



# Strategy update: Complacency

Where we have never been before

ASSET MANAGEMENT  
UNIT

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## Updating the strategy:

### A convulsing the world

By May 25<sup>th</sup> the major stock indices in the US and Europe skyrocketed to new all time highs. The SP500 and Nasdaq reached their all time highs, but the real headline wasn't there. Bitcoin took all the attention from the media by getting to the heaven and back to hell the same day by plunging more than 15%. By the afternoon everybody forgot Bitcoin and moved eyes to see how crude oil prices plummeted almost 5% after OPEC agreed to extend the current production cuts.

Two weeks ago headlines focused on the extreme complacency in the market showed by the VIX trading at 17 straight red closes below 11 points. It never happened before. The following week VIX surged 45% alongside its natural correction.

Brazil also caught the attention on corruption charges to the head of government, making Brazil tracking ETFs to fall historically.

By the week starting at May 22<sup>nd</sup> China's credit rating was downgraded for the first time since 1989.

Many other situations were in the spotlight, just to mention a few, the biggest ever recorded cyberattack in the history, the terrorist attack in Manchester and the relations between Russia, North Korea (DPRK) and the US regarding nuclear issues are targeting the president Donald Trump on federal charges.

One can forget sometimes but this mix of "unbelievable" situation actually happened in the past, it is called complacency. But the even most interesting thing about complacency is identify it and planned the strategy to get advantage of the arbitrage opportunity that represents moments of extreme complacency.

If a natural correction is not seen once in a while to restore equilibriums the accumulation of sentiments and likelihoods to reverse direction can lead to a catastrophic event in the markets, an infamous fat tail event.

Today, the weekly close's still breaking expectations with so low volume. It is like the desire of investors to buy or sell just vanished. That could explain the moments when one of the majors stock markets index just go to a pause, no one buying no one selling.

By the other hand, currencies or FX markets are optimistic about the Japanese Yen. While the dollar entered in depreciation mode the 10 years treasury bonds keeps in downtrend when odds are high to almost 75% of probability a rate hike will be announced in June. All of the aforementioned are pieces in the intermarket puzzle that seems to simply not fit.

Technically, looking closely to mid cap stock market indices and transportation indices is way too far from what the SP500 and Nasdaq are doing at this moment.

## Plan of action:

The action plan at this conditions is simply:

- Currencies: Long Yen against dollar and commodity-linked currencies like the looney, CAD. Regarding the dollar, we highlight the presence of volatility due to the upcoming rate hike.
- Commodities: Our bearish view on crude oil prices remains at the table. Especially if the weekly close in the WTI trade below 50.60. That level is the support for the first range of prices after first OPEC agreement of the bearish era.
- Volatility: Long VIX below 10 points under a perspective of mean reversion move.

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