Weekly Market Summary

28th of August 2015

Ever Dreamed of Making a Fortune in a Short Period of Time?! This Week's Market Action Provided that Opportunity!! **Fadi Nasser (SVP – Head of Treasury Sales)**

Last week, I wrote a piece entitled "There Comes a Time When Confusion Reigns & Markets Tank!" The mail was well received by our valuable clients, though honestly little I knew back then that the days ahead were about to bring such excessive volatility & heightened market distress/opportunities!

So what just happened to financial markets this week?!

Last Friday, a three-day uninterrupted selloff in major equity markets culminated in Europe's benchmark equity gauge (the Stoxx Europe 600 Index) falling 13% from its record. The stock rout - that began after China devalued its currency - gathered strength across markets, eventually hitting the US mid-last week, leading the S&P's 500 Index and Dow Jones Industrial Average to their worst week since 2012. Safe haven assets like gold and the yen climbed sharply.

And whilst multiple trillions of US dollars were already rumored to have been wiped from the value of worldwide stocks and commodity funds, the weakest Chinese manufacturing release since the global financial closing on that Friday as well as the 270 rapid drop in the Dow Industrial Average during the last 2 hours of trading on the same day (Dow finished the session down 531 points) clearly signaled that more pain was forthcoming when financial markets re-open and trading resumes on Monday 24th. SURELY though no one anticipated how Surreal (Incredible, Unbelievable …) that Black Monday would turn out to be!!

By the time Europe woke up on Monday 24th, Asian equity markets had already tumbled: The Shanghai Composite and the Japanese Nikkei 225 indices were lower on the day by 9% and 5% respectively, while a gauge of stock-market momentum in Hong Kong was showing the most extreme selling since the market crash of 1987. Commodities sank to a 16-year low and the currencies of Malaysia and Indonesia dropped to the weakest levels since the Asian financial crisis in 1998. Clearly European equity markets followed, gapping lower in sympathy, while the Euro and the Yen lead a sharp move (higher) against the US dollar. WTI oil broke the $40 psychological level, while copper and aluminum (2 leading indicators of global economic health) headed to their lowest levels in six-years!

The world (at least for the trader community) was falling apart, though many optimists were still confident that North American Leadership (the long awaited US stock markets opening!) would save the day (or what was left of it) and provide some stabilization to global financial markets. Little they knew how their misplaced expectations (or wishful thinking) would lead to major disappointments!

A gauge of market stress getting too jammed up to function (the Chicago Board Options Exchange Volatility Index failed to update for about 30 minutes after the open of stock trading at 9:30 a.m Easter time) !! Such was the extent of the drama at the open of trading in the American equity market on that day, when waves of global selling battered stocks with almost unprecedented force leading the Dow Jones Industrial average to collapse by 1,089 points in a matter of minutes. At its worst, about US$1.2 trillion of market value had been erased from U.S. shares (for that day alone!) before prices leveled off and the Dow Jones Industrial Average rebounded almost 500 points. At one point, the Standard & Poor's 500 Index came within 34 points of setting off a market-wide circuit breaker that would have shut down trading for 15 minutes to restore order. More than 2 billion shares changed hands in the first 30 minutes, almost one-third of what usually trades in a day. Fear gripped traders for half an hour as selling deepened after the biggest plunge in four years. General Electric Co., the 10th largest U.S. company by market value, and JPMorgan Chase & Co. dropped as much as 21%, their worst intraday losses since 1987 and 2009, respectively. Stocks in the Dow Jones Industrial Average were down 11% on average at their lowest point. Apple Inc. tumbled as much as 13% while Google Inc. and Microsoft Corp. sank more than 7%.

Whilst equity markets have since recovered, paring part or most of their earlier hefty losses (for the week Japan's Nikkei 225 down 1.5%, Hong Kong Hang Seng down 3.5%, China's CSI 300 down 6.9%, German DAX up 1.1%, and US Dow Jones +1.0%), uncertainty continues to prevail as we head into September and closer to that fast approaching September 17th FOMC meeting! On the latter, market opinion remains divided, given that recently released US data has exceeded expectations (stronger-than expected Durable Goods report, Consumer Confidence and second quarter GDP), further pressuring the Fed to go ahead with their planned symbolic 25 bps hike while tighter financial conditions and increased market turmoil continue to call for a delay in US rate rises (as Bank of America Merrill Lynch economists rightly observed earlier this week, the economic data say "go" but the markets say "no". It is akin to a tug of war between the domestic real economy and international financial markets).

Last, a very interesting story picked from Bloomberg News this morning, showing how cold headed minds can profit big from such market volatility (a la Warren Buffet famous quote "*You want to be greedy when others are fearful. You want to be fearful when others are greedy*"). Major highlights of that story are reproduced in this week's market update (for readers still hungry for success market stories):

“While a lot of investors were hitting the panic button Monday, a Japanese day trader who had made a big bet against the market timed the bottom almost perfectly and narrated a play-by-play of the trade to his 40,000 Twitter followers. He claims to have walked away with $34 million. As financial markets got crazy this week, many people turned cautious. Some were paralyzed. Not the 36-year-old day trader known by the Internet handle CIS.

CIS had been shorting futures on the Nikkei 225 Stock Average since mid-August, wagering it would fall. By the market close on Monday, a paper profit of $13 million was staring him in the face. He kept building the position. When he cashed out late that night, a collapse in New York had caused his profit to double.
Instead of celebrating, he kept trading. He started betting the market had bottomed. When he finally took his winnings off the table on Tuesday, he tweeted, “That’s the end of my epic rebound trade.” His profit, he said, had almost tripled.

Last year, when he was the subject of a profile in Bloomberg Markets magazine, CIS said that in a decade of day trading, mostly from a spare bedroom in a rented apartment, he had amassed a fortune of about $150 million. At the time, he shared tax returns and brokerage statements to back up his claims. One document showed he had traded $14 billion worth of Japanese equities in 2013 - about half of 1% of all the share transactions done by individuals on the Tokyo Stock Exchange that year.

CIS became a cult figure among Japan’s tight-knit community of day traders by trash talking on Internet message boards early in his career. He’s notorious for lines like “Not even Goldman Sachs can beat me in a trade.” Last year he opened a Twitter account, on which he talks about video games and, regularly, his trading. It’s impossible to say how many of his followers are also day traders, and how many of those buy and sell in his wake. Those who do, of course, are quite possibly helping him make money.

The latest trade began on Aug. 12, when CIS noticed a shift in equity markets he hadn’t seen for a while. Shares in the major indexes were struggling to recover from sell-offs. He started shorting Nikkei futures: 200 contracts the first day and another 1,300 over the following week and a half. The stakes were enormous. With 1,500 contracts at a notional value of about $160,000 each, his bet against the Nikkei was about $240 million. For every 100 yen move in the index, he stood to make or lose $1.25 million. The market was mostly flat over the next few days; CIS bided his time playing video games. On Friday Aug. 21, the Nikkei dipped. Then on Monday, the index plunged the most in two years, and the futures fell more than 1,000 points to 18,410. By the close at 3 p.m. in Tokyo, his profit stood at about $13 million.

This is the point where most traders would take their money off the table and call it a year. Not CIS. “I’m adding to my position,” he wrote on Twitter. “Then I’m going to go for a walk and prayer.” He sold 100 more futures contracts. Two hours later, he sold another 100. His bet against the Nikkei had risen to about $275 million. He *would lose $1.4 million for every 100-yen increase in the index. His logic for hanging on to the trade until the U.S. open, at 10:30 p.m. Tokyo time, was this: Panic would grip American investors returning from a weekend after they saw the scope of Asian selling, including Shanghai's 8.5 percent plunge. That would trigger selling, which, in a feedback loop, would pull Nikkei 225 futures down violently amid the thin volume of late-night trading. "I figured there would be a lot of fear around the U.S. open and that's what I was aiming for," he said. On cue, the Dow Jones Industrial Average fell more than 6 percent in early trading. Nikkei futures tumbled again, dipping 1,250 yen below the 3 p.m. closing level. CIS, home in his pajamas, finally cashed out his short position. His profit had hit $27 million.*

There was still more money to be made from the panic though. Some investors that night were willing to pay a hefty premium for options that protected against the Nikkei crashing below 10,500. That would be a collapse of almost 40 percent. In CIS's view, these investors were looking to buy insurance against a near impossibility. He was happy to take the other side of that trade. The contracts were worth another $250,000 to him. He made the first deal within 10 seconds of what would prove to be the market's bottom at 10:34 p.m. "Too delicious," he tweeted.

About an hour later, as he became more confident in a rebound, he started buying Nikkei futures. Now the play was the opposite of the short bet he'd started the day with. By 1 o'clock Tuesday morning, he'd accumulated 970 contracts, a $145 million wager that the market would start to climb. He made one more trade before bed: a few more option contracts sold to straggling panickers. Those were worth $6,250. By now, at 1:40 a.m., he was a rich man stooping to pick up pennies. He dashed off a last tweet at 2 a.m. "What a day. Still holding on to all my buys," he wrote. "Time to sleep".

CIS returned to Twitter five hours later. Nikkei futures opened at about 18,000 and slowly recovered. Early that afternoon, he closed out his long position".

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