Flash Notes
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# A re-run of the 4Q18 stock market sell-off? Don't think so

In the months before the fateful 4Q18, in which the markets suffered heavy losses, some investors had positioned to hedge themselves against a strong falls in equity indices. (See in chart 1, how the volatility SKEW in 3Q18 reached values above the 150 level, which meant that the price of a PUT significantly out of money was much higher than the price of a symmetric CALL significantly out of money.

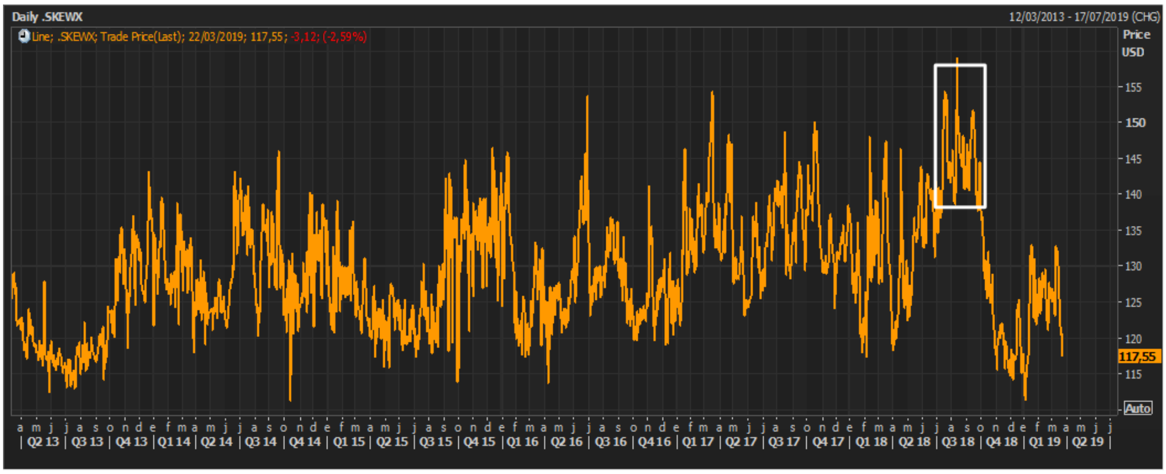
When the level of the SKEW moves to levels far from its average (either up or down) it means that some economic agents are being very active in the OTM (out of the market) options market. If the SKEW goes up sharply, it means that these agents are very active in buying PUTs that are very out of money (they are hedging themselves against strong downward movements). Similarly, if the SKEW goes down markedly, it means that these agents are being very active in buying CALLS out of money (they are positioning themselves for a very strong upward market movements). Please, notice how on January 1, with an SKEW level of less than 115, these agents were already positioned for what was to come; an impressive bullish 2019 start in the markets.

What is curious during the 3Q18 is that while the SKEW index had moved sharply upward (to 155), the traditional VIX index remained stable between 12-14 for the whole period; which means that there was no marked activity in the ATM options market (at the money), though there was an intense activity in the OTM options market. That is to say. Investors were not hedging portfolios against soft falls in the market, but instead against large falls in the market. Why?

My experience dictates that investors who buy OTM options are very different from those who buy ATM options (I usually refer the first ones as the "strong hands"). It is not that all investors were active only in the ATM, while they were passive in the OTM options market. Rather, the information that results from my chart suggests that only one group of investors (the first ones) were very active, while the rest of the investors (most of them) were not active.

In my opinion, if I may say so, investors who are active in the OTM options market anticipate movements better. According to the information I provide today, these investors are positioning themselves for a strong increase in markets. That is what makes me think that the risk of a repeat of the sharp falls observed in the last part of last year is, for now, low.

Best




## VIX Index (Chart 2)