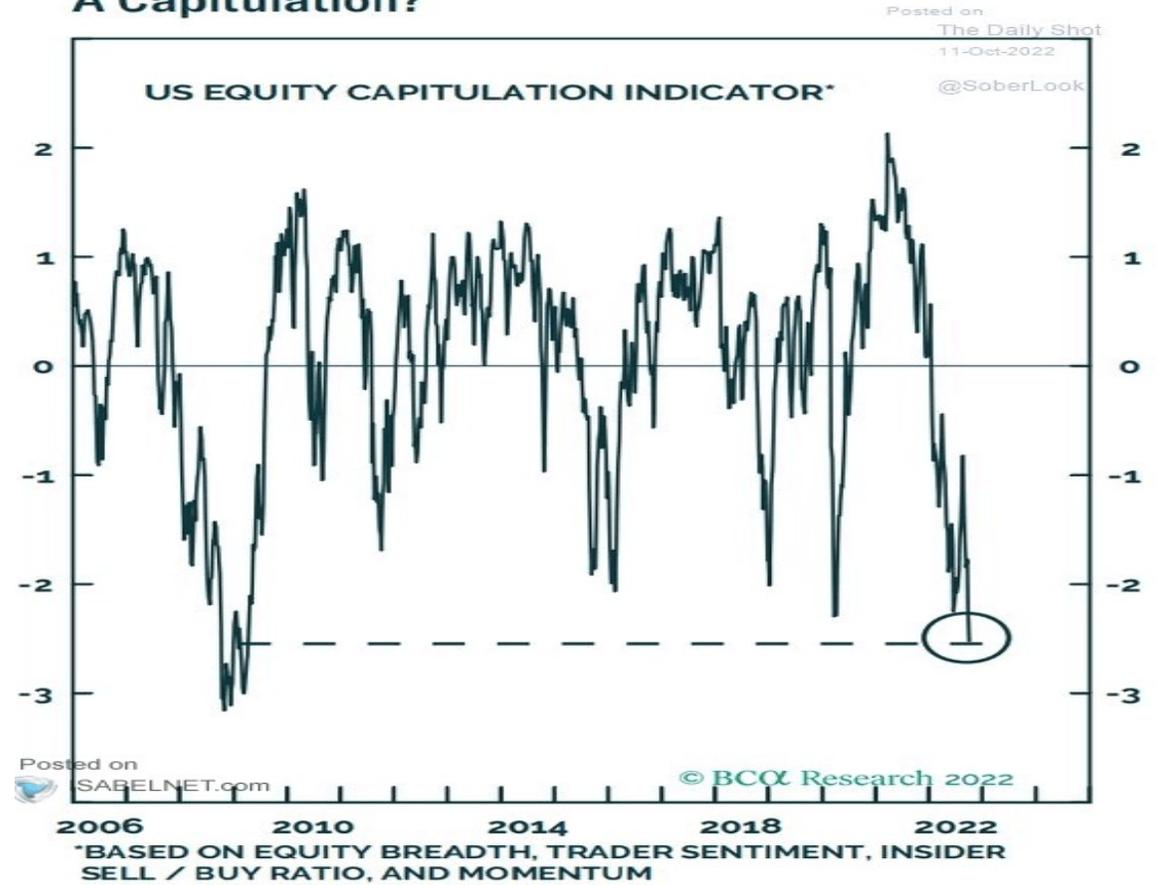


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Similar Data – Another View



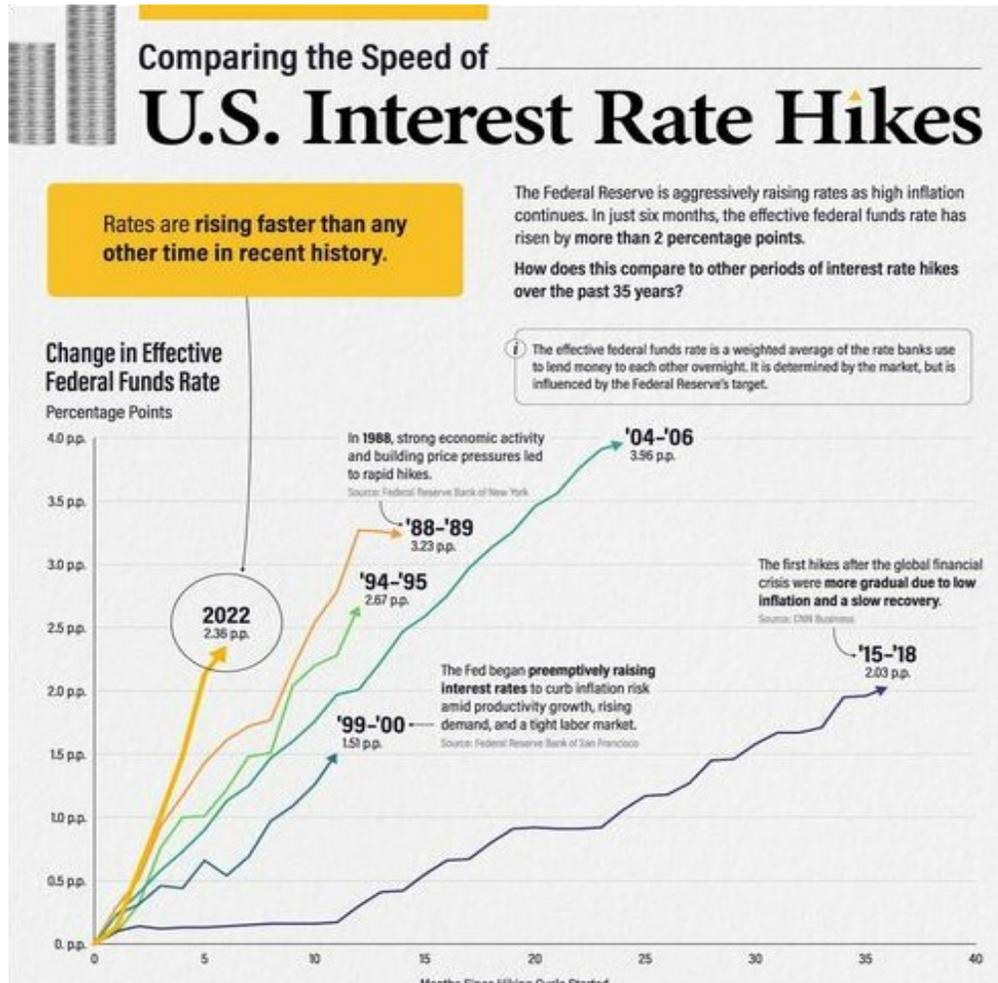
A Capitulation?



Source: Daily Shot & Isabel.Net

October Bottom?

The Interest in Rates!



- The \$64 trillion question:
 - When will the Fed pause/pivot?
 - What will the full impact of higher rates be when that occurs?
 - Ex: Housing ~18% US GDP
- In fairness...
 - The “zero-bound” rate environment of the past decade is without historical precedent.
 - Current Fed Funds rate: 3.0 – 3.25%
 - FOMC meetings: 11/2, 12/14
 - Terminal Rates forecast:
 - 4.40% EOY
 - 4.6% 2023

Source: Visual Capitalist



October Bottom?

A History of October Bottoms... (Nasdaq Composite)



- Overall:
 - 12 of 14 post WWII bear markets ended in October
 - 8 of the 12 preceded mid-term elections
- 1974 example:
 - Followed energy crisis (inflation) and preceded mid-terms
 - Bear market lasted 21 months
 - U.S. Indexes fell ~48% in total
- 1978 example:
 - Further inflationary pressure, interest rates spiked, mid-term election cycle

Source: Yahoo Finance



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A History of October Bottoms... (Nasdaq Composite)



- 1987 example:
 - “Black Monday”
 - Portfolio insurance (complexity)
 - Leverage and legislation
 - Only a 3-month bear market (34% decline)
- 1990 example:
 - Mid-term elections
 - Nasdaq Comp declined by 31%
 - Very slow housing market.
 - Another short (3M) bear market

Source: Yahoo Finance



October Bottom?

A History of October Bottoms... (Nasdaq Composite)



- 1998 example:
 - Mid-term elections
 - Russian default
 - LTCM Bailout
 - Asian Tigers (currency issues)
- 2002 example:
 - Mid-term elections
 - Nasdaq Comp declined by ~78% during Dot Com implosion
 - Reversed ~6 years of previous gains
 - The “scariest” comparison?

Source: Yahoo Finance



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The S&P 500 Index View:

S&P 500 Bear Market Bottoms Since WWII

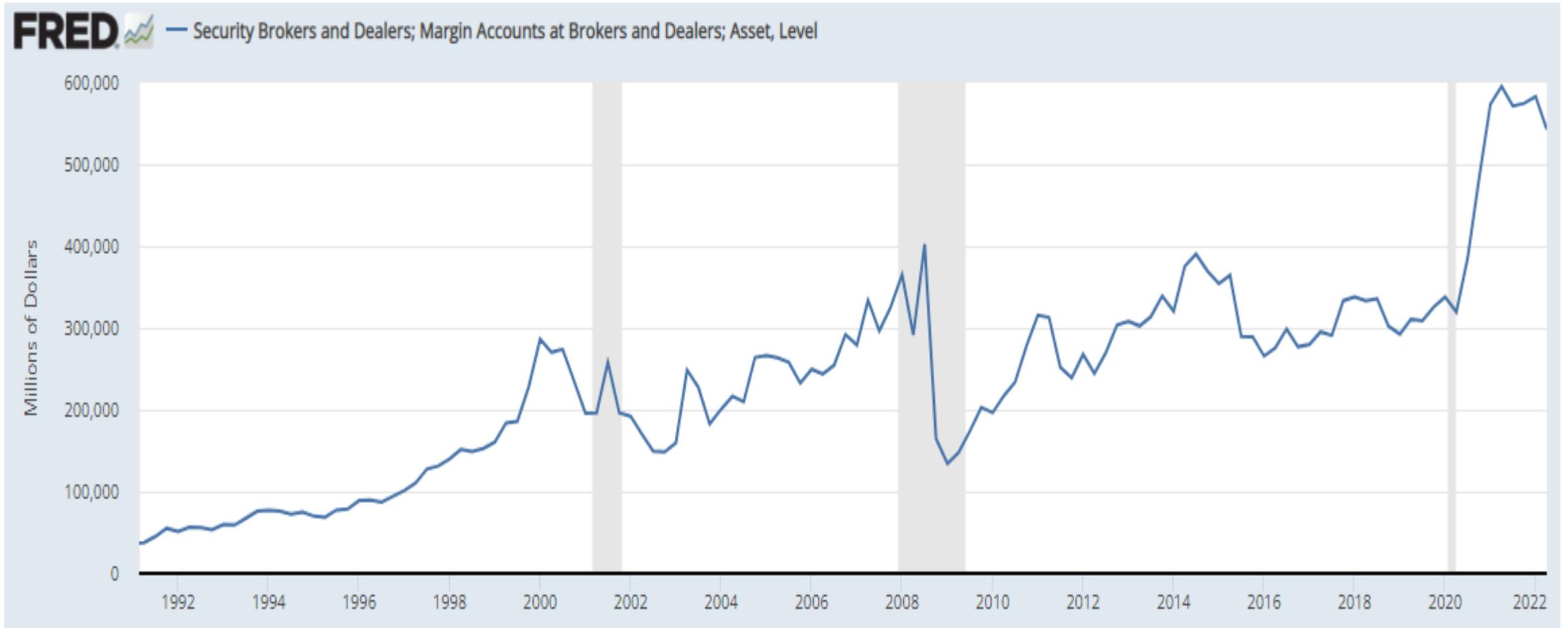
Peak	Trough	% Decline	10 Year Yield	CAPE Ratio	Inflation Rate	Dividend Yield
5/29/1946	10/9/1946	-26.6%	2.3%	14.4	14.9%	4.0%
6/15/1948	6/13/1949	-20.6%	2.3%	9.1	3.3%	7.3%
7/15/1957	10/22/1957	-20.7%	2.8%	12.1	2.9%	5.9%
12/12/1961	6/26/1962	-28.0%	3.9%	16.8	1.3%	3.7%
2/9/1966	10/7/1966	-22.2%	5.0%	18.8	3.8%	3.7%
11/29/1968	5/26/1970	-36.1%	7.9%	14.0	6.0%	4.2%
1/11/1973	10/3/1974	-48.2%	7.9%	8.7	12.1%	5.2%
11/28/1980	8/12/1982	-27.1%	13.1%	6.6	5.9%	6.2%
8/25/1987	12/4/1987	-33.5%	9.0%	13.4	4.4%	3.7%
3/24/2000	10/9/2002	-49.1%	3.9%	22.0	2.0%	1.9%
10/9/2007	3/9/2009	-56.8%	2.8%	13.3	-0.4%	3.6%
2/19/2020	3/23/2020	-33.9%	0.9%	24.8	1.5%	2.3%
Averages		-32.7%	5.1%	14.5	4.8%	4.3%

1/3/2022	10/12/2022	25.4%	4.0%	18.2	8.2%	1.82%
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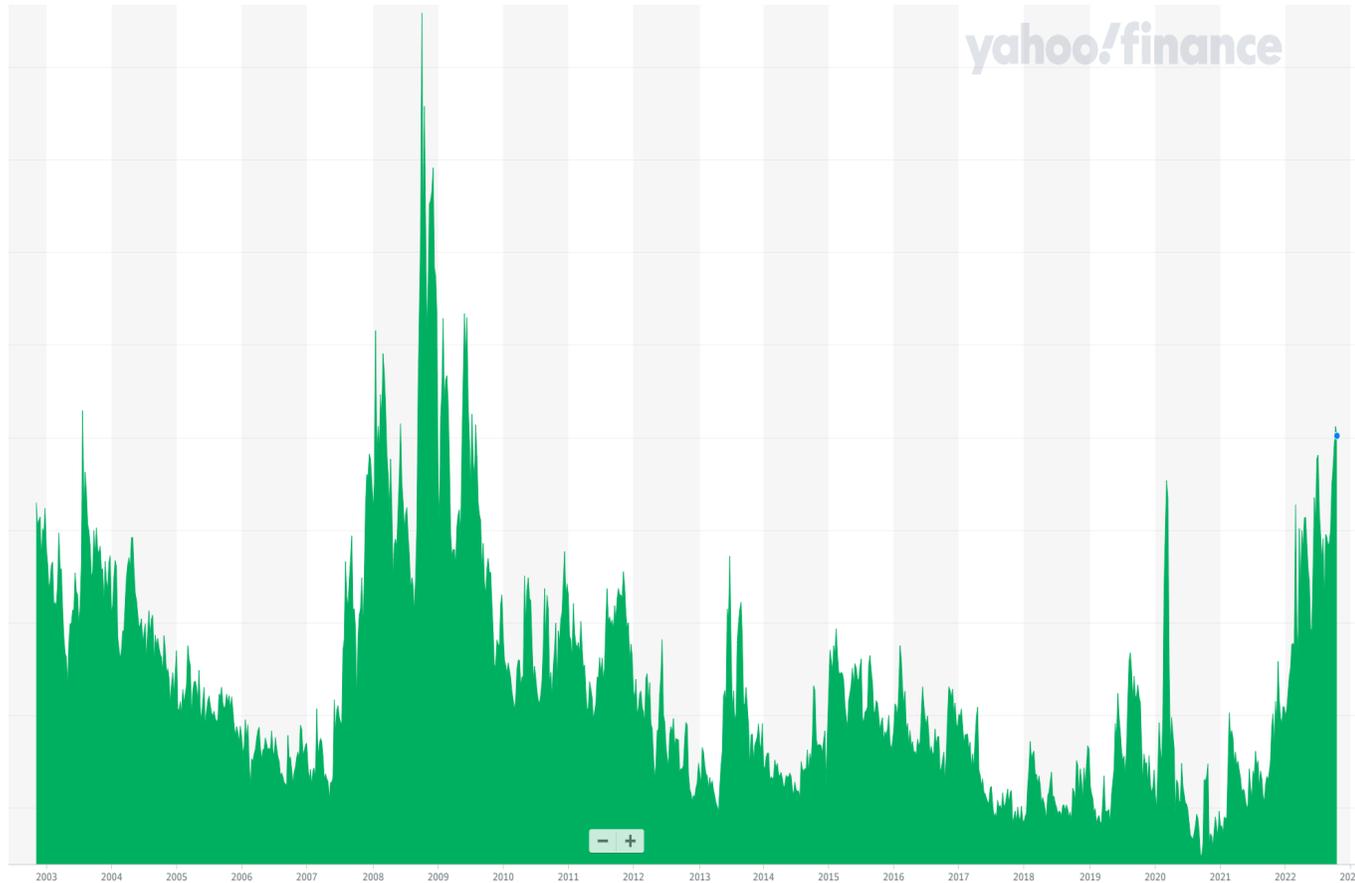
Margin Debt: Arguably Remains Far Too High (to signal bottom)



Source: St Louis Federal Reserve Bank

Overview

Move Index Volatility: Reason for Ongoing Concern



Source: Yahoo Finance

“As the creator of this Index, let me say that both 50 and 150 are the ‘wrong number’. A level near 50 can only occur when the FED actively constrains risk, while a level near 150 occurs when the FED has lost control.

The MOVE at 150 infers interest rate changes of about 9.5bps per day, a volatility that is unsustainable if only because human beings cannot tolerate such stress for long periods of time.”

- Harley Bassman



October Bottom?

Recap

- Both “tops” and “bottoms” are only identifiable in hindsight
- The USD strength puts significant strain on EM economies
 - History of defaults + equity market volatility
- Seasonal trends
 - Potential tailwind?
- Market technical are ugly
 - 200D SMA/etc
- Option metrics are unusual
 - No VIX/VOLQ “spike”
- Mid-term election boost?
 - Potential tailwind
 - No VIX/VOLQ “spike”
- When will MOVE Index subside?

Mark Your Calendar!

November 2	Fed decision
November 4	Jobs report
November 8	Midterms
November 10	CPI data
December 2	Jobs report
December 13	CPI data
December 14	Fed decision



Questions?

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Nasdaq-100[®] Ecosystem:

<https://www.nasdaq.com/nasdaq-100-options-xnd-nqx-ndx-volq/>

VOLQ Overview:

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