MARKET TRACTION

IN THIS ISSUE:

Of Yields, Earnings and Other Problematic Developments

<u>This Week's Trade Ideas:</u>

The deluge of earnings reports combined with the extreme movement in the markets today has made the search for low risk/respectable reward ideas very challenging! (See **DTE** and **ETR**'s charts as ones we passed on due to earnings and the market environment.)

Bullish Ideas:

(View Webinar) Edison International. > EIX > $64.71 Last. Buy the May 18th 65 Calls (ATM*) for $2.00 or less with a close or anticipated close above $65.35 in an up market with expectations for continued strength in the major indices. *This is very short term as earnings are due out on May 1st.

AND/OR:

(View Webinar) PPL Corp. > PPL > $28.50 Last. Buy the May 18th 28 Calls for $1.10 or less with a close or anticipated close above $28.70 in an up market with expectations for continued strength in the major indices. *This is very short term as earnings are due out on May 3rd.

<u>Bullish Mentions</u>:

(View Webinar) None at this time.

Bearish Ideas:

(View Webinar) Progressive Corp. > PGR > $60.71 Last. Buy the May 18th 62.5 Puts for $2.80 or less with a close or anticipated close below $60.25 (AGGRESSIVE*) in a down market with expectations for continued weakness in the major indices. A break below key support at approximately $59.80 is what is likely to be required for real drop to occur so be careful if you hone in on this! This is a counter-trend idea, so it is on a tight leash!

<u>Bearish Mentions:</u>
(View Webinar) RSG. (published last week in an Update)

<u>Market Overview:</u>
Last week, a little way into Market Overview, we wrote this:

NEWS will be made if the earnings are good and the markets do not rise significantly on said news. If that's the case, batten down the hatches mates!

We're getting to that point! The big names are in the news this week and much like the rest of the market they lost their mojo in the second half of last week and have yet to find it again. This must be watched closely as momentum traders and *algos* like to key off these performers and that spills over into most of the rest of the market. As for the rest of the market:

Below the Radar:

The 10-year Treasury note is delivering a yield of 3% and the sky is falling! Normally, when something has been fretted over, in such a prominent way, for so long, the markets will have discounted the actual event itself. That's not the case so far with respect to bonds selling off and yields heading higher, briefly over line-in-the-sand 3%. In fact, these developments seem to be **THE** development that is trumping nearly all other market concerns, at the moment…

Options Academy:

We're going to keep this week's **OA** short and bitter! That's right…there's very few recent examples that are better with respect to our motivation for typically sidestepping earnings. Please notice the garish graphic above with respect to GOOGL and the fallout from their earnings that were reported yesterday after the close of trading. The stock price fell by over 5% at one point during today's trade so let's look at things a little more closely…

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We're noting this AGAIN!

… if you decide to become or remain involved, you must remain nimble!!!

Volatility remains elevated! A great deal of movement continues to be compressed into very short time periods when viewed relatively. Adjustments and rolls need to be completed much more frequently than during normal phases of market price action.

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.

Week 12 of our Special Note:

Things may yet sort out for the Markets and we'll be back to All-Time Highs across the board an on our way to even more ATHs, but significant technical work remains to be done before we can issue the "All Clear". – We're not ruling it out we're simply acknowledging that we're not quite there yet.

Realize that you may be operating in a fast-moving environment should you decide that to enter the markets*.*

We'll continue to reprint this note as long as the markets remain this volatile!

Swing trading in an environment like this one can be very challenging. We've tried to make that very clear here in the newsletter and in our **Morning Call** webinar. The markets have become increasingly driven by news and tweets that we can't know of in advance. Not losing a great deal of money is a very important part of the process of making money over time in the markets!

Outlook:

Here's a full reprint of last week's Outlook:

Our "gut" is back again this week and it believes that the Street is that much closer to weathering the volatility storm that was unleashed 2 ½ months ago. The news cycle is set up to be favorable and the bounce off the 200 SMA is only accelerating. It would take news out of the blue or something very different than we've seen over the course of this bull market for the indices to be stopped in their tracks and reverse Southward. ***Naturally, that could happen, but we believe it will take a new driver to emerge to justify that type of action.***

We continue to strongly suggest that those that venture into these markets have the time and availability necessary to keep an eagle eye on them. There's simply too much movement happening too quickly to treat these times as normal for the purposes of swing trading.

VERY interestingly, that's exactly what happened. Last week the SPYs et al. were breaking above their 100 SMAs and acting well as we wrapped up the newsletter but after a good start on Wednesday morning, indices and stocks were unable to let the good times roll. Many different news items emerged and we published several updates to go along with them and the negative market action they seemed to bring about. The malaise they whipped up remains over this market. So, the **"new driver"** line we highlighted above did in fact emerge and derailed what started out positively.

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And that's exactly what happened. We have to sit up and take notice of the fact, that at least for the moment, things are not acting well and the patterns that worked extremely well for about 9 years are not working as they once had. Is a new paradigm emerging? It may be too early to say but we can say that complacency has no place in this current market environment.

Technicals:

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

Fundamentals:

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

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

Recap of Last Week (written prior to mass selloff!):

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See **Outlook** for more on the graphic above but the quick take away here is that:

1. We went NOWHERE
2. A marked change in market behavior has been seen
3. The markets are treating things differently and bond prices/yields/interest rates are spooking the markets
4. As are other various news items: tariffs, politics, wars, energy etc.

We were leaning very bullish with names last week with only 3 bearish mentions and no bearish ideas officially. We had DHI and LEN as bullish ideas and many other names as bullish mentions. Despite that, we sensed we were due for a *curveball* from the markets and we got one. Actually, we feel pretty fortunate to have dodged a bullet. DHI and LEN started off well but luckily were not able to close above their trigger levels on Wednesday as they along with the markets became very heavy by the end of the day. That weakness continued over into Thursday and intensified. The key elements weren't in place for us to become involved in those official bullish ideas or mentions because triggering never took place and the winds shifted southward against bullishness. We were frustrated but we know that can happen from time to time. We began searching for safer bearish names but very few were to be had. We published a few names late in the week that were fresh.

This type of write-up accompanies our ideas each and every week:

Lennar Corp. > LEN > $57.52 Last. Buy the May 18th 57.5 Calls for $2.35 or less ***with a close or anticipated close above $58.05 in an up market with expectations for continued strength in the major indices*** *and XHB. This week's series of FED speakers could produce volatility especially for sectors with greater interest rate sensitivity (e.g.>>>home builders!)*

We added the bold to highlight the fact that we don't write that out of habit! Closing strongly in the direction of the trade idea/mention is a critical component in swing trading. If things aren't acting well, we've found it better to wait to enter until they do rather than forcing on a trade.

The most frustrating part of last week was the lack of fall from all 3 of our bearish mentions. OZRK, XLF, and KBE either didn't fall at all or actually moved up a little bit. We haven't had counter-movement very much, if at all for quite a long time. To have it occur when the markets changed things up on us as they did was frustrating. This, to us, exemplifies just how strange of a dud week last week truly was in the end. The indices went nowhere and yet our bullish stuff didn't act well nor did our bearish stuff. This outcome tells us that the markets may be fundamentally changing back to ways we haven't seen in several years. At times like this we should never take our eye off the ball.

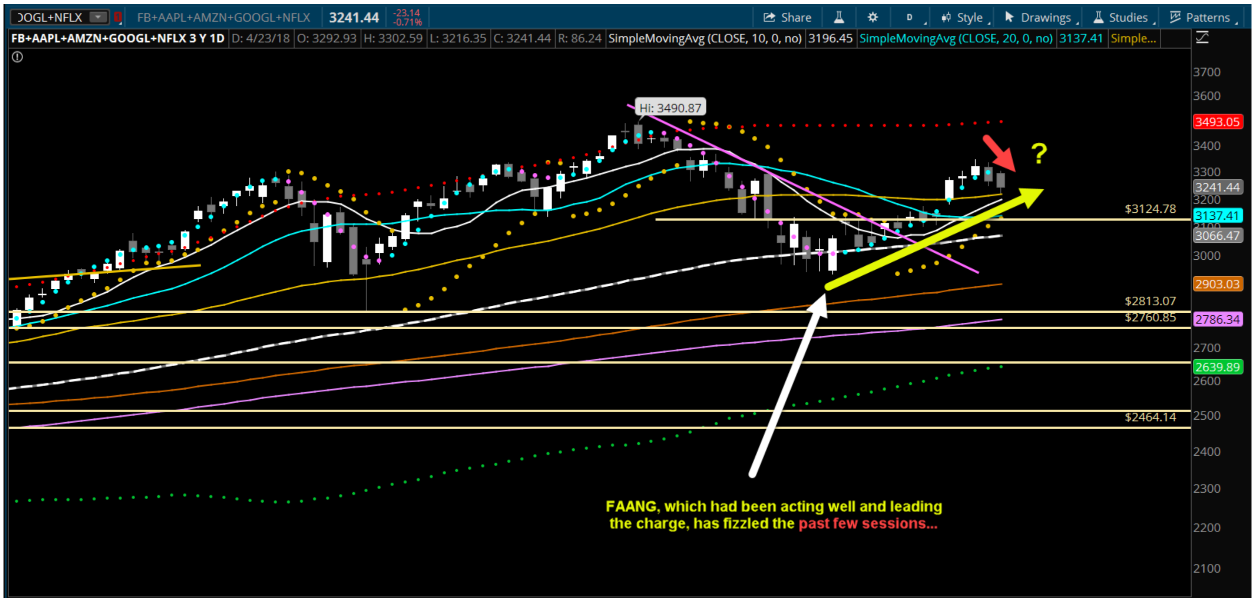
All in all, we can't complain too much about last week because we dodged a bullet thanks to the market moving news hitting the tape on Wednesday and preventing us from getting into our bullish ideas and feeling even more emboldened to get into other bullish mentions. A weak close never leaves a good feeling for bulls and we're fortunate that the ugliness didn't begin early on Thursday instead of midday on Wednesday.

Market Overview

Last week, a little way into Market Overview, we wrote this:

NEWS will be made if the earnings are good and the markets do not rise significantly on said news. If that's the case, batten down the hatches mates!

Let's have a look at FAANG first:



We're getting to that point! The big names are in the news this week and much like the rest of the market they lost their mojo in the second half of last week and have yet to find it again. This must be watched closely as momentum traders and *algos* like to key off these performers and that spills over into most of the rest of the market. As for the rest of the market:

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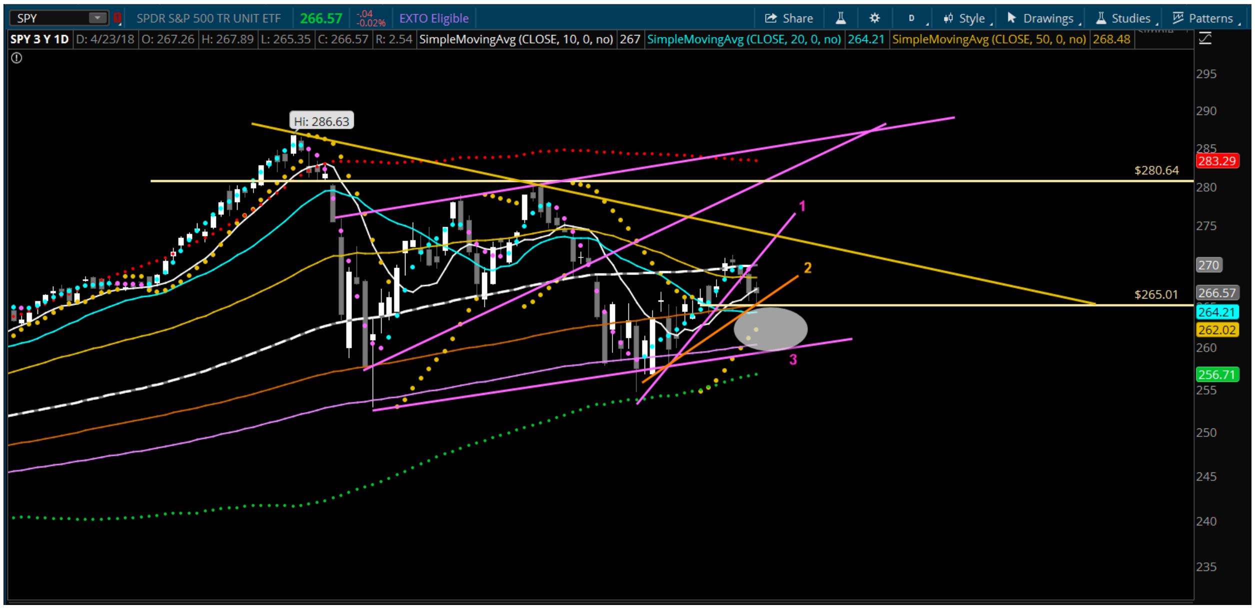

The SPYs fellow below support level 1 that we were monitoring. As we write, they've found temporary support on the orange line and the manila line at 2.

We've placed a white oval just below support line 2 to denote the air pocket that seems to be between the lows and yet another test of the 200 SMA and support at 3. That's not a comforting prospect to bulls but we must acknowledge that it has become a much more likely possibility given the damage that's occurred. A definitive break of the 200 SMA might induce panic selling that would potentially force a test of an even lower low area near the February Panic low.

The economic calendar brings a fair number of important reports this week and when combined with the number of earnings reports that include many high-profile companies, there should be more than enough material to move markets. Whether any of it matters, given the long shadow that bonds/interest rates are casting over the market, remains to be seen. The markets seem to be hypnotized by bonds/rates at the moment, so little of the data due out may move equities markets directly. It may require the data being filtered through the bond markets to gauge any impact at all. We'll see…

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This Week's Economic Calendar

TIME (ET)	REPORT	PERIOD	ACTUAL	MEDIAN FORECAST	PREVIOUS
MONDAY, APRIL 23					
8:30 am	Chicago Fed national activity index	March	0.10	--	0.98
9:45 am	Markit manufacturing PMI (flash)	April	56.5	--	55.6
9:45 am	Markit services PMI (flash)	April	54.4	--	54.0
10 am	Existing home sales	March	5.60 mln	5.52 mln	5.54mln
TUESDAY, APRIL 24					
9 am	Case-Shiller home prices	Feb.		--	6.2%
10 am	Consumer confidence index	April		125.9	127.7
10 am	New home sales	March		630,000	618,000
WEDNESDAY, APRIL 25					
	None scheduled				
THURSDAY, APRIL 26					
8.30 am	Weekly jobless claims	4/21		230,000	232,000
8:30 am	Durable goods orders	March		2.5%	3.0%
8:30 am	Core capital equipment orders	March		--	1.4%
8:30 am	Advance trade in goods	March		-$73.4 bln	-$75.4bln
10 am	Housing vacancies	Q1			
FRIDAY, APRIL 27					
8:30 am	Gross domestic product	Q1		2.0%	2.9% (Q4)
8:30 am	Employment cost index	Q1		0.7%	0.6%
10 am	Consumer sentiment index	April		98.0	97.8

Below the Radar

The 10-year Treasury note is delivering a yield of 3% and the sky is falling! Normally, when something has been fretted over, in such a prominent way, for so long, the markets will have discounted the actual event itself. That's not the case so far with respect to bonds selling off and yields heading higher, briefly over line-in-the-sand 3%. In fact, these developments seem to be **THE** development that is trumping nearly all other market concerns, at the moment. Does it have staying power? Historically speaking, YES. However, there's normally a *"try to ignore it"* phase that transpires before the equity market admits that higher yields are problematic for stock prices. Yet, as we all know, that script doesn't have to play out to perfection and exceptions can emerge for every rule given enough trials. Yields climbing simply can't be underestimated in terms of impact. The mood on the Street has shifted and it seems as if players are selling first and asking questions later. THAT is a **big change** and one we **must** appreciate.

We'll start by noting the transition back into Greed from Fear, has been halted:

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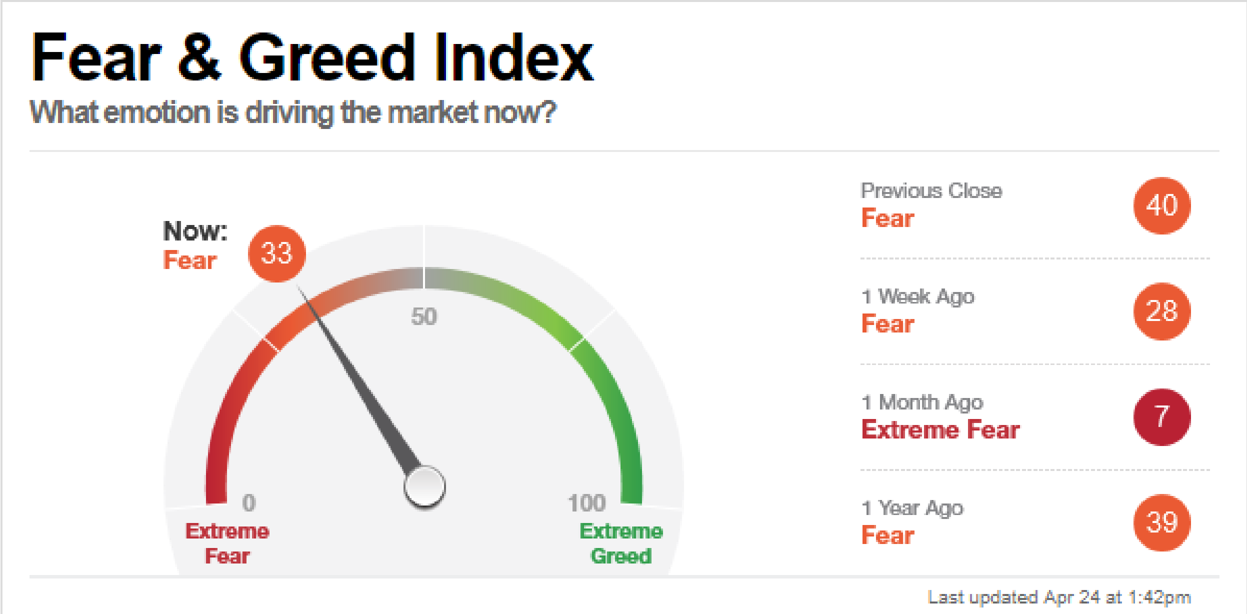


Last week we registered a 29 reading, so we're not much different now despite the rally that fizzled out and today's heavy selling. The VIX however, after nearly returning to normalcy, is spiking:

Other interesting and not very good signs are bubbling up as well:

Dow threatens longest losing streak in a year as 10-year Treasury yield cracks 3%

Published: Apr 24, 2018 12:10 p.m. ET

155 Aa

Investors keep eye on bond yields; Alphabet sinks after results

The markets are acting poorly. April had started out well but nearly all the month's gains have been erased in just a few days despite this:

Earnings were also a major focus, with a deluge of high profile companies reporting results before the open. ***The season has so far been strong, and more than 80% of the S&P 500 companies reporting so far have beaten profit forecasts.*** *While that's above the 73% that beat in the fourth quarter of 2017, better-than-expected results often haven't been enough to lift shares thus far this season.*

In a nutshell, these snippets we found at MarketWatch encapsulates some our thoughts fairly-well:

"Crossing 3% on the 10-year is something that will certainly raise concerns, but at this stage of the cycle, higher yields aren't antithetical to rising stock prices. For the time being I think we're fine, but we're certainly keeping an eye on the yield curve, especially if the Fed becomes more aggressive," said Bruce McCain, chief investment strategist at Key Private Bank. "Ultimately earnings remain the primary driver, along with the fact that the economy is still in pretty good shape.

Hussein Sayed, chief market strategist at FXTM, said that "the 3% by itself is just a psychological level and not a significant threat, ***but if a break above leads to further selling in Treasury bonds, that's going to be a serious warning signal for equity bulls. With a current world running on A.I and algorithms, a selloff may look ugly."***

To us, that's the real risk. BOTS keying off bond yields and selling the living daylights out of equities as a result is something that's been speculated about for a while but not witnessed many times. Could the BOTS accelerate the sell-off as many believe they did in early February? It can't be ruled out. So, in a way, we may be on the frontier of new territory. In times past, the markets shrugged off rising yields for a spell before ultimately reacting to them and the effect they have on economic activity and ultimately profits and equity prices. Will that reaction be condensed into a very short time window vs. those of historical standards? It certainly seems possible given February's WHOOSH lower.

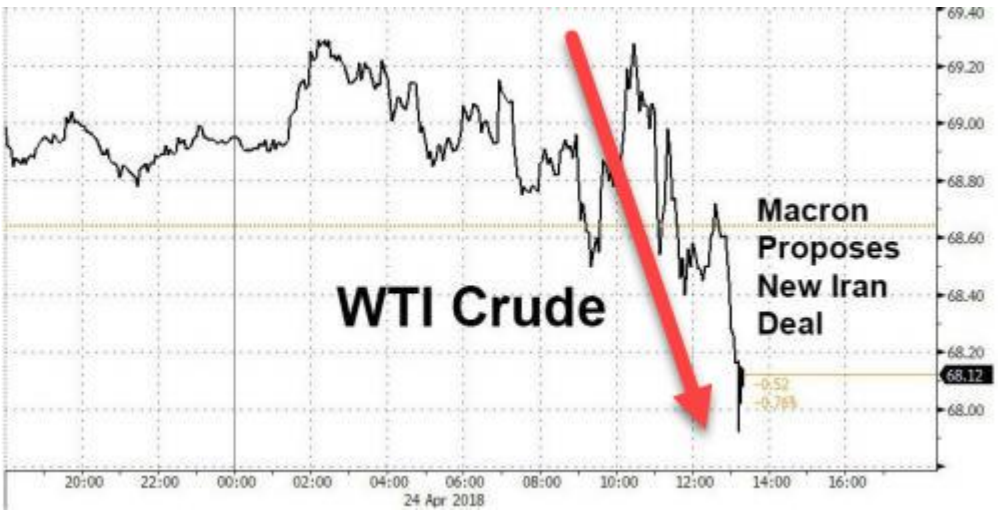
The selling is becoming more indiscriminate as well, which is not normally a good sign, at least at first:

Caterpillar Inc. *CAT, -6.39% surged 3% after the maker of construction and mining equipment reported first-quarter profit and sales that were well above expectations.*

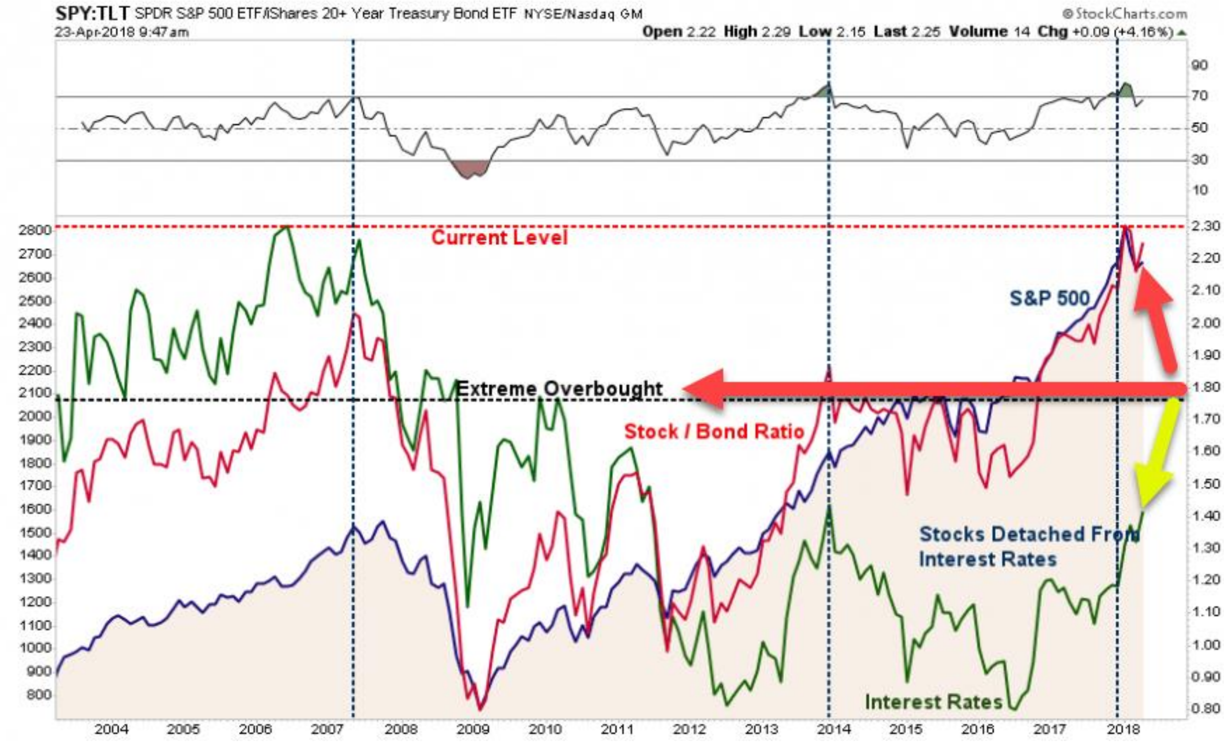
*On the downside, **3M Co.** MMM, -8.11% fell 7% as the company said its full-year earnings would be lower than previously expected.*

Notice that both big name industrials are down big but one after having surged higher initially on huge "beats"! So, to get very technical, they're trashing nearly everything! And there's even more…

Even Energy, which had been performing quite well of late, is under serious pressure too:



Other technical developments are coming to light and they're rather ominous. These are courtesy of Lance Roberts with us adding a graphical assist:



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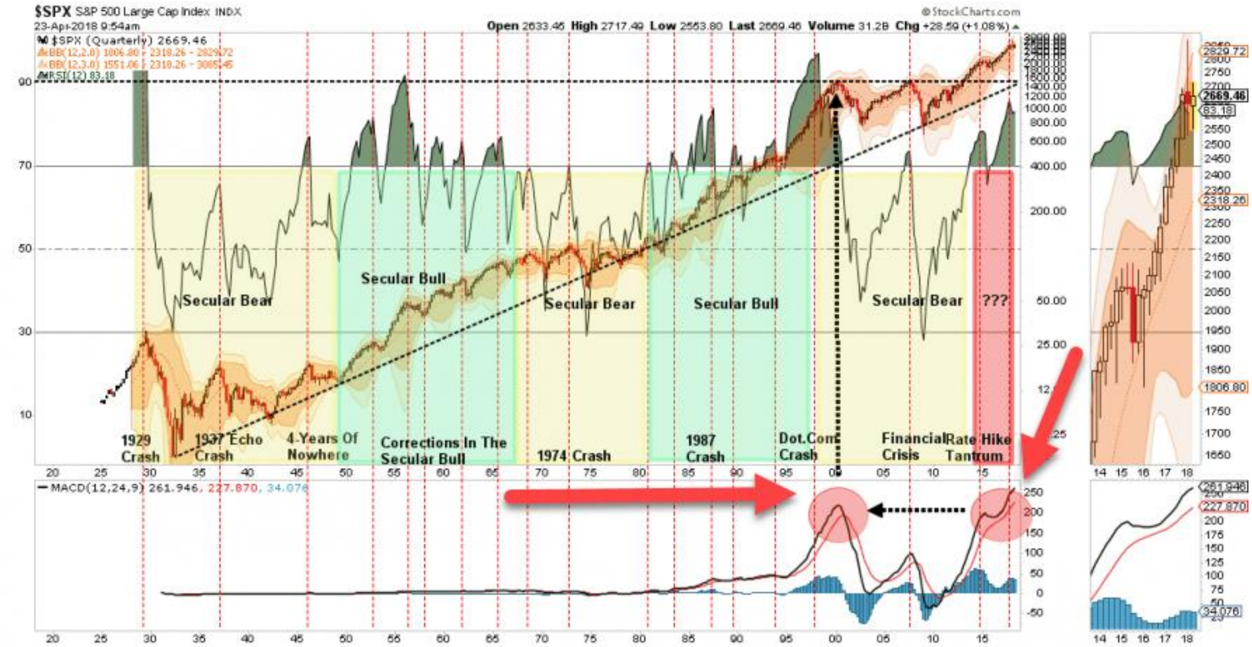
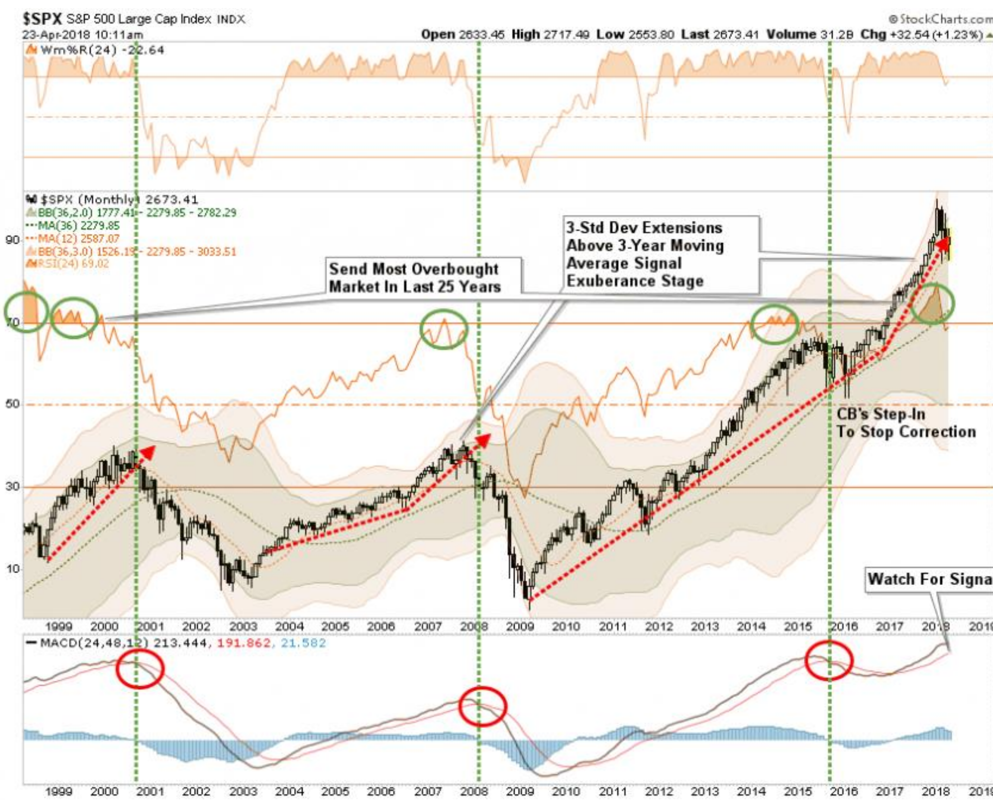
Stocks have been and remain in overbought territory historically and they're very detached from interest rates. Robert's MACD on the extremely long-term charts suggest that things are historically overbought and appear to be losing momentum. This is Y2K or worse:



On this final one, we won't bother to augment it with arrows etc. as it says it all:



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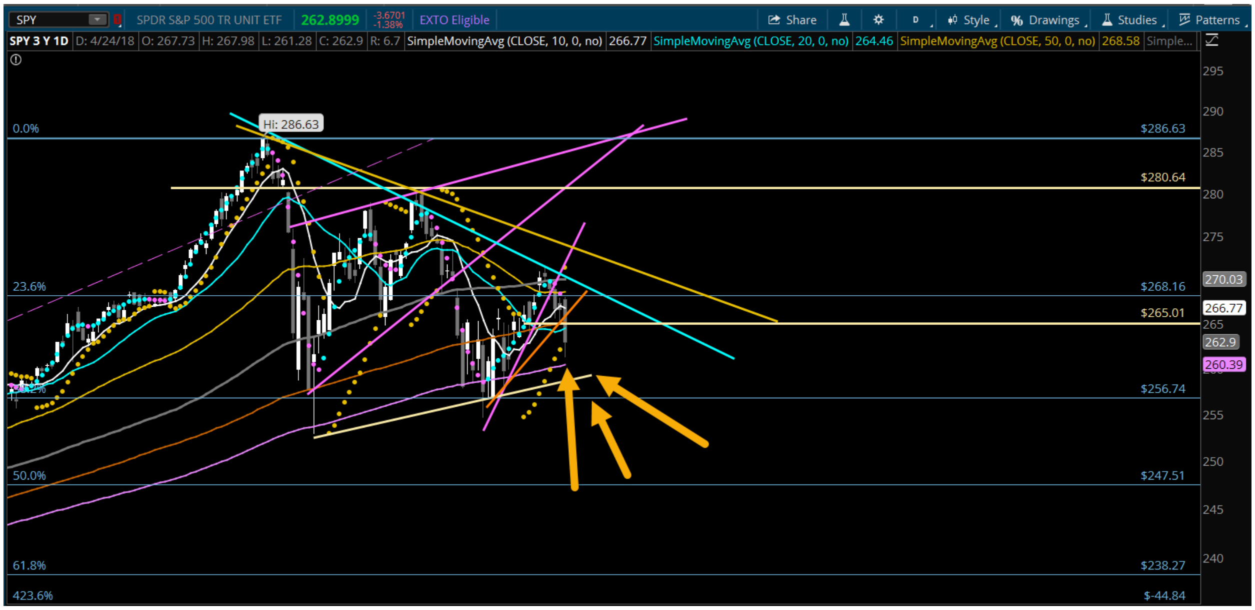
A full-on retest of the 200 SMA (which we discussed last week) and the support line just below it in the SPYs looks more and more likely with each passing day:



There are various forms of support all within the same neighborhood but should the lowest of them fail, we believe the S&P would likely lose another 5% in rapid order.

To close, in short, many of the concerns we've chronicled from many months seem to have left their **Below the Radar** status and are now mushrooming into worrisome headlines. We're not happy about that but it is for this reason that this section is a part of our newsletter. In other words, we're not happy that stock prices are rapidly declining but it's no surprise to us! In fact, it's no surprise at all from a big picture perspective.

Tread Lightly! & Bank and Roll!

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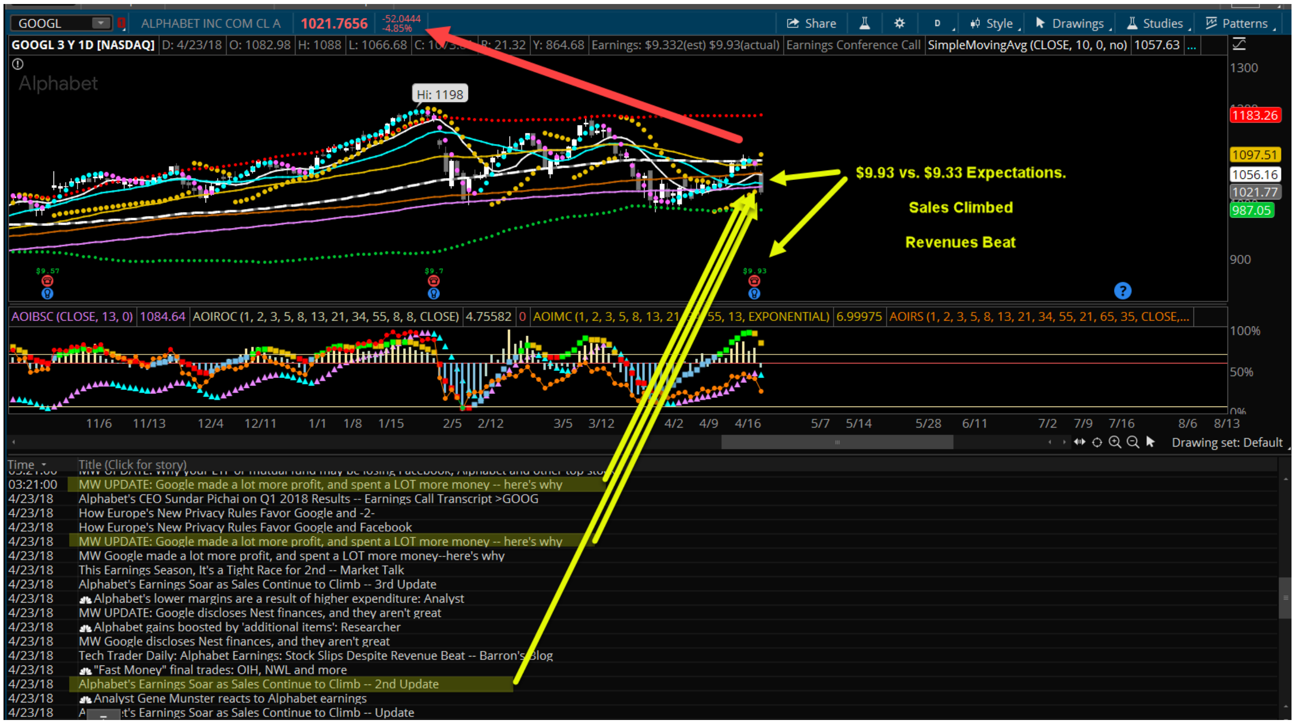
Options Academy



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First off, GOOGL rose big in after hours trading immediately following the earnings release. The spike higher was short-lived but it happened!:

It was even showing up 1% in pre-market briefly. So, using that after hours high as a reference along with today's low, we can state that GOOGL has dropped by over $100.00 per share in just a few hours of trading. The question is: "Why?"

EPS came in at $9.93 vs. $9.33 expectations. Nothing really wrong there as that's normally considered "blowout" performance.

Sales grew.

Revenues grew.

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The initial reaction was strongly positive on seemingly positive news.

Some firms downgraded the stock while others upgraded they're price targets. However, let's make this more tangible and put it in options terms.

Someone that bought the 85-delta earnings expiration call (April 27th) at a strike of 1010 would have paid about $69.00 for it with the stock closing near $1073.00ish yesterday. As we write, that option is worth about $18.00, thus even owning just one call contract would have resulted in a $51.00 paper loss on the call at this moment ($5100 loss in the real world). Not only was the loss due to directional movement but on top of it the options Implied Volatility level is much lower today since the "uncertainty" of the earnings release is out of the way and demand for those calls is drying up. That's really adding insult to monetary injury!

Let's think about this…a speculator that played the "earnings game" bullishly could have been right about the EPS BEAT, right about HIGHER Sales and Revenues, even received a few Wall St. upgrades and still lost a bundle??? Need we type more?

The post-earnings reactions are anyone's guess and even professional Wall St. analysts can't agree on GOOGL's prospects being better or worse as a result of this earnings report. Hmmm…

Earnings responses are often bewildering and take on the look and feel of wild speculation aka GAMBLING! It's for reasons such as these and episodes such as this one in GOOGL that we often avoid earnings risk! We'd like to have action in place to score big on earnings too, but it doesn't always make sense to do so and there are easier and less risky ways to make money actively in the markets. At least, that's how we see it!

If you have questions, ask away in this week's **Morning Call** webinar.