

Subject: RE: [/] Trade Idea: Tax Reform Pure-Play / Long-Short Basket Pair [C]
From: Martin Zeman [REDACTED]
Date: Tue, 26 Sep 2017 18:32:41 -0400
To: Paul Barrett <[REDACTED]>
Cc: Vahe Stepanian <[REDACTED]>, Xavier Avila [REDACTED], Joshua Shoshan [REDACTED], Stewart Oldfield <[REDACTED]>, Davide-A Sferrazza [REDACTED]

One bullet swap.

Let's do some smart trades once we have the docs in place.

From: Paul Barrett [mailto:[REDACTED]]
Sent: Tuesday, September 26, 2017 6:27 PM
To: Martin Zeman [REDACTED]
Cc: Vahe Stepanian <[REDACTED]>; Xavier Avila [REDACTED], Joshua Shoshan [REDACTED], Stewart Oldfield <[REDACTED]>; Davide-A Sferrazza [REDACTED]
Subject: Re: [/] Trade Idea: Tax Reform Pure-Play / Long-Short Basket Pair [C]

I have an RTY vs SPY outperformance option on.

Would take a look once the docs are in place. Looks interesting. Is it one bullet swap or two separate legs?

Paul Barrett

Alpha Group Capital LLC

142 W 57th Street, 11th Floor, New York, NY 10019

[REDACTED] (o) [REDACTED] (c)

On Sep 26, 2017, at 5:13 PM, Martin Zeman [REDACTED] wrote:

Classification: Confidential

<image006.jpg>

Paul,

I want to highlight the below trade idea on the US Tax Reform from the Delta Force team. It's a very smart way to play the tax reform expectations in the US and that trade has already started performing in this 2-week update from Power Fraser who runs the team. It can be traded in a swap format and the highlights are below.

Buy DBUSTXHI / sell DBUSTXLO on swap for beta-neutral, sector-neutral, rates-neutral exposure to a corporate tax cut

1. This trade idea initiated on September 13 and is moving significantly today, +1.8σ

2. DB's Asset Allocation Strategists published an updated report on this trade which included some new baskets:

- Top 50 / Bottom 50 from the SPX-ex-REITs-and-UTES, chosen by effective tax rate after manually adjusting for deferred tax assets – “modified” tax reform on our Monitor
- Top beneficiaries of repatriation based on offshore cash and “buyback alpha score” i.e. stock's statistical tendency to outperform when doing a buyback

We've updated our Trump Policy Monitor, replacing some dead things with our various iterations of tax reform sensitivity. Available for your Launchpad if you want to monitor these trends intraday.

Reminder that we also think Size is a surprisingly good proxy for tax rate so IWM upside works well. IWM outperformance vs SPY today looks small, but becomes much more significant after controlling for sector skews (+1.3 σ), consistent with our model.

Lots more room to go if this starts to look like a real possibility.

<image011.jpg>

ORIGINAL TRADE IDEA PUBLISHED SEPTEMBER 13:

Buy DBUSTXHI / sell DBUSTXLO on swap for beta-neutral, sector-neutral, rates-neutral exposure to a corporate tax cut

<image002.png>

We're getting increasing chatter around the potential for success in tax reform before year end for the Trump administration. (Hey, it could happen!) Our customers are asking us how to trade. We still think IWM vs SPY is the cleanest but we've also seen demand for baskets.

We've seen a variety of constructions of this trade,* aiming to create exposure to tax reform, many of which result in taking a material sector bias and often an implicit interest rates view (for instance, Banks vs Utilities has a huge DV01, as we've highlighted before). And rates have been a widow maker all year.

DB's suggested construction:

- Compute effective tax rate for every company in the S&P 500 on a 5 year trailing basis
- Remove REITs and Utilities sectors due to unique tax treatment
- Remove Telcos due to tiny universe of stocks (n=4)
- Identify the top 10 and bottom 10 stocks from each remaining sector by tax rate and construct as a equal-weight long-short pair.
- Result is DBUSTXHI and DBUSTXLO, tradable on swap in >\$100mm/side/-day, 1ML flat / 1ML + 30 as a pair

Resulting construction looks like the below, in each remaining sector. Full composition available on Bloomberg.

Avg effective tax rate on "low" names: 17% Avg effective tax rate on "high" names: 45%

<image003.png>

S&P 500 Effective Tax Rates, compiled from IBES/Factset/Bloomberg by DB Global Asset Allocation Team

IB us if you're not currently permissioned to see DB indices and we'll turn you on. If nothing else, you'll be able to see if the market is starting to react to tax reform potential. 1 year realized vol of the package is <5% so a 30bps move is average and a 60bps move is significant. 1% is yuge.

*Including DB's own research department which had previously constructed a simple ranking of the 50 highest and lowest tax payers; DBUSHTAX and DBUSLTAX. Also available on Bloomberg for your review, and tradable.

Martin

<image004.gif>

Martin Zeman
Director | Key Client Partners

Deutsche Bank Wealth Management
DB Securities Inc

345 Park Avenue, 10154-0004 New York, NY, USA

Tel. +
Mobile
Email

KCP products and services are intended and available only for persons who are sophisticated institutional investors within the meaning of the FINRA Rule 4512(C)(3), and who are capable of evaluating the strategies, characteristics and investment risks of, and exercising independent judgment in evaluating, the ideas and products discussed herein. Trades and transactions are subject to relevant internal approvals of DBSI or its affiliates prior to execution, and the execution of any transaction or idea discussed herein is conditional on your becoming a client of Deutsche Bank. Key Client Partners (KCP) products, investment ideas and solutions and related matters discussed herein are provided for discussion purposes only, and strictly on a non-advisory basis. The KCP Americas desk does not provide investment advice. The information set forth herein is confidential and personal to you and is being presented for your information and for discussion purposes only. Any reproduction and/or redistribution thereof (in whole or in part) or disclosure of its content without our written consent is strictly forbidden. This communication does not create any legally binding obligation on the part of DBSI or any of its affiliates.

This communication may contain confidential and/or privileged information. If you are not the intended recipient (or have received this communication in error) please notify the sender immediately and destroy this communication. Any unauthorized copying, disclosure or distribution of the material in this communication is strictly forbidden.

Please refer to <https://db.com/disclosures> for additional EU corporate and regulatory disclosures.

Deutsche Bank does not render legal or tax advice, and the information contained in this communication should not be regarded as such.