MARKET TRACTION

Hell-bent for the All-Time-High or Headfake? Que Sera, Sera!

This Week's Trade Ideas:

Bullish Ideas: (View Webinar)

M > Macy's Inc. > $24.67 Last. Buy the April 26th 23 Calls for $2.00 or less with a close or anticipated close above $24.75 in an up market with expectations for continued strength in the major indices.

Bullish Mentions: **(View Webinar)**

Based upon closing prices and all assume an up market with expectations for continued strength in the major indices.

AAPL, FB, TTWO, FMS (may still have room to run).

Bearish Ideas: (View Webinar)

CMCSA > Comcast Corp. > $40.02 Last. Buy the April 18th 40 Puts for $0.75 or less with a close or anticipated close below $39.60 in a down market with expectations for continued weakness in the major indices.

Bearish Mentions: **(View Webinar)**
Based upon closing prices and all assume a down market with expectations for continued weakness in the major indices.

CAH (trigger < $47.00), ABC (riskier due to recent large drop), EA (but away from "big drop" level).

We strongly suggest viewing this week's **Morning Call** webinar for full details with respect to these idea(s), last week's and options education.

Special Note:

Remaining nimble is a focus in the newsletter and in our **Morning Call** webinar and will remain so.

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Market Overview:

We're at the point where we have to treat it as a breakout until it's not, which it easily could be with a gap lurking below and a doji following right on the heels of the *breakout*. The scenario wherein the Gang strings out higher stock prices until earnings hit the tape seems to be unfolding thus far. Dojis aside, they truly seem hell-bent on lifting the indices to a test of the all-time highs.

Below the Radar:

Eventually reality will intrude in this pleasant madness: either the global economy slips into recession and corporate profits tank, kicking out the props of high stock valuations, or global growth resumes, opening the door to stock-market-killing rate increases and balance sheet reductions.

What if we're all not crazy? It seems unlikely but still, what if…???

Morgan Stanley may be crazy too. They may be getting even crazier because they've jacked-up the probabilities that the graveyard may whistle back very soon or that the market will stop trading out of both sides and face the economic deterioration it's pretending doesn't exist:

Options Academy:

Folks are always looking for ways to capitalize on earnings releases. Quite often earnings news and guidance can trigger explosive movement which can be lucrative for those on the right side of it. Naturally, this draws great interest and options markets reflect these facts and thus "earnings" contracts that have expirations just after earnings releases often see their prices (implied volatility levels) rise significantly. Many players, knowing that earnings can drive great movement will seek to acquire the at-the-money straddle as it will allow them to profit regardless of which way the stock moves AS LONG AS THE STOCK PRICE MOVES A LOT! (more than the straddle buyers paid for the straddle).

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MARKET TRACTION

Outlook:

Last week's Outlook:

"… tedium remains in theaters everywhere. A break of key levels would be nice right about now!"

Tedium stayed in place until Friday when we got another one of those upside futures gaps on a mere muttering of "China deal blah, blah, blah…". Monday brought an even bigger overnight gap that wouldn't quit. Naturally, most of these uprisings continue to occur with generally weak economic news surrounding them. A doji appeared today and that brings the "breakout" into question. Yet, they sure seem hell-bent to revisit those all-time highs as we've talked about many times over the past month.

Technicals:

Will be discussed in-depth in the **Morning Call** webinar.

Fundamentals:

These trade idea(s) and mentions are technically-driven.

(Editor's note: These trade ideas may be updated periodically, in keeping with market conditions. It is intended solely for educational purposes.)

Recap of Last Week:

Last week delivered an even more bland "NOTHINGBURGER" than the prior week's *burger*. That is, until Friday's closing out of Q1 shenanigans which were followed by Monday's curious gap up.

FCX was our play-it-safe bull idea last week. It did give us some upside movement, but it stalled today along with the market. We spotted it at $12.70 but wanted to see it move above $13.05 so it would show us something, which it didn't. It closed today at $13.12 so no harm done.

VLO, BHGE, HFC, PSX were all energy related names and that group didn't rally along with the indices. Our trigger lines have collected dust in energy.

FMS moved up a couple of bucks and that's it.
DOX* remains in snooze mode a week later.
ADS was a bright spot for us, and it moved up over $9 from publication after taking out the trigger level.
JNJ was another disappointment than couldn't muster a close over $140.00 as we needed it to.

MYL was the triangle-trapped bear idea from last week and it closed down nearly a whopping 50c from publication. It's a whopping 33c below our trigger level as of today's close! Ugh! Blech!

KRE, we needed a break below a support line, and we got nothing close. In fact, we got the opposite. It didn't even sniff the $49 level and ran strongly to the upside. We wish we'd been bulls!
FSLR, see **KRE**. No seriously see **KRE**. The same fate awaited us here.

MARKET TRACTION

Since the joke will get old, **MGM, TXN, AIG** were the remaining bearish mentions and they all followed the same script. They all took a gander at the support levels we hoped they'd crack and ran in the opposite direction and haven't looked back. Maybe that's why they call 'em support levels…

In summary, and to paraphrase Barry Corbin: "…after very careful consideration, we've come to the conclusion that last week sucked."

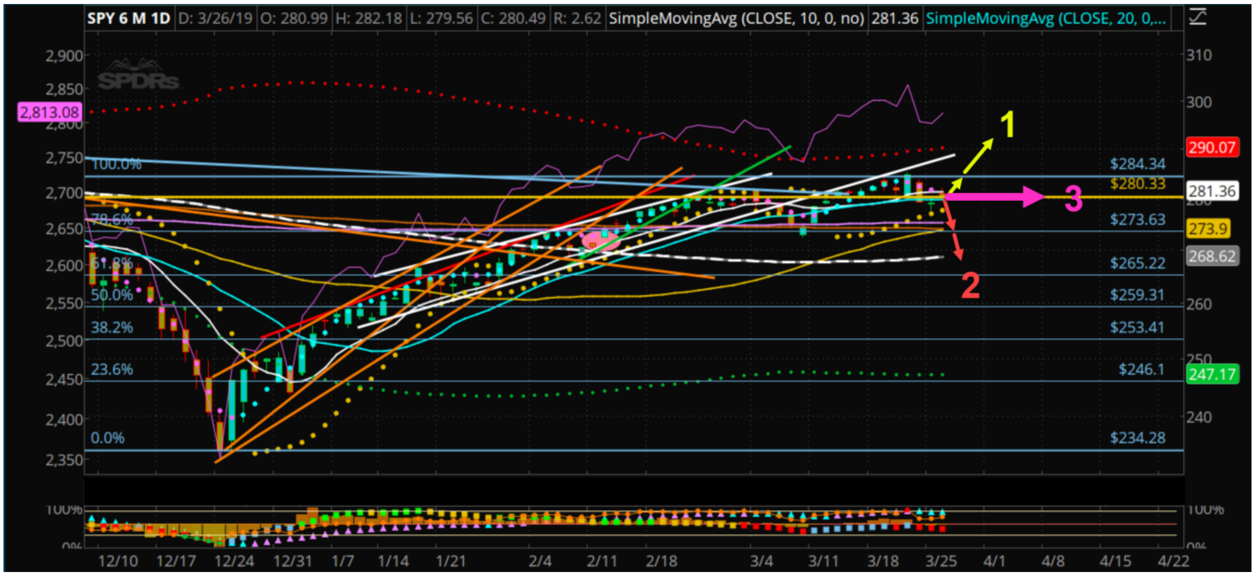
The ideas went a little in the direction we expected but nearly all mentions ignored our triggers. The bears didn't even attempt to break down below them with the market endlessly levitating. The only bull that really delivered was **ADS.** That's the disappointing part. With 9 total bullish names we'd expect a lot more. Granted, we stayed away from high profile names but…

The past week has been a hard one. The overnight nature of the movement probably shut most people out of what little pop there's been regardless.

This listlessness can't end soon enough.

Market Overview

Last week was mostly our Path 3 but began to morph into Path 1 on Monday:



We finished up Market Overview this way:

Up, down, now in the middle. It's back to a slightly elevated level as well. The marketplace itself is confused. It's simple. We have to wait longer for the reveal. It's frustrating but it's much better than being chopped up!

The "reveal" didn't really come until Monday's pop via another night owl jam-job in the futures. That put us over the highest recent high and above SPYs $284 which has been the level we've been watching for a week or so. However, today brought a doji which shouldn't shock us since the theme of the past 3 weeks has been "indecisiveness". Why not call what could be a breakout… immediately into question?

MARKET TRACTION

We're at the point where we have to treat it as a breakout until it's not, which it easily could be with a gap lurking below and a doji following right on the heels of the *breakout*. The scenario wherein the Gang strings out higher stock prices until earnings hit the tape seems to be unfolding thus far. Dojis aside, they truly seem hell-bent on lifting the indices to a test of the all-time highs. Does it make sense? Not really from where we sit but let's not forget that *making sense* doesn't matter. The momentum remains up and with the bulls. They may have paused for 3 weeks but they're trying to move 'em again now and barring a quick failure and gap closure, they have to be given the benefit of doubt. After all, who'd have believed that we'd jam up double digits in Q1 and be less than 3% from all-time highs while folks were taking sleigh rides to grandma's house at yuletide?

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The Gang has the NASDAQ < 2% from closing the October gap. Think about how talented they really are for a moment. Apple would appear to have issues, which puts it mildly. FB and GOOGL continue to treat 1984 as if it's a playbook to execute in real-time to achieve great wealth or something, while at least one of them prostrates themselves begging to be regulated. More players are trying to elbow their way into NFLX's kitchen. And AMZN, well they just keep chugging along. Despite issues here, there and nearly everywhere in FAANG, the *NAZ* has its MOJO back! Samsung may be warning us but no one wants to listen!

We find it hard to fathom that the Gang will get this close to achieving gap-filling immortality and not get the job done. Heck! Even the financials are seeking to join the party!:

The VIX, at least for now, seems to have decided to turn tail and come to grips with the script, err, reality:

MARKET TRACTION

Perhaps most importantly, at least as perceptions go, is China. Chinese equities have approached resistance and won't need much to breakout:

This party looks primed to continue. Could we witness a weak open on Wednesday on bad news out of the blue? SURE, anything is possible. Our bottom line however is that the FED has trumped all concerns and the Powell Put seems to have wings. Bulls won't stop trying to push higher until if and when earnings deteriorate even more than they've been forecasted to, and CEOs and CFOs deliver somber news on those conference calls. Barring unexpected news, they'll keep marching to Powell's sweet music.

MARKET TRACTION

The calendar backs off a little this week but what's the difference? It hasn't mattered all that much for months. FED speakers contradicted the FED's EZ $ track and that didn't matter. Economic numbers have swooned and that hasn't mattered. It's all animal spirits and *Algos* at this point. Que sera, sera!

This Week's Economic Calendar

TIME (ET)	REPORT	PERIOD	ACTUAL	MEDIAN FORECAST	PREVIOUS
MONDAY, APRIL 1					
8:30 am	Retail sales* (new date)	Feb.	-0.2%	0.3%	0.7%
8:30 am	Retail sales ex-autos* (new date)	Feb.	-0.4%	0.4%	1.4%
9:45 am	Markit manufacturing PMI (final)	March	52.4	--	53.0 (Feb.)
10 am	ISM manufacturing index	March	55.3%	54.6%	54.2%
10 am	Construction spending	Feb.	1.0%	-0.1%	2.5%
10 am	Business inventories* (new date)	Jan.	0.8%	--	0.6%
TUESDAY, APRIL 2					
8:30 am	Durable goods orders* (new date)	Feb.	-1.6%	-2.1%	0.1%
8:30 am	Core capex orders* (new date)	Feb.	-0.1%	--	0.9%
Varies	Motor vehicle sales	March		16.8mln	16.6mln
WEDNESDAY, APRIL 3					
8:15 am	ADP employment report	March		--	183,000
8:30 am	Raphael Bostic, Tom Barkin, Esther George speak				
9:45 am	Markit services PMI (final)	March		--	54.8
10 am	ISM nonmanufacturing index	March		58.1%	59.7%
5 pm	Neel Kashkari speaks				
THURSDAY, APRIL 4					
8:30 am	Weekly jobless claims	3/30		216,000	211,000
1 pm	Loretta Mester speaks				
FRIDAY, APRIL 5					
8:30 am	Nonfarm payrolls	March		179,000	20,000
8:30 am	Unemployment rate	March		3.8%	3.8%
8:30 am	Average hourly earnings	March		0.3%	0.4%
3 pm	Consumer credit	Feb.		--	$17 bln
3:30 pm	Raphael Bostic speaks				

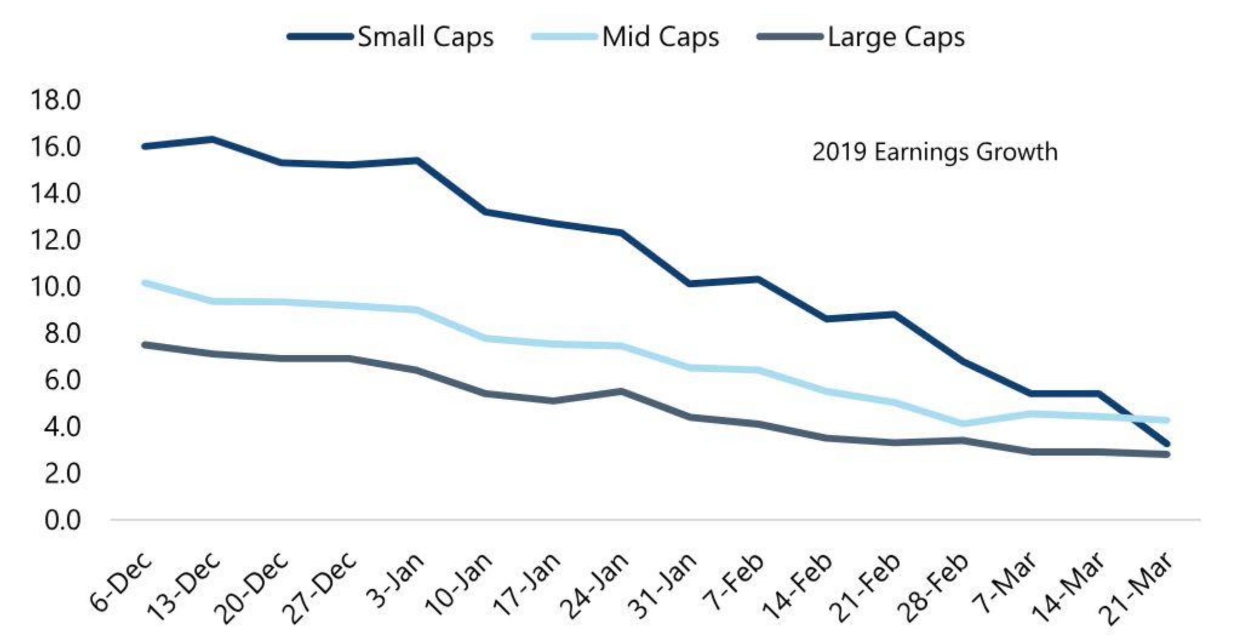
Below the Radar

"What really concerns me is the performance of small and mid cap stocks," Carlos Dominguez, chief investment officer at Element Pointe Advisors said in an interview. That the Russell 2000 ***RUT, -0.18%*** *remains more than 10% below its August highs is a red flag for the broader market, he added.* ***"Small-caps usually lead in a bull market, but they're actually leading to the downside," he added.***

https://www.marketwatch.com/story/why-a-very-ugly-reporting-season-for-small-caps-is-bad-news-for-stock-market-bulls-2019-03-27

With that, we begin **BTR** with more not-so-good news that's likely to be ignored! We'll press on regardless:

Chart 1 - '19's earnings growth has tumbled dramatically since the start of year



Source: FactSet; Standard & Poor's; Jefferies

*Steven DeSanctis, small-and-mid-cap equity strategist at Jefferies warned clients in a Wednesday research note that "****it could be a very ugly reporting season" for small-cap stocks given the speed and severity of cuts to earnings per share, or EPS, estimates.***

Indeed, revisions for the current quarter have been historically large for small and large-caps alike. Over the past decade, the average reduction to earnings for companies in the Russell 2000 has been 12.2%, while analysts have lowered their estimates for first-quarter earnings by 13.5% since Dec. 31, according to FactSet data.

"There is no question that estimated growth is falling fast across size, sector, and style, as companies have taken a more conservative stance to 2019," DeSanctis wrote, pointing out that ***Wall Street expects earnings for Russell 2000 companies to fall by 14.5% in the first quarter and 4.3% in the second quarter. Analysts are still projecting full-year earnings growth****, largely on the belief that the U.S. economy will rebound in the last six months of 2019, powering small-cap EPS to a rise of 12.6% in the fourth quarter.*

This news, should it come to fruition, seals the deal for **BTR**. We've been chronicling the US slowdown that the stock market has been ignoring for 6 months. Our finds were on it, but the FED's capitulation is all that matters for now on Wall St.

We've now covered the corporate earnings part of the equation, at least, mostly in a domestic sense.

Now, we'll turn our attention elsewhere with a check on *Main St.* that shows some rather unpleasant developments there as well:

http://theeconomiccollapseblog.com/archives/retail-layoffs-are-92-percent-higher-in-2019-and-now-even-wal-mart-is-quietly-closing-stores

According to Challenger, Gray & Christmas, ***retail layoffs were up a whopping 92 percent in January and February compared to the same period a year ago.*** *The following comes from NBC News…*

More than 41,000 people have lost their jobs in the retail industry so far this year — ***a 92 percent spike in layoffs*** *since the same time last year, according to a new report.*

And the layoffs continue to mount, with JCPenney announcing this week it would be closing 18 stores in addition to three previously announced closures, as part of a "standard annual review."

Yes, competition from Internet commerce is hurting the traditional retail industry, but it certainly doesn't explain a 92 percent increase.

And very few retailers have been able to avoid this downsizing trend. At this point, even the largest retailer in the entire country has begun "quietly closing stores"…

Walmart is closing at least 11 US stores across eight states.

The stores include one Walmart Supercenter in Lafayette, Louisiana, and Walmart Neighborhood Market stores in Arizona, California, Kansas, South Carolina, Tennessee, Virginia, and Washington.

For decades, Wal-Mart has been expanding extremely aggressively.

They have plenty of cash, and so the only way that it would make sense for them to close stores is if they anticipated that we are heading into a recession.

Now that we're here, we're going to push you to here:

https://www.mauldineconomics.com/frontlinethoughts/recession-signs-everywhere

We've haven't considered everything but the lengthy installment to be found there does expand our coverage that includes this:

MARKET TRACTION

This month, the Federal Reserve joined its global peers by turning decisively dovish. Jerome Powell and friends haven't just stopped tightening. Soon they will begin actively easing by reinvesting the Fed's maturing mortgage bonds into Treasury securities. It's not exactly "Quantitative Easing I, II, and III," but it will have some of the same effects.

Why are they doing this? One theory, which I admit possibly plausible, was that Powell simply caved to Wall Street pressure. The rate hikes and QT were hitting asset prices and liquidity, much to the detriment of bankers and others to whom the Fed pays keen attention ***. But that doesn't truly square with his 2018 speeches and actions. The Fed's March 20 announcement suggests more is happening.***

I think two other factors are driving the Fed's thinking. One is increasing recognition of the same slowing global growth that made other central banks turn dovish in recent months. The other is the Fed's realization that its previous course risked inverting the yield curve, which was violently turning against its fourth-quarter expectations and possibly toward recession. *That would not have looked good in the history books, hence the backtracking.*

And now, we'll visit Charles Hugh Smith who along with us, seems to believe that the market is whistling past…or something to the same effect. Go here to read the nugget that follows the link and more!:

http://charleshughsmith.blogspot.com/2019/04/dear-stock-market-you-cant-have-it-both.html

Eventually reality will intrude in this pleasant madness: *either the global economy slips into recession and corporate profits tank, kicking out the props of high stock valuations, or global growth resumes, opening the door to stock-market-killing rate increases and balance sheet reductions.*

What if we're all not crazy? It seems unlikely but still, what if…???

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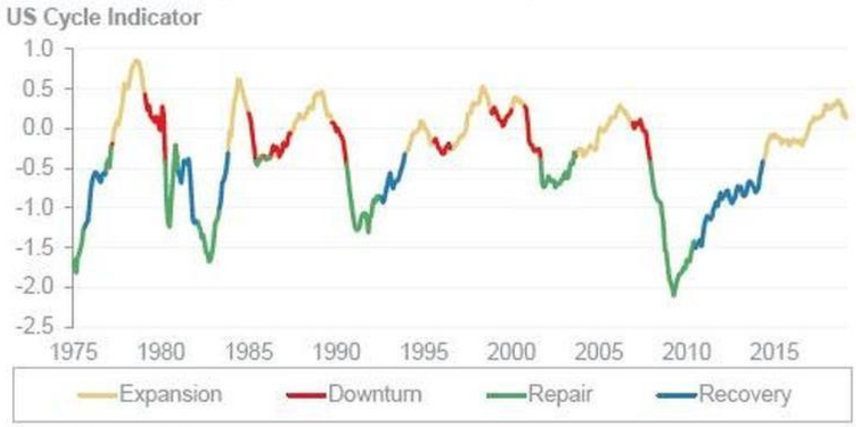
Morgan Stanley may be crazy too. They may be getting even crazier because they've jacked-up the probabilities that the graveyard may whistle back very soon or that the market will stop trading out of both sides and face the economic deterioration it's pretending doesn't exist:
https://www.zerohedge.com/news/2019-04-01/morgan-stanley-sees-70-chance-downturn-early-next-month

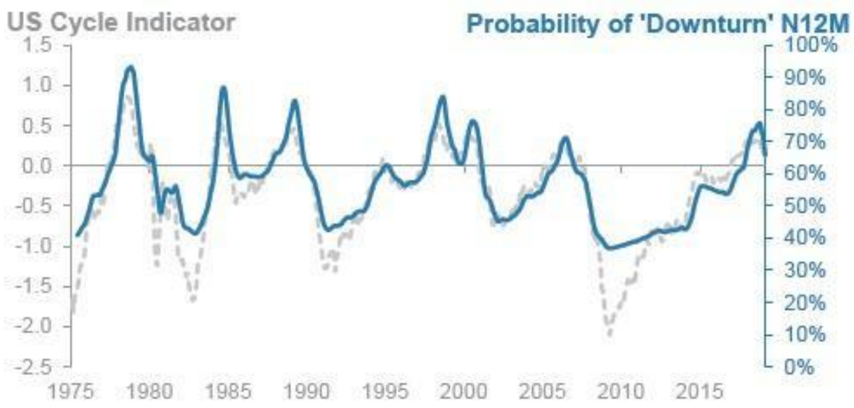
Exhibit 1:

Our updated US cycle indicator is still in expansion...



Source: Morgan Stanley Research

But:



Source: Morgan Stanley Research

Morgan Stanley's updated US market cycle indicator is still in expansion, a phase in which it has been since 2014, ***the bank is now estimating that there is a 70% likelihood that this will shift to downturn over the next 12 months,*** *and that* ***if the recent deterioration in data persists, we could see "a switch from expansion to downturn as early as next month.****"*

Remain nimble my friends!

Bank and Roll!

Options Academy – Preaching the "Poor Man's Straddle" – Sort of…

We're re-running this lightly edited tale of applying the "poor man's straddle" as earnings season is just about here, and we know that folks are getting itchy to make the "easy money" that earnings reports will soon bring. Read on you wheeler-dealers! The "poor man's" is a great alternative but not invincible!

A few earnings reports will trickle out here and there for the two weeks but we're about 20 days away from earnings season kicking in for real. With that in mind, we thought it might be a good idea to briefly review the "poor man's straddle" concept.

Folks are always looking for ways to capitalize on earnings releases. Quite often earnings news and guidance can trigger explosive movement which can be lucrative for those on the right side of it. Naturally, this draws great interest and options markets reflect these facts and thus "earnings" contracts that have expirations just after earnings releases often see their prices (implied volatility levels) rise significantly. Many players, knowing that earnings can drive great movement will seek to acquire the at-the-money straddle as it will allow them to profit regardless of which way the stock moves AS LONG AS THE STOCK PRICE MOVES A LOT! (more than the straddle buyers paid for the straddle). In fact, the ATM straddle price is often referred to as the "implied price move" that's expected by options market participants. The problem with buying the straddle is that it is normally very expensive relative to normal times and if the earnings produce a "dud" reaction, the owner of the straddle is typically crushed mercilessly shortly after the stock and options markets open post-earnings. Thus, earnings straddle buying is often high-risk/ high-reward. It's this dilemma that can make the "poor man's straddle" attractive but there can be a catch...

As the name implies, the "poor man's" acts like a straddle in some ways but it is a less expensive option that doesn't deliver unlimited profit potential. As always in economics, there's a trade-off. And it stays consistent in finance; the reward is commensurate with the risk. Let's look at examples of both to compare the main pros and cons…

(EDITOR's NOTE: This appeared 2 weeks prior to NFLX's earnings report)

NFLX is reporting on July 17th and as a result the July 21st expiration options are priced dramatically higher than non-earnings expirations have been historically. With the stock price near $148.00, those options are thus the ATMs and the ATM straddle is trading for about **$13.60** at present. This suggests that the options markets participants are willing to pay that much for the straddle because they believe the earnings release will produce a move larger than that and thus, they will profit. Of course, that could happen and if it were to happen the owner of the straddle could enjoy virtually unlimited profits as they own both a call and a put and are not short anything against them. The other side of the coin in this case would be an earnings release dud. If the earnings produced virtually no movement, it's possible that in very short order, the straddle value could fall all the way to say **$5.60**! Remember, there would be very few days left until expiration (7/18 vs. 7/21) of those contracts and the NFLX news is out. This "all or nothing" type proposition is what makes betting in both directions with earnings options so risky. Now let's look at the poor man's…

The poor man's straddle consists of shorting a calendar aka time spread. Normally we seek to be long the calendar spread to profit via differing rates of decay. We know that the calendar is worth the most when the stock price is at the strike of the calendar spread in focus, in this case, the $148.00 strike. If we know that, then we also know that the calendar spread will lose value if the stock price moves away from the ATM calendar in either direction. Thus, we profit much like true straddle owners; we make money if the stock price moves in either direction away from the ATM strike on the earnings news.

We're going to have to extrapolate values because the perfect options to compare do not currently exist in the marketplace. Fortunately, our trusty options calculator produced these apples to apples results:

Aug. 4th Exp 148 call value = $7.50

Dec. 15th Ep 148 call value = $13.80

Thus:

(Dec. 15th Exp 148 call value = $13.80) - (Aug. 4th Exp 148 call value = $7.50) = $6.30 Calendar Sale Value

Let's assume we sell the calendar spread the same day we'd buy the straddle and let's also examine how the poor man's would fare with no post-earnings movement or a big move up or down. Keep in mind that we used historical real-world post-earnings volatilities as inputs to produce these values. In other words, we used the volatility tilt (aka the term structure of volatility) across time to approximate the values as fairly as we could. The day after earnings is July 18th. On that day with the stock price unchanged from where we sold the calendar (due earnings reaction) its value would be:

Aug. 4th Exp 148 call value = $4.37

Dec. 15th Ep 148 call value = $13.02

Thus, post-earnings the calendar value would be:

(Dec. 15th Exp 148 call value = $13.02) - (Aug. 4th Exp 148 call value = $4.37) = **$8.65** Calendar Sale Value

Since we sold the calendar originally for **$6.30**, it's new value would leave us in the hole by **$2.35**. That's not a surprise since we used the poor man's straddle and the earnings were a dud! However, we'd have lost a lot less than the $8.00 that genuine straddles owners would have!

HOWEVER, let's now look at a $15.00 move up and down. We're going to jump to the results to save space:

$15 Move Up: @ $163.00 the post-earnings calendar with realistic vol. assumptions is worth: **$6.45**

$15 Move Down: @ $163.00 the post-earnings calendar with realistic vol. assumptions is worth: **$5.55**

Since we sold the poor man's at $6.30, here are the net results:

$15 Move Up: **$0.15 LOSS**! (per contract x 100 shares)

$15 Move Down: **$0.75** Gain (per contract x 100 shares)

WHAT??? Isn't the poor man's straddle supposed to be the *smart play*?

The answer is YES, it can be BUT… clearly in this example it is not a windfall even if we win. The main reason for this is the realistic volatility assumptions that we're using. What's happened in NFLX is that the marketplace has evolved to not only anticipate how participants are likely to play the ATM straddle but also how many of them will attempt to capitalize on movement in other ways and thus volatility levels are reflecting that reality. The poor man's can work very well but investors need to perform research on the respective volatility levels of the options/expirations that they're utilizing to initiate the trade. It's not just as easy as slapping this crafty strategy on and collecting money!

It's worth noting that much bigger moves in NFLX would help us potentially but we can't regularly count on super-outsized moves to make us profits.

This example suggests that the thorough bird may not always get the worm, but they may be able to consistently avoid losing their shirt, and time, and commissions, and focus, and so on…

Hopefully this cautionary tale will help you to steer clear of volatility traps. If you have questions, please ask away in our next **Morning Call** webinar. 😊