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# When calm **no longer** **means safe:** navigating a new volatility regime



**Equity market volatility is shifting into a new regime where quiet markets can snap violently without warning. With these sudden, fleeting spikes turning volatility into a roller coaster, investors may need nimble, actively managed protection rather than static, set-and-forget hedges.**

Volatility is the measure of how quickly markets move up and down. For investors, volatility is important as it can affect the value of their holdings. But patterns of volatility in equity markets are changing.

In the past, sharp rises in implied equity index volatility – the market’s expectation of how much an equity price will fluctuate in the future – used to be relatively rare. When it did surge, the move back to more normal levels tended to be gradual – hence the phrase “elevator up and *stairs down*”.



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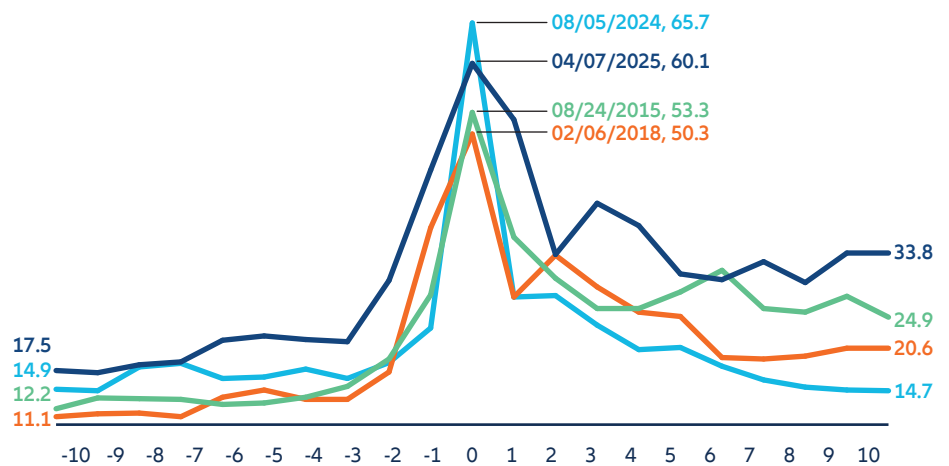
## Key takeaways

- Volatility behaviour is becoming more erratic – even periods of low volatility no longer mean low risk as falling stock correlations mask underlying fragility and leave markets vulnerable to abrupt dislocations.
- Five structural forces – from options trading growth to volatility targeting – now drive more frequent, sharper volatility spikes.
- Investors can benefit from actively managed protection strategies that adapt to shifting volatility, pricing, and correlations.
- Effective volatility management requires going beyond the headline VIX level and focusing on other factors, such as the term structure, skew, volatility risk premium, and dealer positioning, to understand the true market risk.

More recently, including during the latest Middle East conflict, volatility behaviour has become more erratic. Extended periods of calm have been punctuated by sudden, short-lived spikes. And perhaps most striking about the pattern is that the moves down have been about as sudden as the moves up (see Exhibit 1). “Elevator up and *elevator down*” may be a more apt description.

Our analysis finds that spikes in the VIX Index (known as Wall Street’s fear gauge) that used to occur every three to five years now appear every year. And the time for volatility to subside has halved, from around 25 days to only nine days.

**Exhibit 1: Pointy peaks: recent intraday peaks in the VIX Index reflect sharp up and down movement in volatility**



Days before and after intraday peaks of VIX Index, value at 0 indicates the intraday high of that day

Source: Allianz Global Investors calculations using Cboe Volatility Index data. Data as at 31 December 2025.

[Read our full research about changing volatility patterns – and what this means for portfolio management](#)

## Don’t be fooled by low volatility

In our view, the change in volatility patterns signals a striking disconnect between real-world risks and the market’s assessment of how much volatility they could trigger. Periods of calm in volatility markets may not always fully reflect the level of risk posed by uncertainties ranging from artificial intelligence (AI) to geopolitical upheaval, climate change or fears of recession and inflation. These factors could fuel fresh volatility.

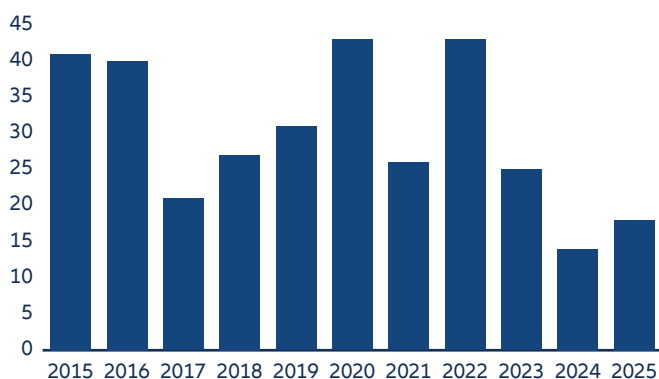
Digging deeper, we find that the main reason for the low implied index volatility often observed over the last several years is the decline of the implied correlation among single-name stocks. In other words, individual stocks are expected

to be less in sync with one another in the future (see Exhibit 2). But volatility around individual stocks has remained elevated throughout the period (see Exhibit 3). So, even though individual stock volatility might be high, because stocks are moving less in sync, the index looks calm.

The dynamic creates a misleading environment of “low volatility, medium risk” that is vulnerable to sudden dislocations. For investors, such conditions can mean that the cost of protecting their portfolio against market downturns (for example, by using put options) sometimes does not reflect the underlying market risks.

**Exhibit 2: In recent years, markets expected stocks to be less in sync than in the past**

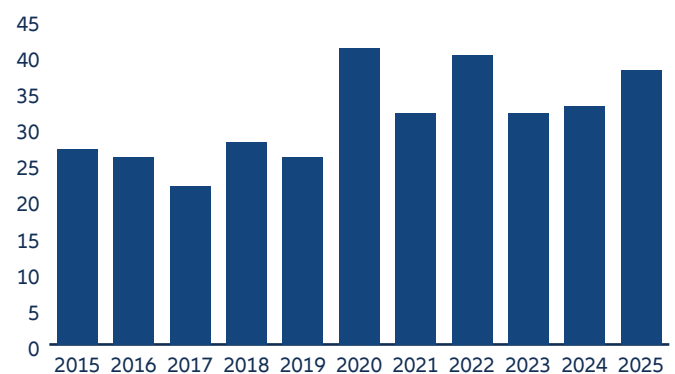
Average implied correlation of the top S&P 500 on a year-by-year basis



Source: Allianz Global Investors calculations. Cboe Implied Correlation 1M 50 Delta. Data as at 31 December 2025.

**Exhibit 3: Volatility levels for individual stocks have risen in recent years**

Average single-name volatility on a year-by-year basis



Source: Allianz Global Investors calculations. Cboe S&P 500 Constituent Volatility Index. Data as at 31 December 2025.

## Five structural shifts behind changing volatility patterns

What lies behind this change in volatility behaviour? It reflects a set of structural shifts over recent years in how markets trade. We've identified five key factors to explain the change in volatility dynamics:

### 1. Explosion in options trading and introduction of short-term options maturities:

The rapid growth in listed options trading and the rise of zero-day-to-expiry (ODTE) contracts – which expire the day they are traded – have fundamentally altered volatility dynamics. The flows stemming from these very short-dated contracts can intensify intraday dealer hedging, creating rapid feedback loops that cause sharp but fleeting volatility spikes. So far, this risk hasn't fully materialised, reflecting relatively balanced flow in these options and the fact that most structures have been traded as spreads. Should this change, ODTE may become a bigger risk for larger-than-expected daily moves.

### 2. Emergence of new liquidity providers and changes in regulations:

The onset of regulations after the 2008 global financial crisis reduced the capacity of banks to fulfil their traditional role as market makers. In their place, electronic liquidity providers have emerged as the dominant players. But their tendency to withdraw during periods of market stress has resulted in thinner liquidity and faster volatility spikes during market shocks. At the same time, these firms are typically among the first to resume pricing once the spike subsides, which helps volatility normalise more quickly.

### 3. Growth in options-based and leveraged exchange-traded funds:

The surge in popularity of call-overwriting strategies (those that sell a call option on a stock or index that an investor owns) has dampened implied volatility. However, when markets fall, volatility rises, allowing investors to sell a smaller amount of call options to earn similar premiums to the normal market environment. As a result, during market stress, call overwriting strategies provide a smaller dampening effect against market swings, leaving markets more exposed to sudden spikes in volatility.

### 4. Rise of retail options trading:

Retail participation in options markets has grown rapidly since the Covid-19 pandemic, fuelled by zero-commission trading, easy-to-use platforms, and the rising popularity of meme stocks. Although



smaller in size than institutional flows, retail traders tend to concentrate in very short-dated, high-leverage contracts that distort dealer positioning and reduce local liquidity. This behaviour forces dealers into reactive hedging that amplifies market moves, contributing to sharp but short-lived spikes in volatility that can interact with broader structural forces to intensify intraday swings.

### 5. Growth of volatility-targeting approaches:

Strategies targeting volatility mechanically adjust equity exposure to maintain a set volatility level, increasing equity weights in calm markets and reducing them sharply when volatility rises. This behaviour reinforces market stability during quiet periods but amplifies sell-offs when volatility spikes, as systematic de-risking adds to downward pressure. Once volatility fades, these strategies rapidly re-enter the market, helping volatility normalise more quickly and shortening the duration of spikes. Given their widespread use across large institutional pools of capital, they have become an important structural driver of today's "spiky but short-lived" volatility regime.

## An active approach can help navigate a new volatility regime

These five structural forces have made volatility spikes more frequent, sharper, and faster to develop. Higher trading volumes and shorter-dated options may not fully explain how quickly the VIX can move. But their effects become much stronger when combined with stricter banking regulations, market maker concentration, exchange-traded funds (ETF) growth (including leveraged products), greater retail involvement, and expanded volatility-targeting strategies.

Periods of very low volatility should not be interpreted as periods of low market risk. In fact, they often create attractive opportunities to use options and volatility instruments for protection purposes. This is especially important because traditional safe-haven assets have become less reliable, and bonds increasingly behave like risk assets. Cheap equity index put options can be used for tail-risk hedging, but these strategies need to be actively managed. They must adjust as option prices, implied volatility, and implied correlations change.

## Ways to manage volatility within a portfolio

**We think there are several factors that can help improve portfolio performance through effective volatility management:**

**Integrating volatility into portfolio thinking:** Rather than relying on static hedges, a more flexible approach may be beneficial. Using calm markets to secure reasonably priced protection may make portfolios more resilient, helping investors stay invested in rallies while better guarding against sudden drawdowns

**Avoid complacency during calm markets:** Low headline volatility can sometimes mask underlying risks. For example, even when the VIX is near historical lows, there may be opportunities to benefit from differences in implied volatility among options with the same expiration date but different strike prices (the price at which an option can be exercised).

**Identify more attractively priced protection:** The difference between implied and realised volatility – the volatility risk premium – is also important. A wide premium may make volatility-selling strategies attractive.

**Adapt hedges dynamically:** A wide volatility risk premium may also indicate higher hedging costs for investors seeking protection, underlining the importance of an active approach to hedging. And it is important to understand how dealer positioning affects markets, as their hedging can either smooth or magnify price moves.

**In summary, a dynamic approach to shifting volatility pressures is essential for investors seeking to remain protected from market swings without forfeiting upside.**

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