We share the Weekly Gamma Bands Update by Viking Analytics. The report uses options gamma to help you better manage risk and your equity allocations.

Gamma Band Update

The S&P 500 (SPX) again closed the week above the Gamma Flip level, and in our view is prepared to trade with low volatility through the key mid-year option expiration on June 18th as long as price remains above the gamma flip level. If SPX value falls below the gamma flip and 20 day moving average, we would then expect to see increasing volatility.

Our daily Gamma Band model[1] maintained a 100% allocation to SPX last week. When the daily price closes below ?Gamma Flip? (currently near 4,205), the model will reduce exposure in order to avoid price volatility and sell-off risk. If the market closes on a daily basis below the lower gamma level (currently near 3,995), the model will reduce the SPX allocation to zero.

Investors who keep an eye on various gamma-related levels are more aware when market volatility is expected to increase. One application of Gamma Bands is to maintain high allocations to stocks when risk is expected to be lower. For investors who have been conditioned to ?buy low and sell high,? it is counter-intuitive to increase allocations when the market rises, but this approach has shown to increase risk-adjusted returns in the back-test.

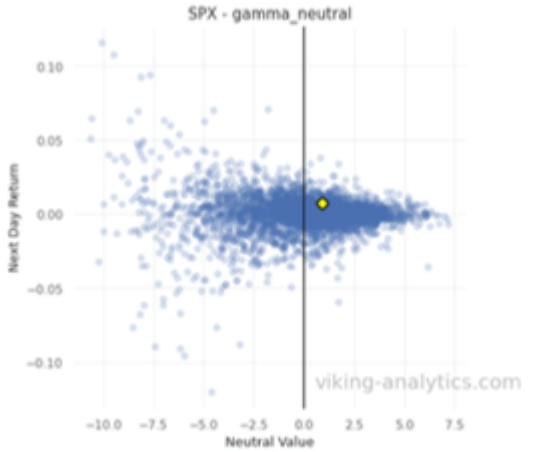


The Gamma Band model is one of several indicators that we publish daily in our SPX Report. With stocks continuing to extend historically high valuations, risk management tools are more important than ever to manage the next drawdown, whenever it comes.

A sample of the SPX report can be downloaded from this link. Please visit our website to learn more about our daily reports and quantitative algorithms.

The Gamma Flip - Background

Many market analysts have noted that daily volatility in the S&P 500 will change when the value of the SPX moves from one gamma regime to another. Some analysts call this level the ?gamma flip.? The scatterplot below shows how price volatility (on the y-axis) is increasingly lower as the value of SPX rises higher above the Gamma Neutral level (on the right side of the chart). When the value of the S&P closes lower than Gamma Neutral (to the left of the chart), volatility increases.



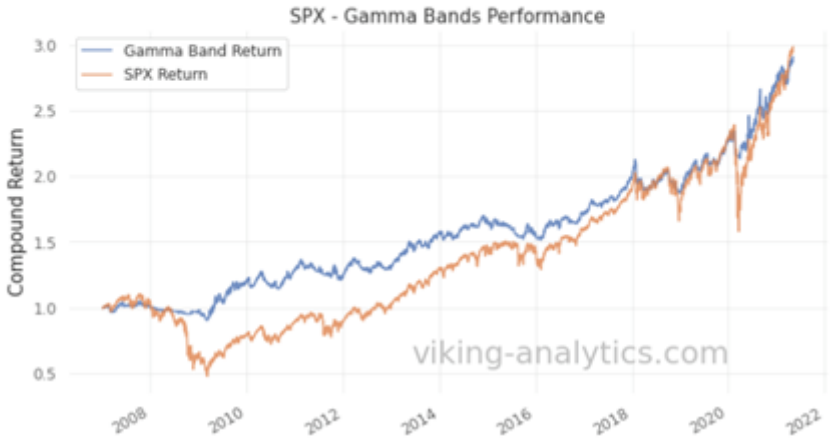
Gamma Band Model ? Background

The purpose of the Gamma Band model is to show how tail risk can be reduced by following a few simple rules. The daily Gamma Band model has improved risk-adjusted returns by over 60% since 2007. The graph below demonstrates how this approach can limit drawdowns while maintaining good returns. A quick video introduction of the Gamma Band model can be seen by following this link.

Gamma Band Historic Information

	sharpe	kurtosis	annual_vol
Gamma Band Return	0.79	7.81	0.10
SPX Return	0.47	12.72	0.21

* Gamma Bands improve backtested Sharpe by: 67.4%



Disclaimer

This is for informational purposes only and is not trading advice. The information contained in this article is subject to our full disclaimer on our website.

[1] The Gamma Band model in our SPX Market Report adjusts position size DAILY based upon the daily closing levels of SPX value and calculated Gamma Neutral. The Weekly Gamma Band model is shown for illustrative purposes only.

Authors

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