Lee Robinson: Short-vol trades worsened market losses

Ex-Trafalgar manager says some traders weren't prepared for volatility surge

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Former Trafalgar Asset Managers manager Lee Robinson has added his voice to the chorus blaming strategies selling volatility for the market reversals earlier this month.

"This is the first time that rising volatility has caused markets to fall rather than the other way round," Robinson, who now runs Altana Wealth, said in a research note this week. "This was due to the large build up in strategies explicitly or implicitly selling volatility."

Low volatility had become so ingrained in the rising stock market that instruments betting on rising volatility were losing money – which led some to bet against it, according to Robinson.

The Dow Jones Industrial Average posted its biggest single-day loss since 2011 on Monday 5 February. Two "short vol" investment products created by Credit Suisse and Nomura – which had previously posted strong gains – nose-dived and were shut down following the accompanying spike in volatility. City Financial's Decca Fund, run by former Hutchin Hill trader Shahraab Ahmad, lost a quarter of its value in the stock market rout because of short-volatility positioning, according to a Bloomberg report.

"The short VIX strategy may have made double-digit returns in good times but then it lost 95-100% of your capital when it entered the inevitable bad times," said Robinson, commenting on market losses rather than his own fund. Altana's Volatility Fund, which runs $300 million, sells insurance on volatility expectations, and its gains or declines are based on whether realised volatility is higher or lower than expected.

"If you think about the mindset of these short VIX trades and what we're actually doing, it couldn't be further apart," said Robinson. The fund was down 2% for the month as of earlier this week.

Funds posting high losses "spent all their time thinking about the nice things that happen in normal times and – make no mistake – capturing a double-digit roll yield in a futures contract can be a fantastic strategy," he added. "However, they casually left out what happens if something goes wrong."

Robinson founded London and Monaco-based Altana in 2009 to manage his family wealth. It has subsequently taken in some external investment.

The Australian previously rose to prominence as a portfolio manager for Tudor and then co-founder of Trafalgar, which posted strong event-driven returns in noughties markets and managed more than $3 billion at its peak.