UP BY THE ESCALATOR, DOWN BY THE ELEVATOR

By Eden Rahim

Post-2008 Crisis market corrections seem to play out differently to Corrections prior to the crisis. In particular, prior to the crisis, corrections were typically a grind-it-out affair oscillating down for 3-9 months, wearing down investor expectations.

However, the bull market since the crisis low in March 2009 has seen 8 near double-digit to mid-teens percent declines averaging -12% occurring swiftly over an average of only 20 days. It is as if a trap door opens under investor complacency, and months of price advance is erased in days. Rapid price attrition, regardless of the catalyst, is the market's way of reminding investors to respect risk they had forgotten about.

Which brings us to the current episode. This bloodbath has witnessed a colossal drawdown of -12% over a few days, as measured using overnight low in the S&P 500 emini futures on February 6th. The fuel for this panic was hedging the Vega associated with the liquidation of Short Volatility funds. In some instances we have seen 'mechanical' origins that fueled the corrections. I guess it doesn't really matter what the cause is as long as the market achieves its aim of shocking ill-positioned investors out of complacency.

The flood of funds into inverse volatility funds crystalized the sentiment that investors were less concerned about buying cheap insurance through Index Put options or Long VIX Calls options, and more enamored with pressing their bets that the relentless 13 consecutive months of advances would persist.This was the outcome of that crowded trade.The market can be unforgiving.

Such swift market broadsides underscores the value of our ongoing use of hedge insurance to protect the Biotech portfolio from the unexpected.

Source S&P 500 Data: Bloomberg Database, Concept: Next Edge Capital Corp.