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October 20, 2014 | Issue 4.47

"WARNING: Next week is going to be highly volatile, so proceed with caution!"

- last week's CA

But where there is volatility, there is opportunity. We booked four more winners last week, the two new trades I suggested during the week are near take-profit levels, and my confirmation mid-week of: (1) greens-golds steepeners and (2) adding to flies around the back blue and golds (i.e. M7-8-9) on a dip worked well.

Here are my thoughts on various topics:

Equities. Rates seem to be trading off of equities lately. Surely I can't be the only one who thinks that a 10-20% correction in the equity markets is "reasonable"? I'm not saying that it would be good for consumer confidence or the economy. But the S&P almost TRIPLED in 5.5 years. That is not normal in a mature economy. Just eyeballing a reasonable trajectory for S&Ps over the past 4 decades, somewhere around 1700 seems completely reasonable (discounting the exuberant tech bubble of 2000 and the housing bubble of 2007). Whenever I read the news about some stock outperforming, it's rarely about something actually related to *growth*. It seems like most share price increases are by-products of inversions, stock buy-backs, spinoffs, GAAP accounting and lofty valuations on tech companies that have made no money. And let's not forget the *currently* low cash flow valuation discount rate provided by the FOMC. I'm not saying those things aren't worth higher valuations – but "where's the beef?!?"

Ebola. I live near the ebola capital of the US – Dallas. Some of the moms around here are a little nervous. A few families we know had bought tickets to the Texas State Fair and opted not to go, to avoid the crowds. A few families avoid eating out - and we live over 30 miles away! I am not particularly worried, but I am still having my mother and my in-laws visit us later in the year – just in case. So I suppose this could be a damper on consumer spending for a month or so. Now that the knuckleheadness of various local doctors, nurses and other participants of this

Value on the Curve: (active CA trades):

1. ▲** **Too much positive curvature in the greens *relatively*.** Rates are way too low for this degree of curvature.
2. ** **Too much curvature around Z5/H6 –** We took profit in Z5. I still like H6 vs the level of longer term rates.
3. ** **Greens-Blues is too flat.** I don't see how we are not tightening in 2017.
4. ▼* **Take advantage of the flat vol curve between greens and golds.** We still didn't steepen as much as I thought, but it was enough to take some nice profit.
5. ▼* **Not enough curvature in the golds.** We should start taking a little off the table.

Value on the Horizon: ("C" trades):

- **If we get a massive short squeeze, look to set opportunistic shorts.** Well, we got the short squeeze. We may get another.
- **DONE Play for bearish sentiment before FOMC statements and minutes.** The markets seem to have caught on to this theme.
- **DONE Play for increased year-end turn premium on EDZ8.** I forgot to mention this earlier with all the market activity, but a few weeks ago, 3 month cash libor did nothing as it went over year-end. That does not disprove this theory, but I prefer to look at this again next year when rates may actually increase.

Noteworthy Levels:

- **None.**

comedy of errors has been exposed, I do not think this will reach epidemic proportions. Most reasonable people *should* be headed straight for the local hospital at the first sign of a fever. Dallas is not like NYC where you have millions of people taking mass transit every day. Pretty much everyone drives to work and few people actually walk anywhere. It is much harder for Dallasites (yes – ironically the word that refers to the locals sounds like a virus) to be in contact with a lot of people here than in most major cities. There is a small chance it gets worse, but it is highly unlikely this reaches epidemic proportions unless there is something we don't know about its transmission.

Eurodollar rally. EDZ6 rallied 51 bps in the past two weeks (after payroll Friday). But I had been saying that the markets were about 3+ months too early in its hiking estimates for a while. The FOMC surprised me a little when they made no *real* mention of "considerable" in the minutes. As I previously mentioned (that the FOMC apparently agrees with), you can't ignore the health of your major trading partners when assessing your own health. So these factors justify a large majority of the rally. I attribute the rest to equities and ebola, which I think could be faded – obviously not via an outright short, but I will be on the lookout for a good risk/reward trade. The data continues to be "constructive," aside from maybe retail sales. Typically when you stop out of a position, you take some time off and reevaluate. So it is possible the bears come back and start pricing in June again. We are data dependent after all.

Bullard. From the "this is why I ignore Bank Presidents" files… Bullard came out and suggested on Thursday that the FOMC should consider delaying tapering. After listening to the interview, his premise was that he wanted to keep the QE program open – just in case. He was one of the 6 bears I kept talking about for most of the year, and had been calling for earlier hikes. Well, he was a bear… until this week. Shaun White would be proud of that 180. Do not be surprised if it turns into a 360 within 3 months.

The calendar & FOMC. We have a quiet data week (other than possibly CPI). So this means just sitting there and watching equities. The FOMC meeting is the following week. Despite Bullard, I would be shocked if the FOMC actually did not go through with final tapering. They do not sound like they will remove "considerable," but even if they do for statement conciseness reasons, I do not think their intent is to be hawkish. If I were on the FOMC, I just go through with taper. If it has been agreed that "considerable time" is anywhere from 2 to 12 months, I see no reason to take that out. Because the last thing they should want to do right now is spook the already-fragile markets. The FOMC should be in "exude calm for the American public" mode. I think doing anything other than finishing tapering and maintaining "considerable" would reek of concern and desperation. As mentioned in the points above, not that much has changed in my core view, and I see no reason for panic… unless we get more ebola and a 30+% correction.

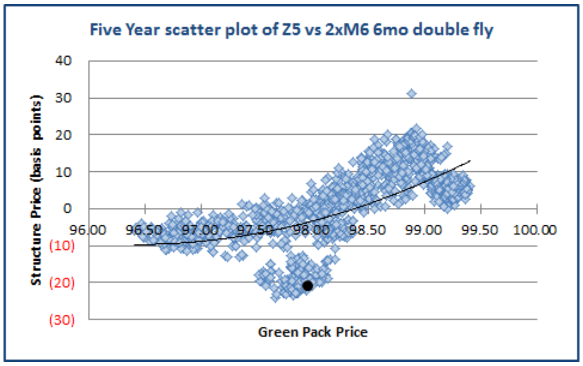
My core view. I still believe in the "later but faster" – but considering all the developments, perhaps a little later than what I was thinking a month ago. I too am data dependent. The peak curvature around the middle of the greens is misplaced *relative to* where the rest of the curve is. However, this could be stubborn to disappear if it is arising from large put-buying. I still see the blues as the more likely and attractive positive curvature candidate.

In these fast-moving markets, I need to send new trades via email. Stay tuned.

TRADE IDEA (Sent 10/15):

This trade is away now.

59) Buy EDZ5-M6-Z6 6mo fly vs Sell 2x EDM6-Z6-M7 6mo fly @ -26 (last print)



- *The flies in the greens (still around +10) are way too high, considering we had this kind of rally. It is especially silly for this to be lower today.*
- *Part of this is put-buying on 2EZ, but since we are 2 months of contract roll, and levels are extreme, this makes sense to do.*
- *All the lower points on the graph were BG-related - in fact, the entire cluster is! Bill Gross is nowhere near the size he used to be (and he used to buy a ton of reds), so this should not get as low as it had in the past.*
- *We made money on this type of structure 4 times this summer! This should do better on both a rally and a selloff.*
- *There are a lot of turns in this trade, but when the 3 month libor cash fixing went over year-end a few weeks ago, there was nothing. So I think we can fade the turn that is priced in here.*
- *Positive roll (on both directions)*

TRADE IDEA (Sent 10/15):

This trade is away now.

DK) Buy the M7 6mo fly vs Sell the M8 6mo fly @ 1 settle

If you have crisis protection (like the above) and do not think the world is coming to an end, consider buying the M7 6mo fly vs selling the M8 6mo fly @ 1 settle. I guess those guys who liked being short Z7 for the last FOMC SEP is not out, but this microtrade offers a lot of value. So I think if you sit on the bid, you may get filled. The same structure up to a year ahead is +5. That is a lot of cushion. And for those of you who do not remember, this was +10 at one point just a few weeks ago (which we sold).

TRADE UPDATE:

It's not often you get to lock in 100+Bp-Units in a week. I sent out the M7 6mo vs M8 6mo double fly, which did well, but I am not including it on the Trade List because not enough traded.

There is some minor value in the trades listed below (rated with "*") so give those a second look. But at this point, I am waiting for other opportunities to arise.

Trade	Entry	Exit / Close	P&L (bps)	Size [max]	(Sizing) Comments
32) * Buy 1.5x 0EZ5 99.125 call vs Sell 1x 2EZ6 98.125 call	0 (+1 fill at +1.25)	-5.125	-5.125 (to -6.375)	4 [4]	Less hikes in 2015 and more in 2016 makes a lot of sense on *a rally*. Look to do 2:1 for zero, assuming stable markets.
37) Buy EDU8-H9-U9 6mo fly	2 (+fills at +1.5, +1, +0.5)	2	0 (to +1.5)	20 [20]	There is a small tail probability that this goes much higher on a large bull steepening. Look to unwind at 2.5-3.
50) Buy 1.67x 2EZ6 98.25 call vs Sell 1x 4EZ8 97.125 call	-0.25	8 (settled 11)	+8.25	8 [10]	Converted to Trade 58 on 10/14 and took in 2.5 bps, by selling 3x 82 strike and buying 2x 81 strike. 66BUs is a solid result. Trade Closed.
52) * Buy EDZ6-Z7 spread	68	67	-1	1 [2]	It's quite mind-numbing that we could rally so much and not steepen this part of the curve.
53) * Buy EDH6-U6 spread vs sell 3x Z6-M7-Z7 fly	18.5	22	+3.5	3 [6]	My official target is 23.5. But 22.5 could be good in this environment.
54) Sell EDZ6-M7-Z7 fly vs Buy Z7-M8-Z8 fly	8.5 (+3 fill at 9.5)	7 (settled 5)	+0.5 (to +1.5)	4 [8]	We bought back the Z6 6mo fly @ 9.5 on 10/13. We sold 2.5s in the Z7 6mo fly on 10/15. A profit of 9BUs on a microtrade. Trade Closed.
55) ** Sell EDH5-H6-H7 1 year fly vs sell 0.5x EDM8 @ 4853.5	4853.5 (+1 fill at 4856.5)	4853.7	-0.25 (to +2.75)	2 [2]	This is my core view on the curve right now, but doing smaller may be more prudent.
56) Buy 2x 0EZ5 99.125 call vs Sell 1x 2EZ6 98.125 call	0	6	+3.25	4 [4]	The Z4-5-6 fly went below -40, as predicted. We cashed out on 10/14. +24BUs. Trade Closed.
57) * Buy EDM7-M8-M9 1 year fly	16.5 (+1 fill at 15)	17.5	1.5 (to +2.5)	▲2.5 [4]	Added 1 unit at 15 on 10/13. Clients added down to 12 and took partial profit between 16.5 and 17.5.
58) Buy 2EZ5 98.125 call vs Sell 4EZ6 97.125 call	-0.5	+5.5	+6	1 [2]	Clients exited as high as +6.5 (my recommended exit on 10/16). +6BUs. Trade Closed.
59) * Buy EDZ5-M6-Z6 fly vs Sell 2x EDM6-Z6-M7 fly	-25.5	-21	+4.5	2 [8]	Trade sent on 10/15. Favorable close. I like taking profit around here.

2013 Trades Closed in 2014 (9 total): Winners: 8, Losers: 0, Neutral: 0, DK: 1

2014 Trades Closed (53 total, including 4 Winners above):
Winners: 32, Losers: 7, Neutral: 5, DK: 9

Trade Table Notes:
The Table shows the list of active trades. The Trade List (and in particular with the specified the sizing) is not intended to be traded as a "book". As new readers are constantly being added, the Trade List highlights the best available positions (in my opinion) on the curve *at that point in time*. Trades are removed as profit is taken, or when a trade ceases to provide value (which may result in a loss).