From: Ens, Amanda <[redacted]>
Sent: Tuesday, November 15, 2016 2:44 PM
To: jeffrey E.; Richard Kahn
Subject: SPX put contingent on higher rates

Navigating post-Trump volatility

* We are recording unprecedented divergences in falling equity vol with rising rates vol post Trump's win. Intra-day S&P realized vol collapsed from near 60% to below 20% in 2d [Chart 1]

* While equities have shown less conviction over what a Trump win means (given strong sector rotation), the bond market has sold off with one of the largest moves in history [Chart 2 & 3]

* Stabilizing rates volatility from here is key to markets remaining calm and while equity upside may continue, it is not without higher risks

* We like cheap optionality to hedge long-equities if rates continue to move sharply

For investors long equities, we look at ways to cheapen protecting from downside risks in the event of further bond market volatility catalysed by Trump policy uncertainty

* Buy an SPX Apr-17 95% put conditional on US 10Y CMS > 2.5% at maturity for 0.87%

o 70% discount vs. vanilla

o CMS ref. 2.11%, SPX ref. 2,164.2

CMS = constant maturity swap

Chart 1: The response in S&P 500 realized equity volatility to the US election surprise was similar to Brexit but more extreme, as the spike in volatility collapsed at record speed

Source: BofA Merrill Lynch Global Research. Based on daily data from June 2004 to current

Chart 2: Ten-year US Treasury yields see a near record spike after the US election

Chart 3: Long Bond futures prices down near record amount (~5%) in the four days since the election

Source: BofA Merrill Lynch Global Research. Based on daily data since 1962.

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