

# THC MARKET BULLETIN

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## TYM0 - 7 vs OTR Trade on 4/16/2010

THC's **Cointegration** results identify the contributing factors to the P/L of the basis trade:

**Scenario:** \$1.25M long in the 7yr OTR (912828MV9) and \$1M short in the 10 yr futures from 4/15 9:00PM to 4/16 4:00PM. The futures and OTR DV01 are -\$748.15 and \$759.54 respectively with the basis tail risk ( net DV01) of \$11.39. That is, if the yield curve between 7 yr and 10 yr makes a parallel downward shift of 1 basis point, the basis position would profit \$11.39.

**Info:** SEC accused Goldman Sachs of fraud on the morning of 4/16, resulting in significant market movements. Cointegration can be utilized to monitor the price movements on that day.

The cointegration figure below depicts all components of the P/L (blue line) at 5-minute intervals during the US and Asian trading day, starting at 9:00pm EDT, 4/15. The P/L acts as an "index" of entry and exit positions. In particular, we should focus on the returns from three movements: (1) the futures price move relative to the OTR (purple); (2) the 7 yr rate move, the CTD rate (green), (3) 10 yr OTR rate move, (light green).

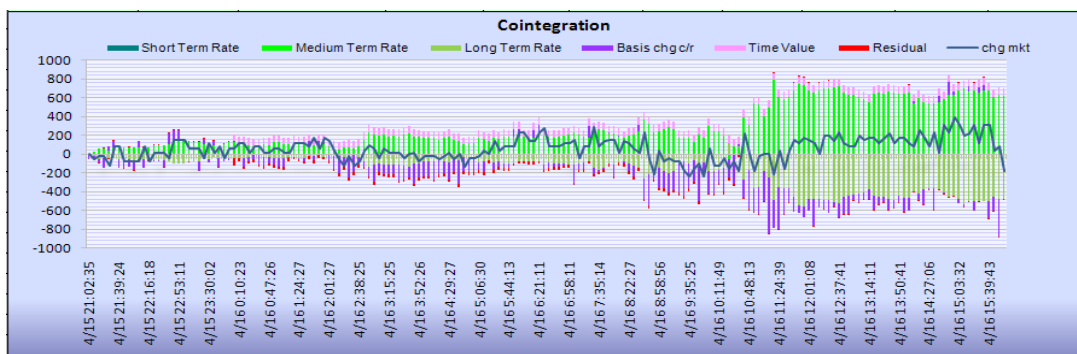
### Results:

- (1) Basis trading picked up around 3:00am. Increasing futures prices (purple bars) negatively impacted the basis trade. Conversely, the 7 yr rate move mitigated the P/L of the trade.
- (2) Futures richness was eliminated by 6:00am resulting in a positive P/L of the trade.
- (3) When the US market gathered momentum around 9:00am, the futures again led the market, with the 7 yr following, but with much larger movements.
- (4) Between 10:45am and 11:30am, the market was in full swing. By then, movement in the futures had already been priced in. (Purple bars are large and level).
- (5) After 11:30am, the 10 yr rate movement relative to the 7 yr rate movement became important, lowering the P/L of the trade.

### Conclusion

While the Goldman announcement was made in the morning, the results seem to show the futures market was active ahead of the cash market. Traders should isolate the interest rate effect from the futures cheap/rich movements by adjusting the tail risk to exploit the trading opportunities.

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