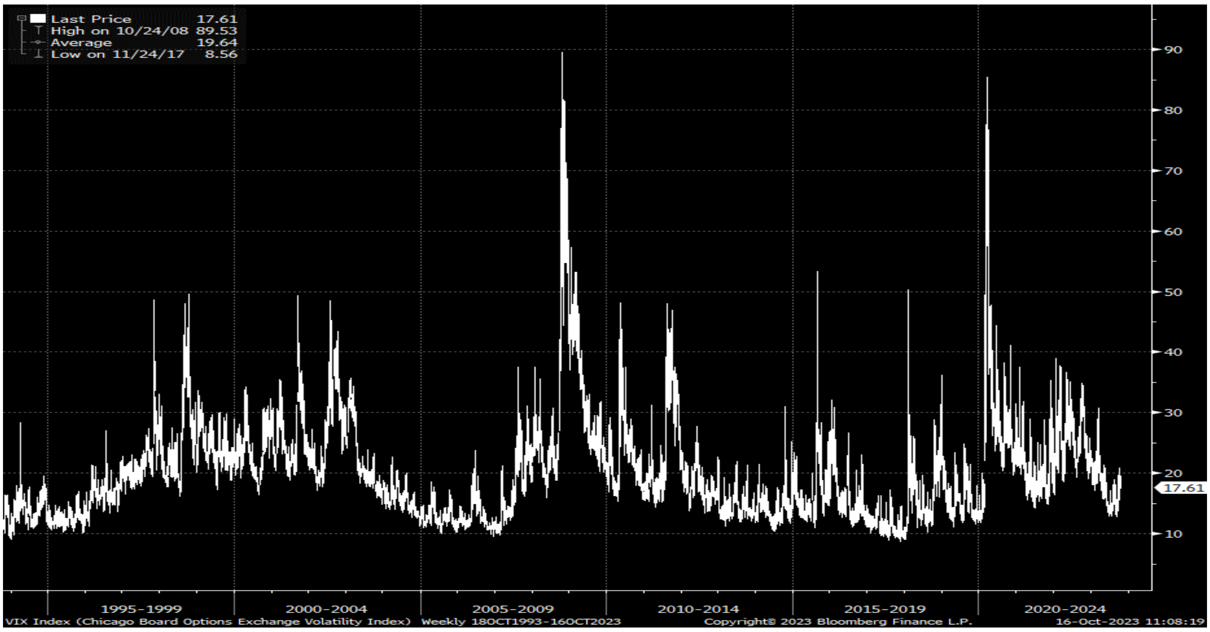
Weekly Blog

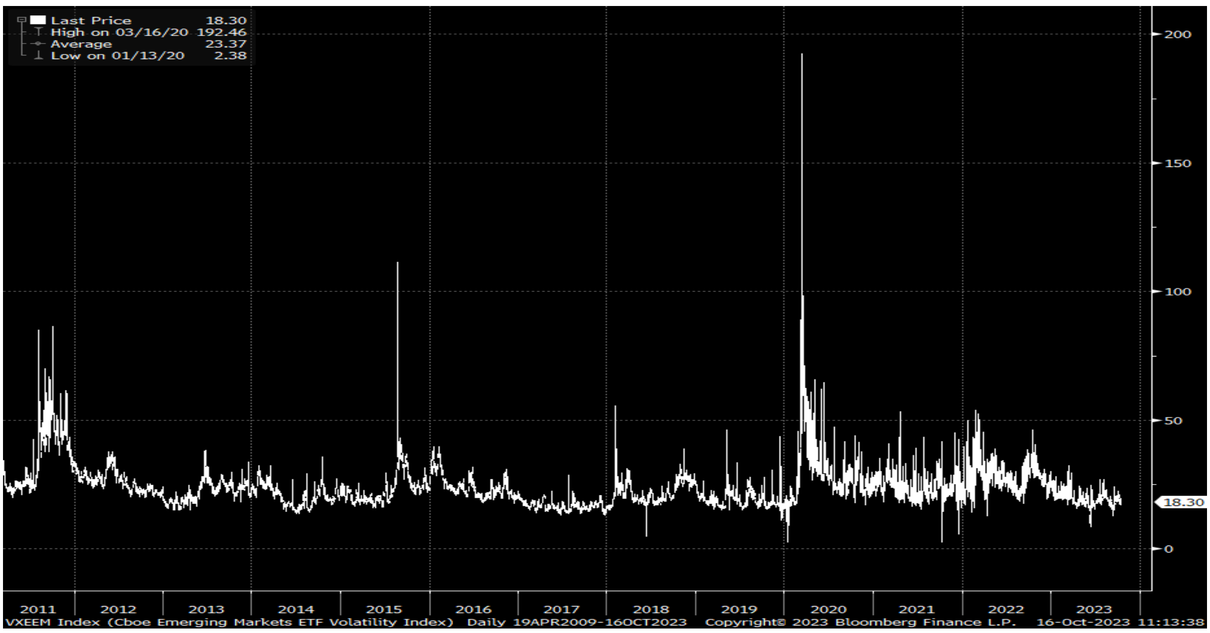
October 27th, 2023



Source: Bloomberg

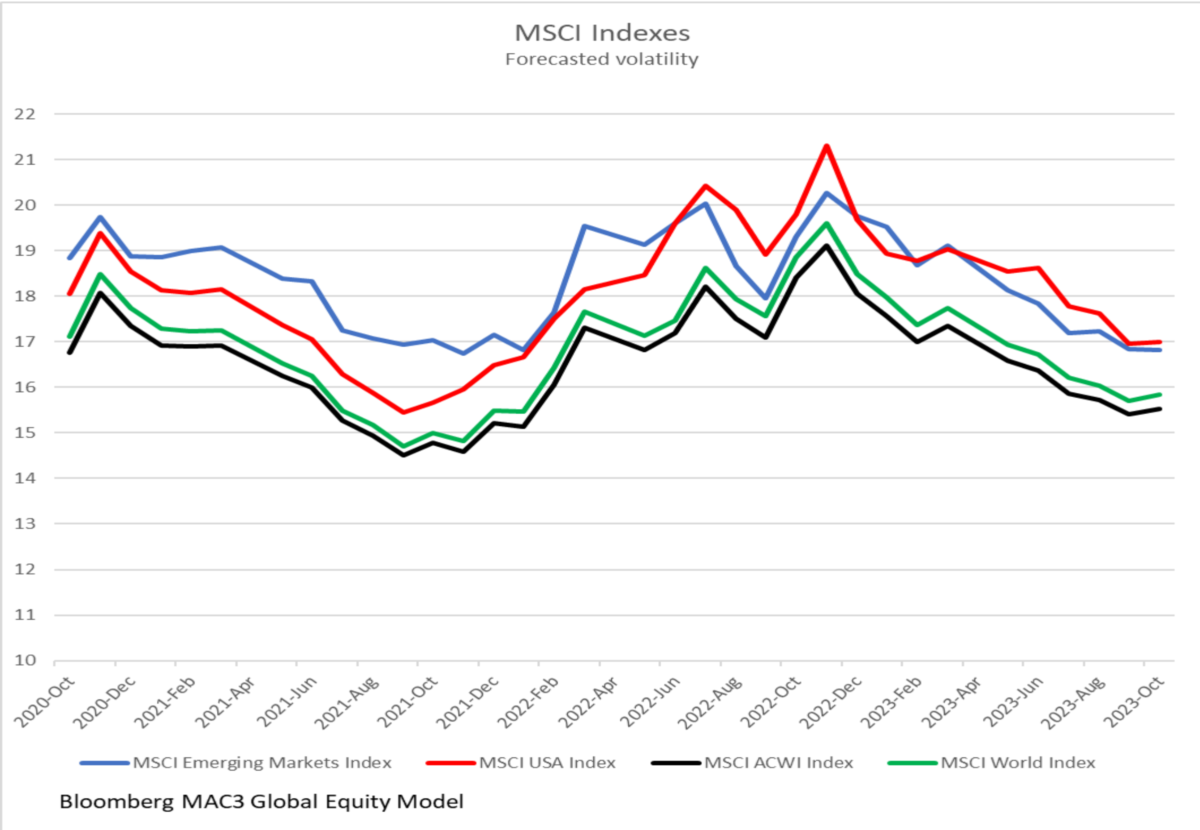
Volatility has been very tame over the past 3 to 6 months despite political, economic and financial uncertainty. The cost to insure against higher volatility seems relatively low.

The VIX as of October 16th was around 17 and this represents the 50th percentile based on daily data over a 30-year period, as can be seen above. The VXEEM (CBOE Emerging Markets ETF Volatility Index) was around 18, which represents the 25th percentile based on daily data starting in March 2011, as shown below.



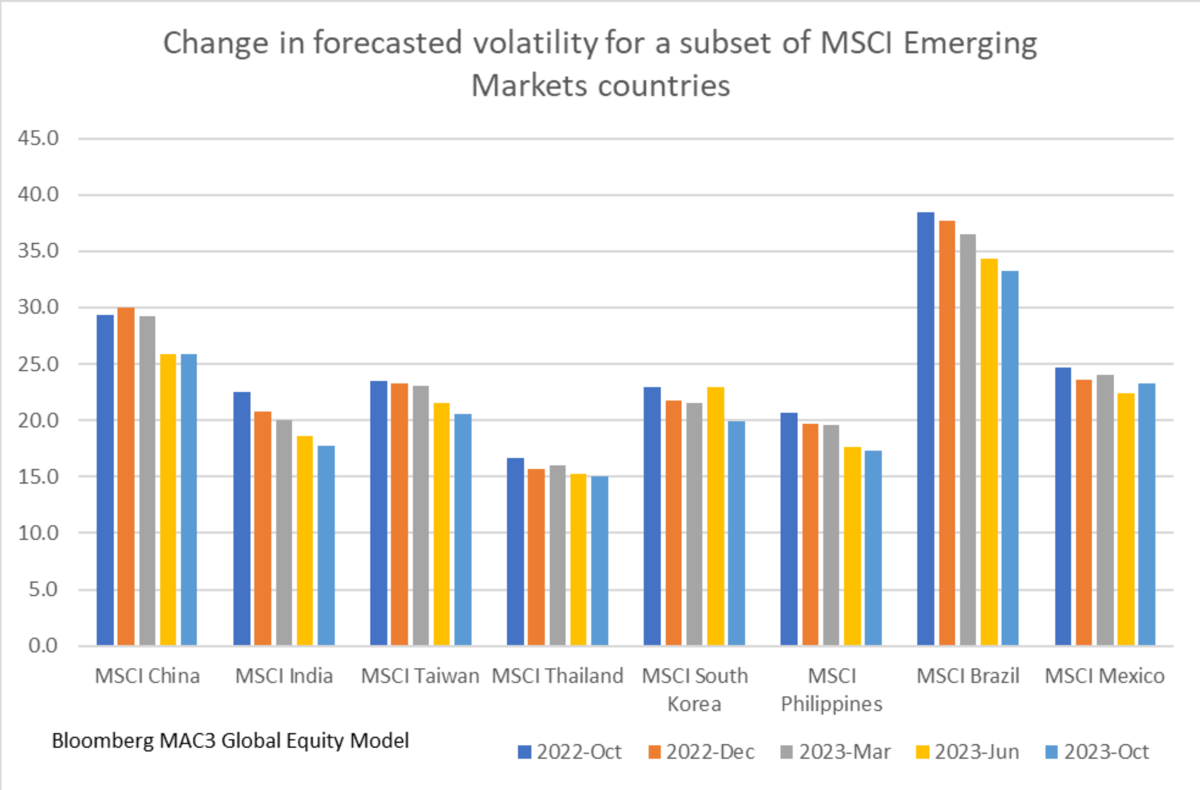
Source: Bloomberg

Under another lens, forecasted volatility has also come down steadily over the past year. According to The Bloomberg MAC3 US Equity model, annualized forecasted volatility for the MSCI USA Index went down from 21.6% last November to 17.0% currently, as presented in the following graph. The same trend can be seen for the MSCI Emerging Markets Index, going from 20.3% last November to where it currently stands at 16.8%. And the same trend applies to the MSCI ACWI Index and the MSCI World (Developed) Index. An interesting point to highlight is that the MSCI USA Index has had periods of higher forecasted volatility than the MSCI Emerging Markets Index since August 2022.



Source: Bloomberg, MSCI

Individual countries part of the MSCI Emerging Markets Index all saw their forecasted volatility fall over the past year. Although individual country volatility has decreased, the percentage change differs from country to country. For example, volatility in India has come down 21% over the past year, while volatility in Mexico has only come down by 6%, as we can see in the next graph.



Source: Bloomberg, MSCI

A word of caution, although current volatility/risk forecasts are low, this does not mean that it is smooth sailing ahead. Periods of low volatility may push investors to more speculative bets and more concentrated strategies. Of the 650 stocks that are members of the MSCI USA Index, only 28% have beaten the index this year. Of those stocks, the "Magnificent Seven[1]", representing 25% of the index weight, are responsible for about 80% of the return of the index. On average, they have returned 94%.

This last figure shows 13 significant US market drawdowns since 1998. 5 drawdowns began when the starting point of volatility was in the bottom decile of historical values:

- 2/19/2020:10.9%;
- 10/8/2018:7.8%;
- 1/26/2018:7.5%;
- 9/18/2014:8.4%;
- 7/19/2007:11.6%.

[1] The Magnificent Seven are: Apple, Nvidia, Microsoft, Meta Platforms, Amazon, Tesla and Alphabet.

Year	Start Date	End Date	Drawdown	Drawdown Days	Start Vol	End Vol	Change in Vol	Recovery Date	Recovery Days
2020	2/19/2020	3/23/2020	-34.6%	33	10.9%	34.2%	214%	8/6/2020	137
2018	10/8/2018	12/24/2018	-18.6%	77	7.8%	21.1%	171%	3/21/2019	87
2018	1/26/2018	2/8/2018	-8.9%	13	7.5%	15.1%	101%	7/12/2018	154
2014	9/18/2014	10/15/2014	-7.4%	27	8.4%	18.2%	117%	10/31/2014	16
2012	5/1/2012	6/4/2012	-8.8%	34	15.0%	18.7%	25%	8/7/2012	64
2011	7/7/2011	8/8/2011	-9.4%	32	12.3%	30.1%	145%	2/3/2012	179
2010	4/23/2010	7/2/2010	-15.5%	70	12.7%	24.1%	90%	11/3/2010	124
2008	8/28/2008	11/20/2008	-42.4%	84	17.7%	48.6%	175%	4/15/2010	511
2007	7/19/2007	8/15/2007	-9.1%	27	11.6%	15.8%	36%	10/1/2007	47
2007	10/9/2007	11/26/2007	-9.3%	48	15.0%	16.5%	10%	N/A	Multi-Years
2002	3/19/2002	7/23/2002	-30.6%	126	18.3%	30.5%	67%	N/A	Multi-Years
2000	9/1/2000	4/4/2001	-27.4%	215	18.7%	28.3%	51%	N/A	Multi-Years
1998	7/17/1998	10/8/1998	-20.7%	83	14.4%	24.4%	69%	12/21/1998	74

Source: Axioma

Given the uncertainty and increasing geopolitical risks, prudence is advisable. Active managers should stick to high confidence calls and control their exposures and active risk.

Best regards,

Mount Murray Investment