MARKET TRACTION

On the Eve of a Melt Up or Melt Down – Or So It Seems…

<u>IMPORTANT REMINDER:</u> As we announced last week, this will be the FINAL Market Traction newsletter and tomorrow morning will be the final webinar as we will no longer be offering the service. We were offered the opportunity to co-manage 6, and soon to be more, active specialized trading services that vary in directive from what we were asked to do here.

As a loyal subscriber, we can arrange to send you a completely free copy of Jon and Pete Najarian's new book, Follow the Smart Money, and offer you a chance to try their new, yet similar, subscription service – TNT Options, for free for 30 days that we happen to co-manage. Please email us at WR@OPTREV.com. Thank you.

A VERY SPECIAL NOTE:

As noted above, this is our final installment of this newsletter. The past 2+ years have been very good to us overall, though this final month has us nearly bored to tears! We will however provide updates through April 30th. Hopefully, there will finally be a good reason to do so! We wish to thank you all and wish you the very best moving forward. We hope to see you in our new offerings. Farewell!

This Week's Trade Ideas:

<u>Bullish Ideas: (View Webinar)</u>

ACB > Aurora Cannabis Inc. > $9.06 Last. Buy the May 17th 8.5 Calls for $1.00 or $1.05 respectively (trigger level dependent) or less with a close or anticipated close above $9.23 or $9.33 (**Aggressive Trigger $9.23/Conservative Trigger $9.33.**) in an up market with expectations for continued strength in the major indices and the cannabis complex.

<u>Bullish Mentions</u>: **(View Webinar)**

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

BOX (speculative – options volume), AMAT, AMD (earnings soon), TWLO (earnings soon).

<u>Bearish Ideas: (View Webinar)</u>

None at this time with the market on a wilding spree.

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

LB, XLP (reversal – options volume).

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.

MARKET TRACTION

Market Overview:
Remember: "…***bulls remain in control until they're not.***" We must stick with that take until the charts tell us not to, something they've yet to do. We've chronicled the disconnect between equities prices and the underlying realities of earnings revisions and slowing here and abroad but we always note that we must follow the charts. That remains the case now. They're on the verge of breaking the S&P 500 out above ATH resistance and thus there's not resistance beyond that. It may seem odd, crazy, whatever the case, but that's where we are at present.

Below the Radar:
Summing that up, nearly everyone is short volatility as conditions become more and more extreme! Let's not forget what a self-reinforcing cycle higher stock prices create! Everyone's in love and the main reasons are "optimism" and stocks are heading higher!

Options Academy:

One major gripe we have with vertical spreads, beyond the limiting of profit potential, is that they often require the trader to wait until very close to expiration to "max out" on the profit potential they do offer. That can get tricky…

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Outlook:

Last week's Outlook:

*Yet, **they sure seem hell-bent to revisit those all-time highs** as we've talked about many times over the past month.*

***They tried and came within 1 point of reaching the SPYs target. Is that it? We doubt it** but a little weakness is due after the past two weeks.*

*A target we've talked about seemingly forever and now only the All Time Highs will matter to the upside. A rising wedge is in place as are deteriorating fundamentals here and abroad. **Will it matter? It doesn't seem so**, but one can never be certain. **We have to be on Melt Up and Melt Down watch at the same time!***

And that's how things will end for us in our final edition. We're still on Melt Up and Melt Down watch this week and they still seem hell-bent on those all-time highs and they got to them on some indices but not all. Today we finally saw the breakout from our wedge and we're now seemingly on our way higher.

Technicals:

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

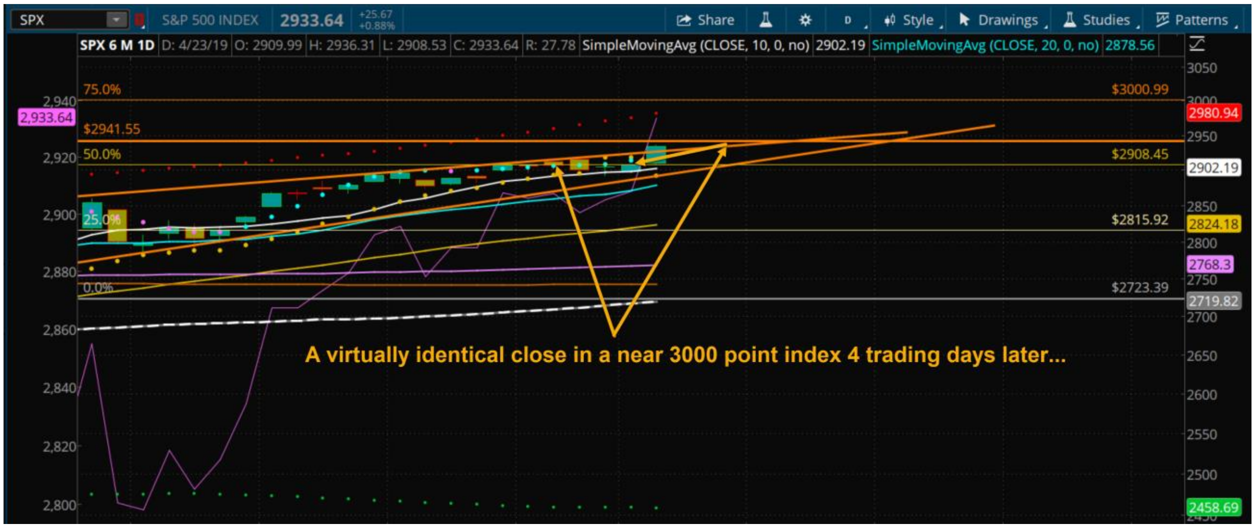
Fundamentals:

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:

A picture reveals the *nothing*:



Until today's wacky blast off, the **SPX** was virtually unchanged from last Tuesday until yesterday's close. The trading ranges were very narrow and the little weakness we saw coming last week lasted for 4 trading days, but the market held the 10 SMA support each time. It was more awfully boring action.

As we noted last week, we don't normally include a chart in our *Recap* but finding safe directional trades to push out in such an environment is nearly impossible.

As has been the case, names from prior weeks such as **AAPL** and **FB** for example, continued to push towards higher and higher targets we discussed many moons ago. Such has been this last month for us and our shorter-term efforts.

We had **BMY** and **Z** as bullish mentions, but both became frightened and ran away before crossing our trigger levels discussed in last week's webinar.

ABBV was the bearish mention and it promptly fell through our trigger and to the $77.00 target level too fast and then used today's mini-melt up to bounce back nearly all the way. The market was a little weak which as is usually the case, helped **ABBV** fall quite easily, too easily. It was nearly impossible for anyone to have gotten into it prior to a lot of drop.

Market Overview – Special Déjà Deux Edition

From last week's **MO:**

Now we either:

1. Pop through to challenge the ATHs.

2. Fail here and fall out of the wedge and likely find support a little lower.

Absent news, that seems to be it. ***If it is "1", we'll have to see how they act at the ATHs.***

*That's really it for now, seriously. That's how bound up things are****. Something must occur within days, technically speaking.***

Today finally brought us an attempt to leave the rising wedge. Today was a professional jam-jog higher and the Melt Up we referenced recently, seems to be on the verge of launching.

More from last week:

In short, things continue to become more reckless but ***that may not matter and for the record, the bulls remain in control until they're not. There's not much more to say than that until the latest "Rising Wedge in White" is resolved:***

The wedge resistance finally gave way today:

Remember: "…***bulls remain in control until they're not.****"* We must stick with that take until the charts tell us not to, something they've yet to do. We've chronicled the disconnect between equities prices and the underlying realities of earnings revisions and slowing here and abroad but we always note that we must follow the charts. That remains the case now. They're on the verge of breaking the S&P 500 out above ATH resistance and thus there's not resistance beyond that. It may seem odd, crazy, whatever the case, but that's where we are at present. The market has ignored nearly everything negative and is being gassed up on 2nd half of the year optimism from nowhere and the "FOMO" and short squeezing. BUT we want to be able to ride movement for profit and we seem to be on the verge of more upside. Could it be a false breakout? Sure, it always can but we have to deal with that if it comes not before as it may not play out that way.

It's frothy and it seems to want to get even more frothy. It may get MUCH crazier for all we know. There's no doubt that sobriety is hard to find at this point, but it is worth watching this video if you want a credible take on what's going on at this juncture:

https://www.cnbc.com/video/2019/04/23/earnings-growth-expectations-for-second-part-of-the-year-are-too-high-says-morgan-stanleys-mike-wilson.html?fbclid=IwAR171WLgLFmjbJ8vTw3Pfs8ieWjgEm7NnMdi-rBbO07JW1g134r2SRmvgtU

Today's Nasdaq liftoff was dramatic. Note that it has something akin to an inverted Head and Shoulders pattern and it seems to have blasted past the *neckline* today. As with nearly everything in trading, that portends a moonshot Melt Up or if it fails to fire, a serious Melt Down scenario. Rolling remains critical and becomes more so when it gets more VERTICAL.

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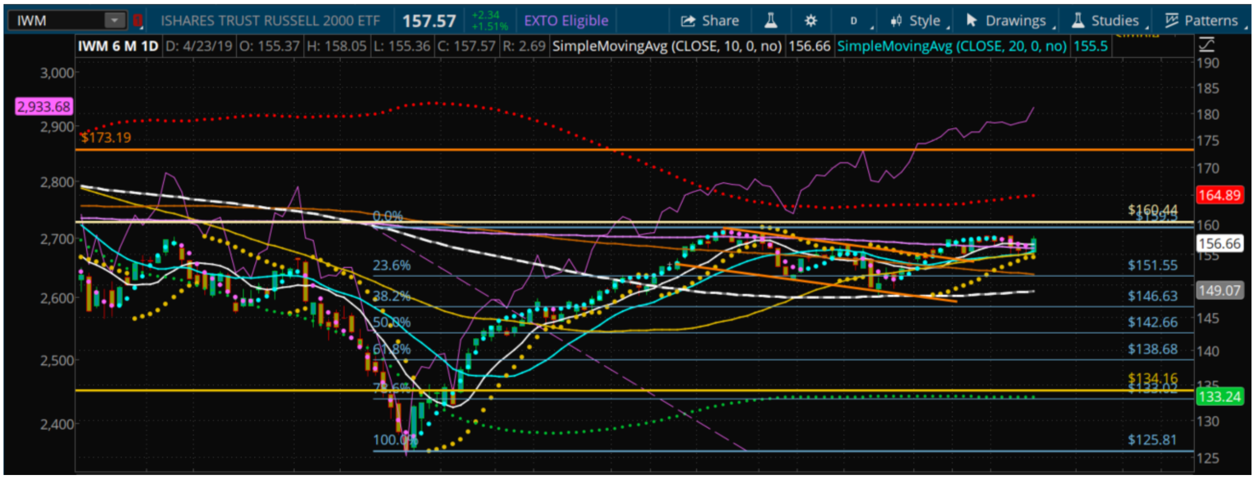
Not to be left behind, the DOW is within a whisker now too, and that's despite Boeing's plight:

The Russell 2000 is the only true laggard now and it had a very nice pop today:



Essentially, they've completely "fixed "nearly everything but the IWM and that's sent the VIX packing but not to new lows just yet. How did they do it? How did we go from snoozing to nowhere to "record breaking" suddenly? Well, the Gang goosed FAANG up by nearly 6% in just 1 week!!!

Any questions?

If we're truly on the eve of another disconnected from economic realities Melt Up, we have to go with the flow as we normally would and simply plan to be very, very aggressive rollers. If they blow right past today's highs, that's something we'll go with knowing that we're already slightly overbought, but we'll be ready to bank and roll or close at a moment's notice. Finally, could it be a head-fake? It certainly could but that should reveal itself quickly. If they don't continue to buy, buy, buy, that could be a tell.

The calendar is light this week but heavy next week. Friday could be something with GDP and Consumer Sentiment both due out. Nearly every day of next week has an important release in theory. As we noted last week, numbers haven't mattered much to the markets.

This and Next Week's Economic Calendars

TIME (ET)	REPORT	PERIOD	ACTUAL	MEDIAN FORECAST	PREVIOUS
MONDAY, APRIL 22					
8:30 am	Chicago Fed national activity index	March	-0.15	--	-0.31
10 am	Existing home sales	March	5.21mln	5.35mln	5.48 mln
TUESDAY, APRIL 23					
10 am	New home sales	March		660,000	667,000
WEDNESDAY, APRIL 24					
	None scheduled				
THURSDAY, APRIL 25					
8:30 am	Weekly jobless claims	4/20		202,000	192,000
8:30 am	Durable goods orders	March		0.5%	-1.6%
8:30 am	Core capex orders	March		--	-0.1%
10 am	Housing vacancies	Q1			
FRIDAY, APRIL 26					
8:30 am	Gross domestic product	Q1		2.6%	2.2% (Q4)
10 am	Consumer sentiment index	April		97.0	96.9 (March)

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TIME (ET)	REPORT	PERIOD	ACTUAL	FORECAST	PREVIOUS
MONDAY, APRIL 29					
8:30 am	Personal income	March			0.2%
8:30 am	Consumer spending	March			0.1% (Jan.)
8:30 am	Core inflation	March			0.1% (Jan.)
TUESDAY, APRIL 30					
8:30 am	Employment cost index	Q1			0.7%
9 am	Case-Shiller house price index	Feb.			
9:45 am	Chicago PMI	April			58.7
10 am	Consumer confidence index	April			124.1
10 am	Pending home sales index	March			-1.0%
WEDNESDAY,MAY 1					
8:15 am	ADP employment	April			120,000
9:45 am	Markit manufacturing PMI	April			52.4
10 am	ISM manufacturing index	April			55.3%
10 am	Construction spending	March			1.0%
2 pm	FOMC statement				2.25-2.5%
2:30 pm	Jerome Powell press conference				
Varies	Motor vehicle sales	April			17.5mln
THURSDAY, MAY 2					
8:30 am	Weekly jobless claims	4/27		--	--
8:30 am	Productivity	Q1			1.9%
8:30 am	Unit labor costs	Q1			2.0%
10 am	Factory orders	March			-0.5%
FRIDAY, MAY 3					
8:30 am	Nonfarm payrolls	April			196,000
8:30 am	Unemployment rate	April			3.8%
8:30 am	Average hourly earnings	April			0.1%
8:30 am	Advance trade in goods	March			N/A
9:45 am	Markit services PMI	April			52.9
10 am	ISM nonmanufacturing index	April			56.1%

MARKET TRACTION

Below the Radar

Our final **BTR** will again this week be mostly a visual experience. Let's see where we are…

Seven Fear & Greed Indicators

How we calculate the index More »

Put and Call Options

Extreme Greed

During the last five trading days, volume in put options has lagged volume in call options by 42.59% as investors make bullish bets in their portfolios. This is among the lowest levels of put buying seen during the last two years, indicating extreme greed on the part of investors.

Last changed Apr 16 from a Greed rating

Updated Apr 23 at 4:00pm

CBOE 5-Day Average Put/Call Ratio

Safe Haven Demand

Extreme Greed

Stocks have outperformed bonds by 6.11 percentage points during the last 20 trading days. This is close to the strongest performance for stocks relative to bonds in the past two years and indicates investors are rotating into stocks from the relative safety of bonds.

Last changed Apr 18 from a Greed rating

Updated Apr 23 at 4:10pm

Difference in 20-day stock and bond returns

Stock Price Strength

Extreme Greed

The number of stocks hitting 52-week highs exceeds the number hitting lows and is at the upper end of its range, indicating extreme greed.

Last changed Jan 24 from a Greed rating

Updated Apr 23 at 4:05pm

Net new 52-week highs and lows on the NYSE

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Market Momentum

Extreme Greed

The S&P 500 is 7.92% above its 125-day average. This is further above the average than has been typical during the last two years and rapid increases like this often indicate extreme greed.

Last changed Apr 22 from a Greed rating

Updated Apr 23 at 4:20pm

Stock Price Breadth

Greed

The McClellan Volume Summation Index measures advancing and declining volume on the NYSE. During the last month, approximately 7.94% more of each day's volume has traded in advancing issues than in declining issues, pushing this indicator towards the upper end of its range for the last two years.

Last changed Apr 18 from an Extreme Greed rating

Updated Apr 23 at 4:05pm

Market Volatility

Neutral

The CBOE Volatility Index (VIX) is at 12.28. This is a neutral reading and indicates that market risks appear low.

Last changed Dec 27 from a Fear rating

Updated Apr 23 at 4:14pm

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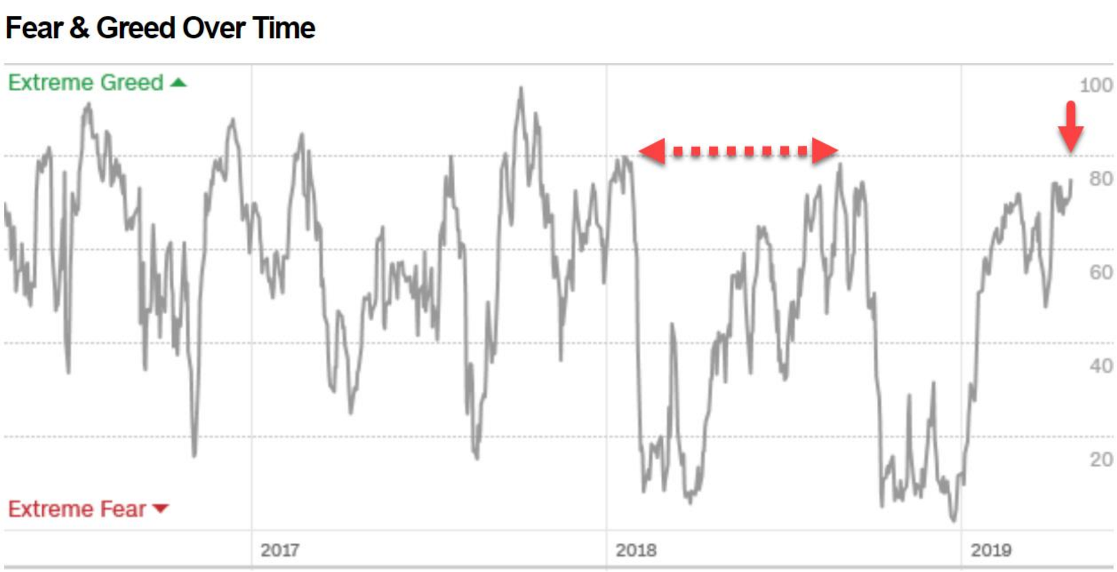
We’re nearing the level that preceded both of 2018’s *smashings* that we were fortunate to sidestep:



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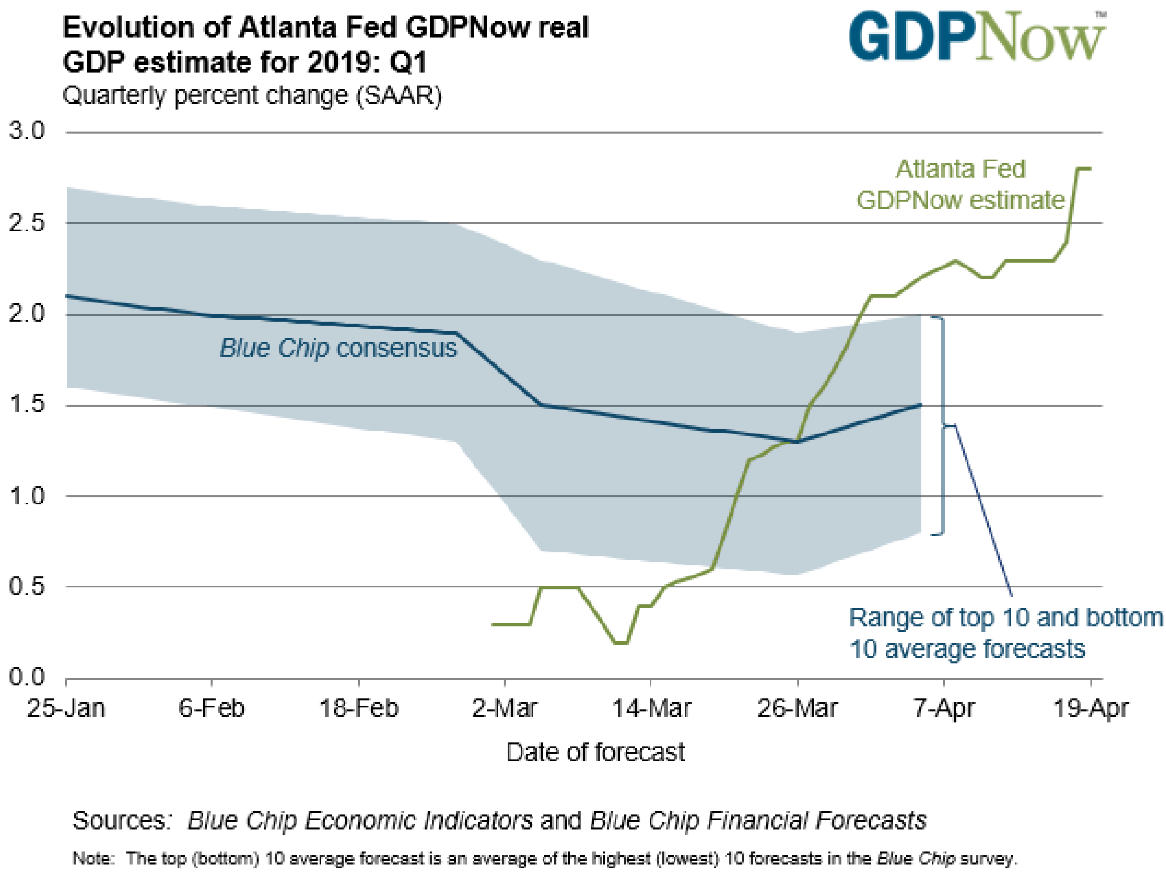
Some things that are very odd have been unfolding:



Notice that with 2 weeks left in Q1, the GDP estimate was barely above ZERO. Suddenly, it jumped to over 2.0% growth in that little bit of time!!! We've read a few pieces that claim that EPIC "channel stuffing" unfolded which allowed our favorite CFOs to "book" a ton more business than would have otherwise been transacted. Hmmm, the world may never know but it sure looks sketchy. That's quite a 10-business day surge!

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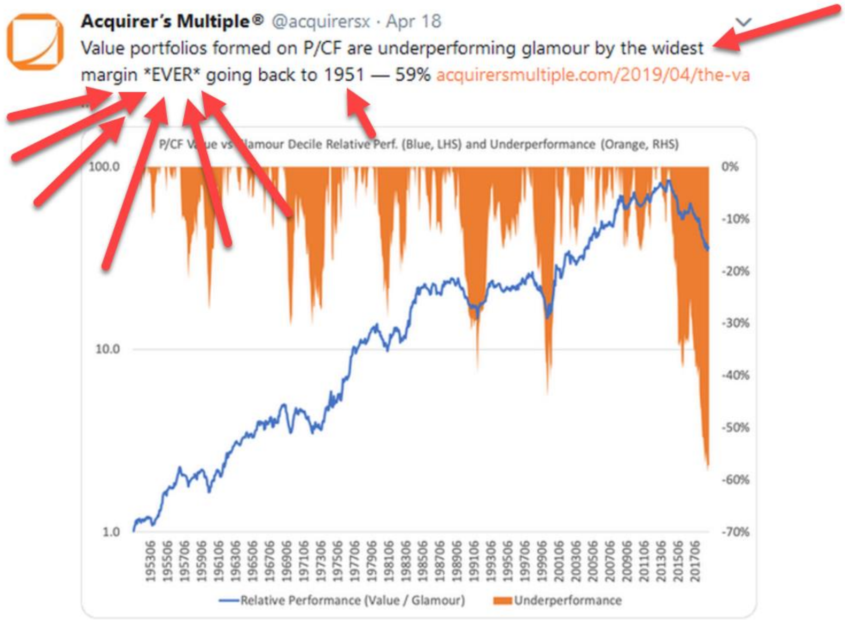
As noted by the Wall Street Journal on Monday:

> *"Sentiment is incredibly bullish. So many people are chasing performance now." – Nancy Davis, CIO at Quadratic Capital Management.*

She is right.

Currently, momentum and growth stocks are substantially outperforming value oriented stocks.



Which is worse than where it was when it was awful:

https://www.newsmax.com/finance/oliviergarret/buy-growth-stock-seen-this/2018/02/07/id/842052/

woodfordfunds.com

> ***"From time to time, markets become detached from valuation reality and while they are, fund managers like me appear to be incapable of delivering good outcomes. I appreciate that this can be an uncomfortable journey for investors, but valuation is the only reliable predictor of long-term investment returns. I remain focused on capturing the opportunity that exists in parts of the market that have been left behind since we voted to leave the EU two and half years ago. The portfolios are populated with profoundly undervalued companies, many that are exposed to the UK economy. Crucially, the portfolios are positioned how I want them to be and are completely focused on a valuation opportunity, the likes of which I haven't seen for more than 30 years."***
>
> — Neil Woodford

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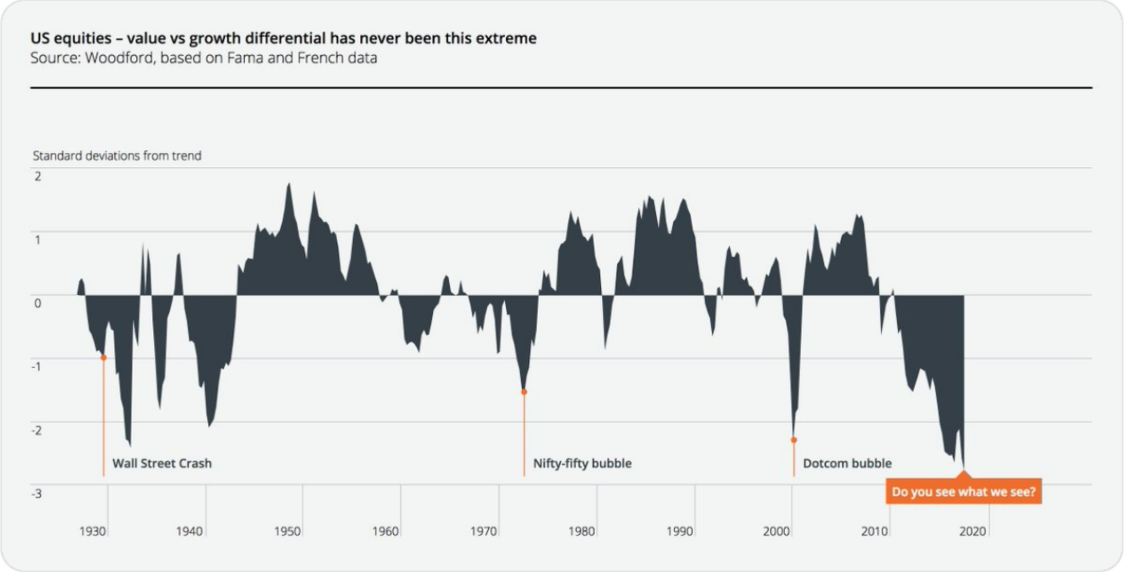
Woodford
@woodfordfunds

Follow

"The difference between the performance of value stocks and growth stocks today, is greater than at any stage in stock market history. Let that sink in..."

Read Neil's thoughts on the bubble here: woodfordfunds.com/words/blog/we- ...



The result is that growth stocks now look *massively overvalued* relative to value stocks. Look at the chart below. The last time growth outperformed value like this was the dot-com boom. And we all know how that ended.

Source: tradingview.com

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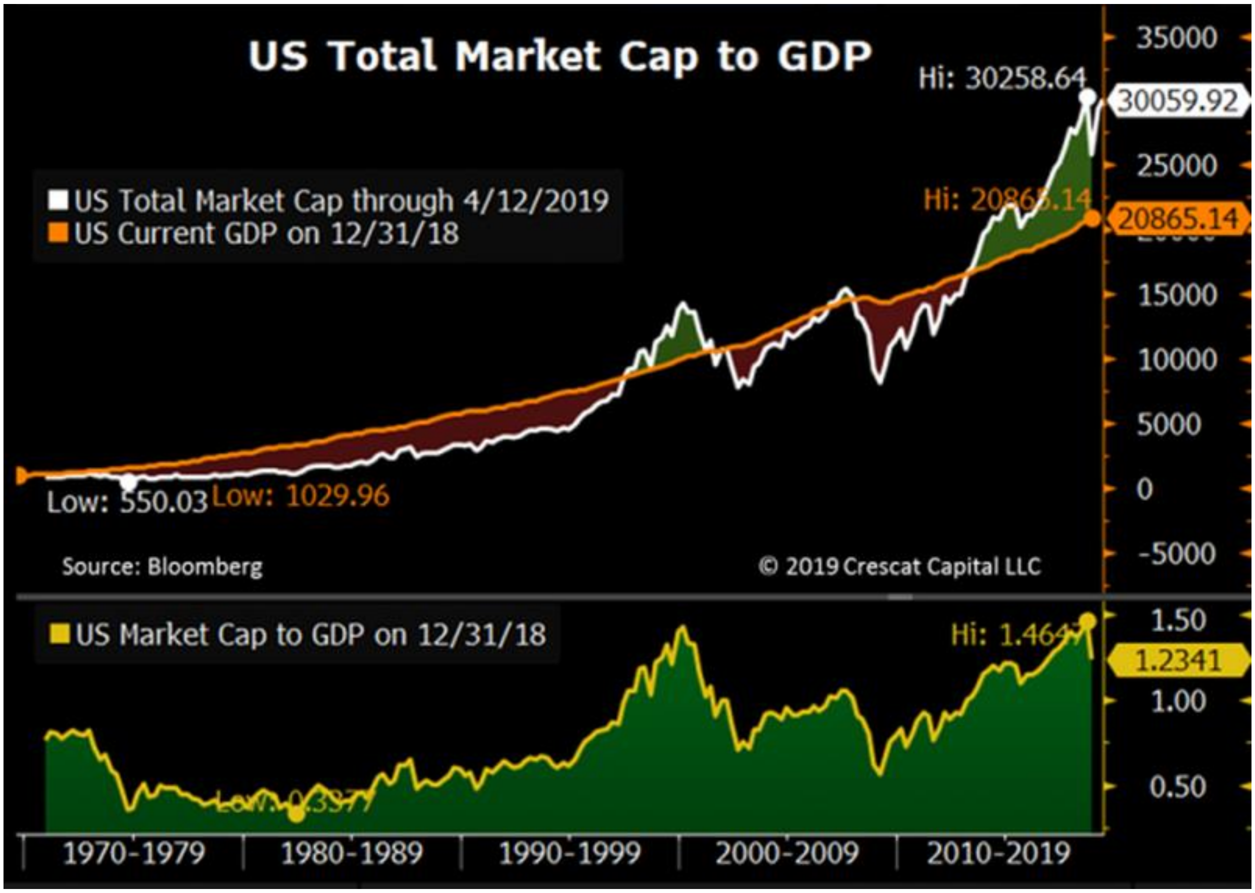
And the hits just keep coming as we found a Lance Roberts piece that was a treasure trove of Rolling Encouragement!



S&P 500 Valuations

Factors	Most Recent Value	Historical Percentile
Median Price to Book	3.6	99%
Median EV To Sales (Ex-Financials)	3.1	99%
Margin-Adjusted CAPE	44	99%
US Total Market Cap to GDP	140%	98%
Cyclically-Adjusted P/E (CAPE)	33.2	98%
Median EV to EBITDA (Ex-Financials)	12.7	96%
EV to Free Cash Flow Margin-Adjusted (Ex-Financials)	40.6	95%
Median Price to Sales	2.53	94%

Source: Bloomberg; Yale/Robert Shiller; John Hussman *Numbers as of March of 2019 ©2019 Crescat Capital LLC

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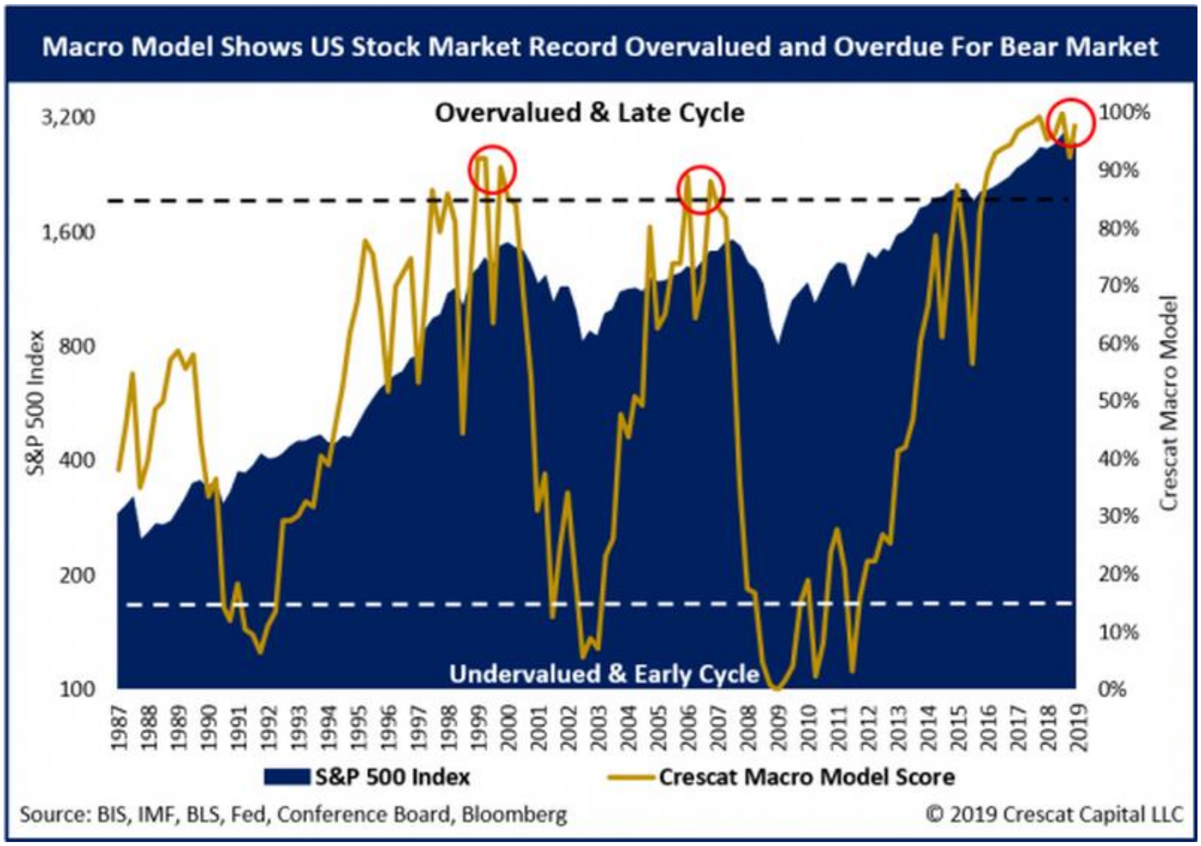

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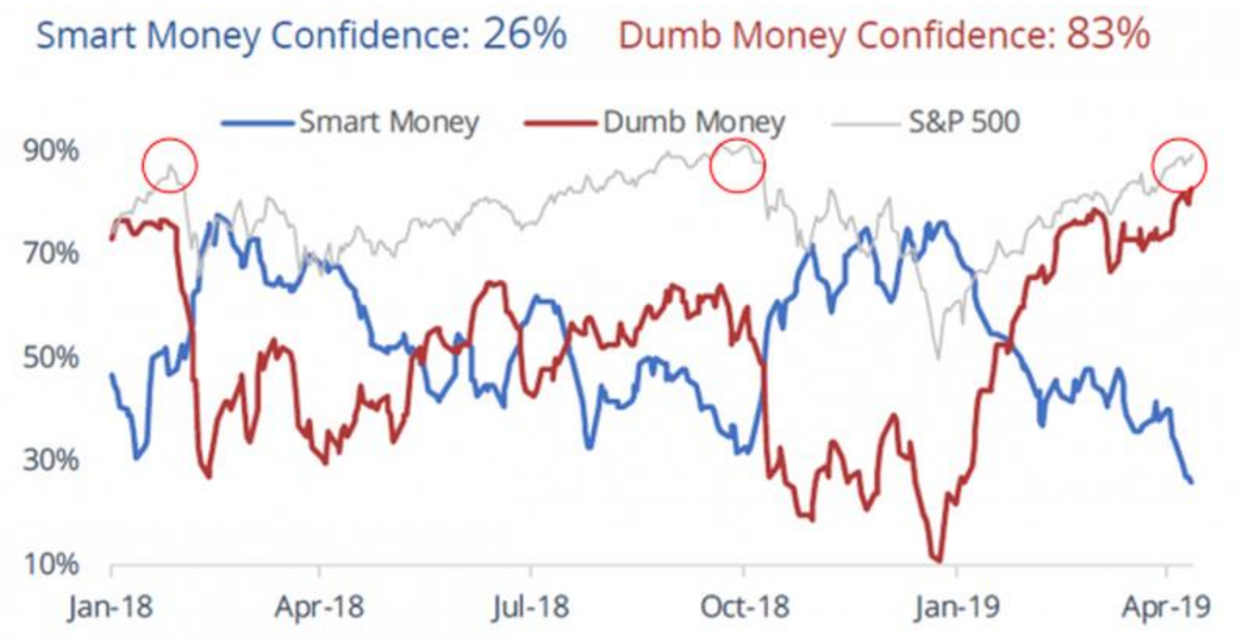
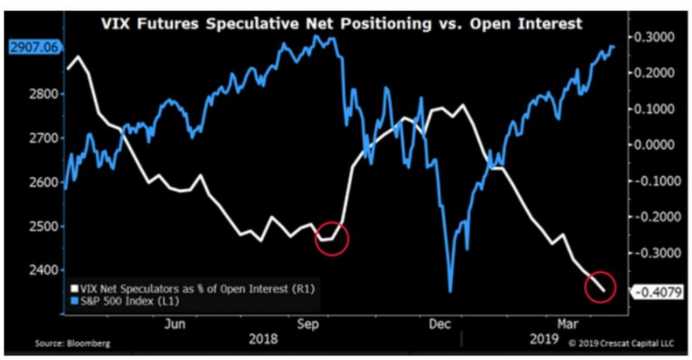
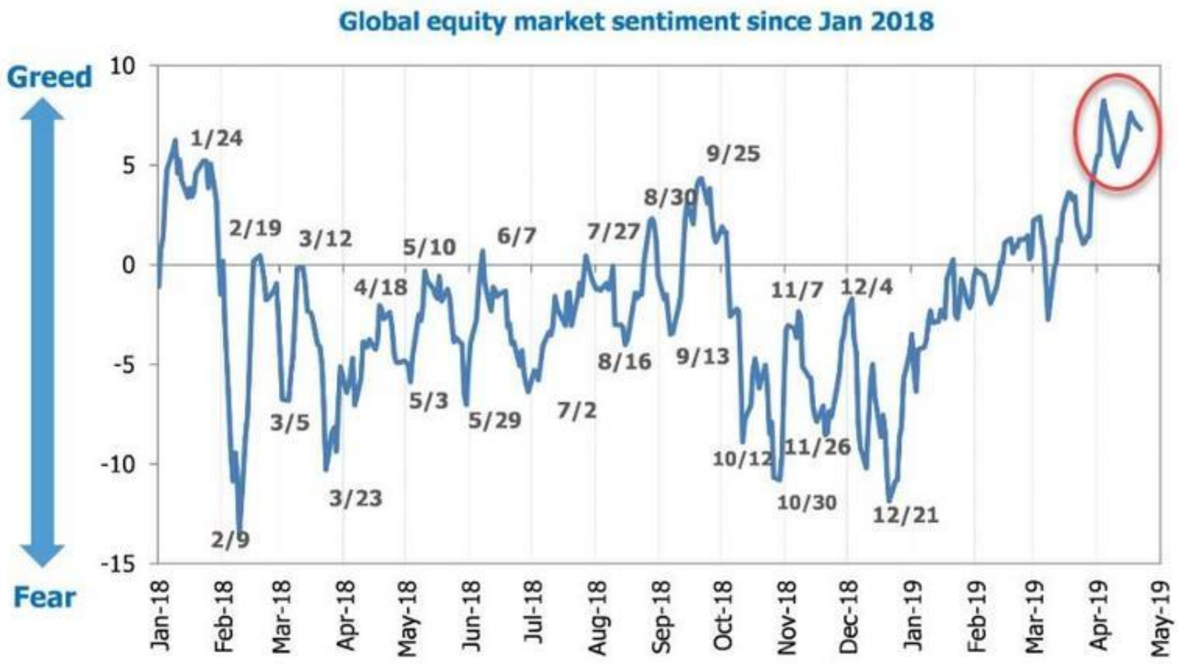


The chart below shows a third sentiment indicator we found that looks incredibly frothy today, VIX speculation at an extreme. Speculative futures traders are more net short stock market volatility than they were at the September market peak.



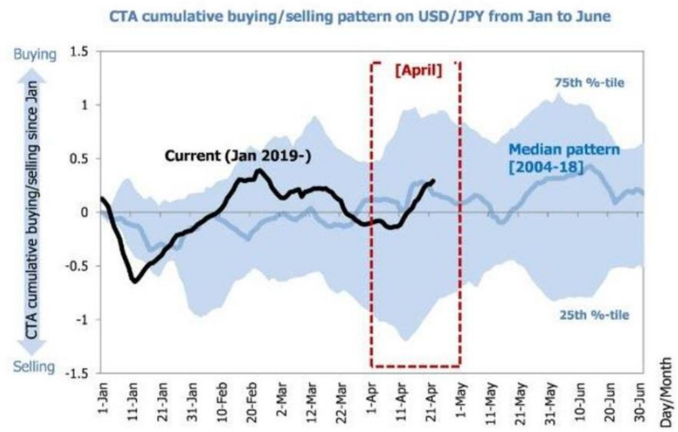
Summing that up, nearly everyone is short volatility as conditions become more and more extreme! Let's not forget what a self-reinforcing cycle higher stock prices create! Everyone's in love and the main reasons are "optimism" and stocks are heading higher!

MARKET TRACTION



So, what happens next, literally?

Precedent says that when CTAs expand their net long position USD/JPY in early April through mid-month, they tend to then sell to lock-in profits on those positions in late April and into the first half of May.



Always remain nimble my friends!

Always Bank and Roll!

Options Academy

One major gripe we have with vertical spreads, beyond the limiting of profit potential, is that they often require the trader to wait until very close to expiration to "max out" on the profit potential they do offer. That can get tricky…

Consider a one month out expiration for a hypothetical vertical spread. If a stock quickly moves to the short strike in a vertical debit spread for example, we can be placed in a rather unnatural position of cheering for the stock to then "stay still" or not retrace for say 2 or 3 more weeks to realize most of our profit potential. Not very appealing…

It's for that and other reasons that we prefer to operate with only a long call or long put position most often. If we've bought the proper call or put and the stock delivers the expected movement we've forecasted, then we have a direct path to the profits we sought without having to wait for them. The *Greeks* will deliver those for us in theory. In reality, the markets will do so underpinned by supply and demand paying respect to theoretical options pricing and the Greeks by extension.

However, despite our preferences, vertical spreads can have their time and place for those that insist on earnings action…

Earnings began to flow in earnest last week and they are ramping up even more so this week. Many may recall that vertical spreads can be well-suited to high implied volatility environments such as earnings. Why? Because with a properly structured vertical spread, we're buying one contract and selling another against it. We're buying some level of implied volatility (IV) and likely selling a similar level of implied volatility against it since we're operating within the same expiration when we initiate and vertical spread. The vertical spread goes a long way in mitigating the volatility risk (VEGA) that's inherent in trading in pre-earnings release environments.

The vertical spread can also help us to become involved in "high dollar" stocks that have high dollar options. Some stocks, AMZN for example, are so pricey on a per-share basis that naturally the options become very pricey as well. That's only exacerbated, of course, when earnings are bearing down on us as most of us know that options prices tend to spike in front of earnings releases. Think about it…

All the Johnny Comelately action-seekers tend to want to jump in to the fray to have some kind of action. Some are bulls and expect *earning beats*, so they buy calls. Others are bears and they expect *earnings misses*, so they buy puts. With nothing but buyers showing up, foaming at the mouth to boot, seeking options, the market-makers raise prices to avoid being *steamrolled* and of course to try to find an equilibrium level to balance buyers and sellers.

Stepping in and buying one long call or put or going long a straddle or strangle can be quite daring and exceedingly risky at such a time. We already know that we can largely offset implied volatility risk by opting for a vertical spread, but we can also dramatically lower the cost to participate as well. The credit we receive for selling one contract will help to offset the contract we purchase and thus reduce the overall cost and, in many cases, dramatically. In the process of accomplishing those two things, we can also greatly reduce or even eliminate Theta depending upon how we structure a vertical spread. That's impossible to do with a long call or put only. And VERY impossible to do with a long straddle or strangle!
😉

Granted, straddles and strangles and long calls or puts do offer nearly unlimited profit potential but what's likely to happen if the earnings release is a "dud"? Remember, we're talking about an unusually high implied volatility environment! It's very likely that it won't be pretty if the earnings release doesn't generate big movement!

Finally, here's one more thing to consider if you're willing to consider a vertical spread as an earnings-play vehicle. If we focus on the near-term expirations, will either have little time left or will have experienced a big move after the release, or both. That's important because under those conditions, the vertical will deliver the big profit potential much more quickly than it does under normal conditions. Stocks either make big moves or time runs out quickly, or both. Verticals reach their full value in rapid order if big moves are made or if little time is left. And don't forget, this happens, assuming you've used a vertical for earnings, while you've addressed Vega and Theta risk along with the prohibitively high cost of options in high dollar stocks. Not too bad! Not too bad at all for Johnny or Jenny Comelately!

If you have questions, please ask away in our next **Morning Call** webinar. 😋