

Delta Investment Management is a registered investment advisory firm headquartered in San Francisco. Delta welcomes discussions with individuals seeking investment advice and advisors seeking a new partner. Delta manages portfolios at TD Ameritrade and Schwab. Please contact Delta at info@deltaim.com or 415-249-6337 to learn more.

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Investment Batting Average Peril

In baseball, batting average is a useful statistic. It indicates how frequently the batter gets on base. The downside of not getting on base is waiting for the next turn at bat. The risk/reward of taking a turn at bat in baseball is good even with a low batting average. In investing, batting average can be deceptive because risk may be asymmetric.

In investing, you can have a high batting average. But one losing trade can wipe out all of the accumulated gains. This would be the equivalent of a baseball batter being called out on three strikes and then being permanently banned from the game as a result. The downside is much greater than the upside. This is asymmetric risk.

On November 24, 2017 the CBOE Volatility Index (VIX) reached an all-time low of 8.56. Of the 20 lowest VIX closes, 18 occurred in 2017 and 2018. Of the 68 times the VIX has closed below 10 over the past 27 years, 59 of these occurrences were in 2017 and 2018. Volatility has been very, very low over the past year.

CBOE Volatility Index (VIX)



Selling volatility is usually a winning trade. It has a high batting average. Most of the time, volatility does not change much from day to day. But on some days, volatility may spike. For example, when Lehman Brothers filed for bankruptcy in September 2008 with \$600,000,000,000 in assets, volatility spiked from about 20 at the beginning of the month to a high of 89 by October 24. A volatility seller would have been wiped out by this 345% volatility rise.

Difference Between Implied and Realized Volatility 2003 – June, 2017



The VIX has only traded to 50 or higher three times in its history (since April 1, 1993). One of those three times was earlier this month. Normally when the VIX goes above 30, there is some obvious headline news that is causing widespread investor anxiety. In this case, the macro investment environment was quiet while stocks plunged and volatility spiked. It appears that hedge funds who operate privately at the institutional level of the market may have been the leading cause.

LJM Partners is a Chicago-based hedge fund that was short volatility in their LJM Preservation and Growth Fund. In the scramble to cover their short-volatility trade, LJM and other institutions in the same position placed significant downside pressure on the stock market. After posting positive results in every year since the fund launched in 2006, it lost over 80% of its value this month. This is asymmetric risk. This is a high batting average in a losing investment. LJM is not the only fund to have run into asymmetric risk this month. Traders/sponsors of inverse VIX securities, including Credit Suisse, suffered losses and some of these securities are being permanently retired.

Part of our approach to money management is to avoid investments involving negative asymmetric risk. We start by considering how much money we might lose in an investment before we think about how much we might make. This is a key ingredient to how we grow and protect wealth over time.

Give Us a Call Today

We invite you to give us a call at **(415) 249-6337**, visit www.deltaim.com or email us at info@deltaim.com if you have questions about how we can assist you in managing your investment accounts.



Delta Stock Market Dashboard

MARKET SENTIMENT IS

BULLISH

THIS WEEK'S NUMBER IS

48.0

Our technical indicator decreased
this week from 58.3 to 48.0

INDICATOR STATISTICS

Consecutive Bullish Weeks:	66
Cycle Inception Date:	11/15/2016
Range:	47.9 – 75.7
Mean:	63.0
Bullish Weeks YTD:	7
Bearish Weeks YTD:	0
*S&P 500	25.1%
*DJIA	33.5%
*NASDAQ	36.4%

* Percentage change during current cycle

Delta Market Sentiment Indicator Over the Past Year



(Delta MSI is published every week in *Barron's*)

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