MARKET TRACTION

Does Lack of News Salvation Lead to a Tax-Loss Selling Tsunami?

This Week's Trade Ideas:

Bullish Ideas: (View Webinar)

DWDP > DowDupont Inc. > $52.29 Last. Buy the Jan. 11th 51.5 Calls for **$3.05** or less with a close or anticipated close above $53.35 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, NVDA, MCHP, DE.

Bearish Ideas: (View Webinar)

BK > Bank of New York Corp. > $46.73 Last. Buy the Jan. 11th 47.5 Puts for $1.90 or less with a close or anticipated close below $46.57in 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.

None at this time.

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.

MARKET TRACTION

Outlook:

Last week's Outlook yet again with highlights:

So, what's next? There's a case to be made for both sides. *Today's opening gap was sold into quite heavily yet* ***the SPYs remain above the critical $260.00 level on a closing basis. Be prepared for anything*** *as a news-driven move above $270.00 could open up more upside hijinks!*

Since, we got 2 day of rally attempts and then 2 days of failure, so the two-sided case was accurate.

And last week's headline:

"On the Edge of a Volatility Maelstrom?"

At the time of publication last week, we had many more bulls than bears and looking back on it, that was the right read at the time. Last Monday, Tuesday, and Wednesday, bulls tried to rally the market each day on the open, but the action weakened by the end of each day and we saw closes below the opening each day.

We'd seen enough after Thursday's action and sent out an update with respect to neutralizing risk. Despite arguing for prudence and caution for over 2 months and counting, we pushed out an update reiterating those sentiments late in the week (see **Recap**). Safety first!

Now? The break below the $260.00 level in the SPYs, that we've been watching out for, finally happened yesterday. We'd expect that there's more selling and even lower lows on the way before a rally of any significance can transpire. BUT, BUT, BUT we have the FED news looming, we have government shutdown stuff looming, DC and NYC political intrigued about to impact, and we have China uncertainty too. No one likes to hear it but we're preaching prudence again because we can't know the news ahead of time as we are not "Inner Circle" members….yet! 😉

Technicals:

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

Fundamentals:

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

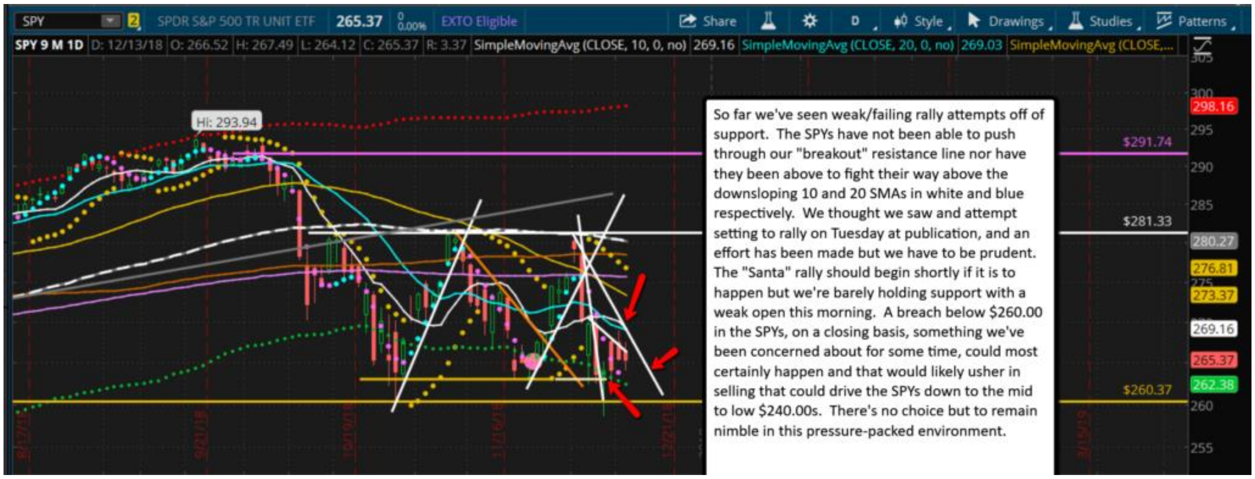
(Editor's note: These trade ideas may be updated periodically, in keeping with market conditions. It is intended solely for educational purposes.)

Recap of Last Week:

Given the nature of last week's action and our "two-sided argument" take on it, we're presenting this critical update that we sent out last Friday morning:

Newsletter Update:

The graphic pretty much says it all. ***This is a risky time and we'd expect the decision as to the next significant leg of movement in the market to be made soon. As always, when in doubt, remain prudent, hedge, roll, close etc. It's been a listless week so far with failed rallies and now there's a weak opening. More when warranted.***



If you have any issues or questions, please contact us at service@tractiontech.com

Thanks!

As for the stock-by-stock portion, let's cover our lone official bear from last week:

***CIEN > Ciena Corp. > $31.59** Last. Buy the Jan. 4th 33 Puts for $3.05 or less with a close or anticipated close below $30.65 in a down market with expectations for continued weakness in the major indices. *** Earnings due. Trade only considered post-earnings in a weak market.

We sent that out as a correction to be clear. **CIEN** jammed up post-earnings but sold off for nearly $4.00 since.

As for the bulls, **INTC** was our official idea. It tried on Wednesday and Thursday, but it came under pressure on Friday with everything else and has remained that way.

ATHM – tried to move up initially but with the market failing it failed.

***QCOM –** has tried, but it can't do it on its own. Hung in there.

CSCO – never tried so it was disappointing in that regard. Been smoked since the market rolled over.

JNJ – tried as the market tried for two days but then got annihilated with awful news that will hurt the company's reputation. This is a great example as to why 70 Delta Calls make a lot of sense and especially so in risky environments.

DOCU – a lot like QCOM, hasn't budged much to the downside.

MARKET TRACTION

MCHP – much like QCOM and DOCU.

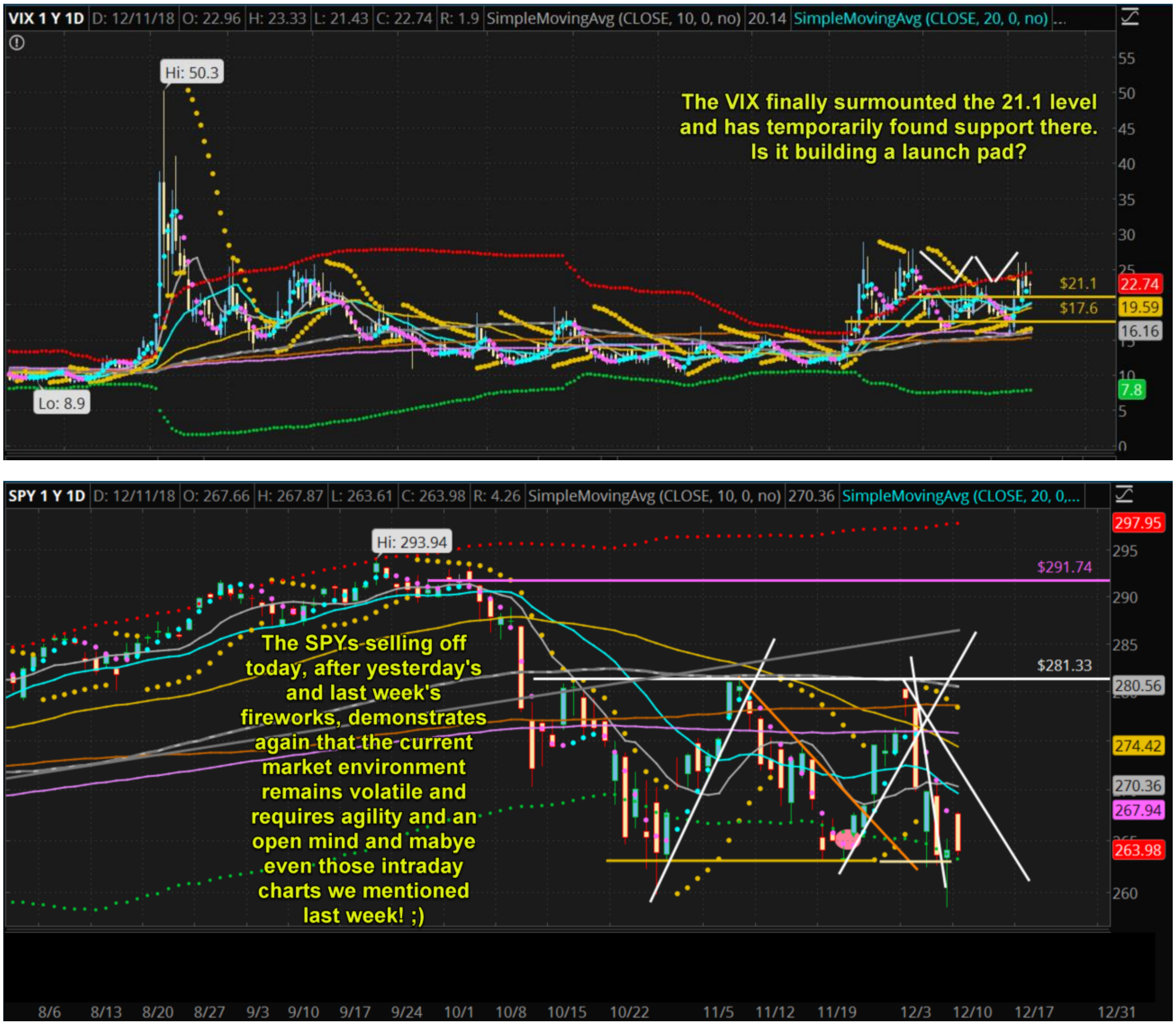
***SWKS -** much like QCOM, DOCU, MCHP!

DLTR – much like…just kidding, it too has hung in there.

We didn't use it last week, but we felt it and tried to convey it. What's that? Well, we didn't use the old "pennies in front of a steamroller" analogy because we know that we overuse it but that's the feeling we had. Both sides of what we saw last week played out. Bulls tried on Wednesday and Thursday, they failed, and bears re-emerged, and the long-discussed $260.00 level was breached. The second-best thing we did last week was to send out the Friday morning update. The best thing we did last week was to urge prudence and caution after sensing that a volatility maelstrom was brewing.

Market Overview

Again, and again, we're forced to go back to last week to begin this week's **Market Overview:**



*So, we can see that the $260.00 level may have more stout support than at first glance which also informs us to **why a break of it is likely to produce serious selling**. Moving on…*

The market remains below trend, so we must remain concerned and give bears their due. A decisive close below $260.00 in the SPYs could bring about the assault on the next level down that we've been speculating about for some time. *From $240 - $245.00ish should reveal some support if we get there.* ***The technicals continue to look bad.*** *Below trend, below the 50, 100, 150 and 200 SMAs with the 50 having crossed below the 200. We can add that most key SMAs are also negatively sloped. Still though, as we noted above, they're holding up KEY TECH and it could ignite and lift the markets.* ***In summary, it remains a prudent roller's market!*** *The problem with being "all bear all the time" at a moment like this is sentiment.*

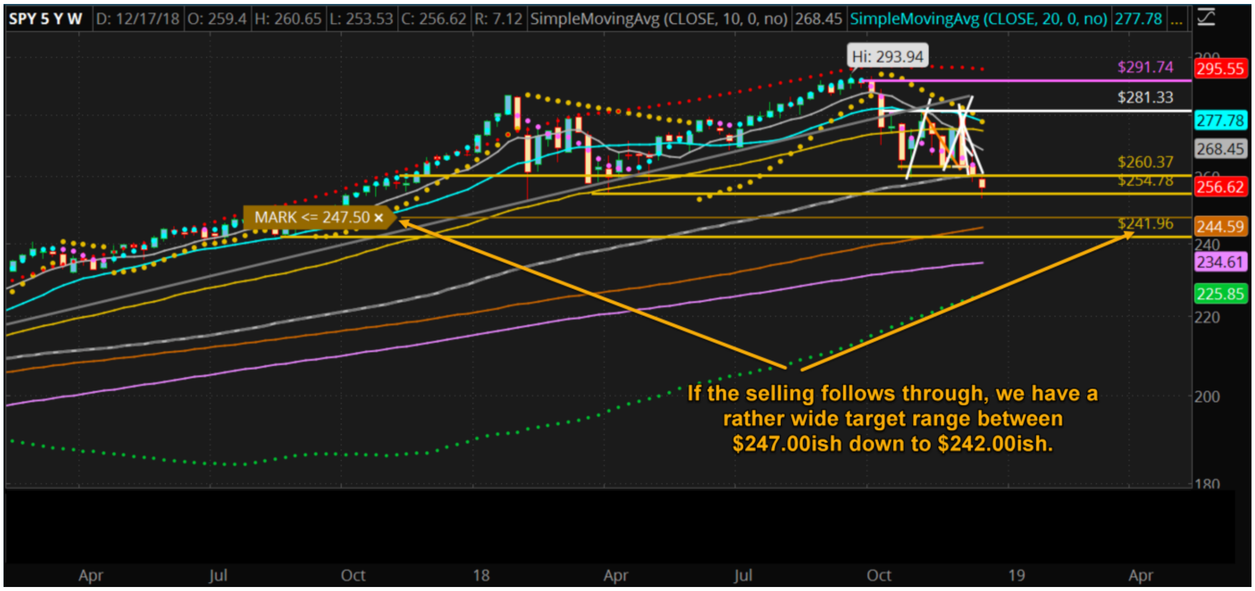
MARKET TRACTION

We’re really down there:

That’s essentially where we left off last week. We felt a little rally attempt coming and they did give it a go on each of the next two days after publication. The failure to rally in any significant way off the support level for 2 straight days had us focus back on extreme prudence. Friday’s action was ugly, but they managed a closing level that held off panic selling. Monday though, the defensive posturing was over, and we plunged through $260.00 in the SPYs.

MARKET TRACTION

HERE WE ARE NOW:



A “bigger picture” view provides us with a better sense as to the degree of vulnerability.

Looking at the current action more closely on the daily chart, we’re now post-breakdown. We’re between two levels we expected to matter and now we are in wait on a ton of news. Do we see a rally that fails near $260.00 confirming the breakdown or is it already too painful for too many for that scenario to even launch?

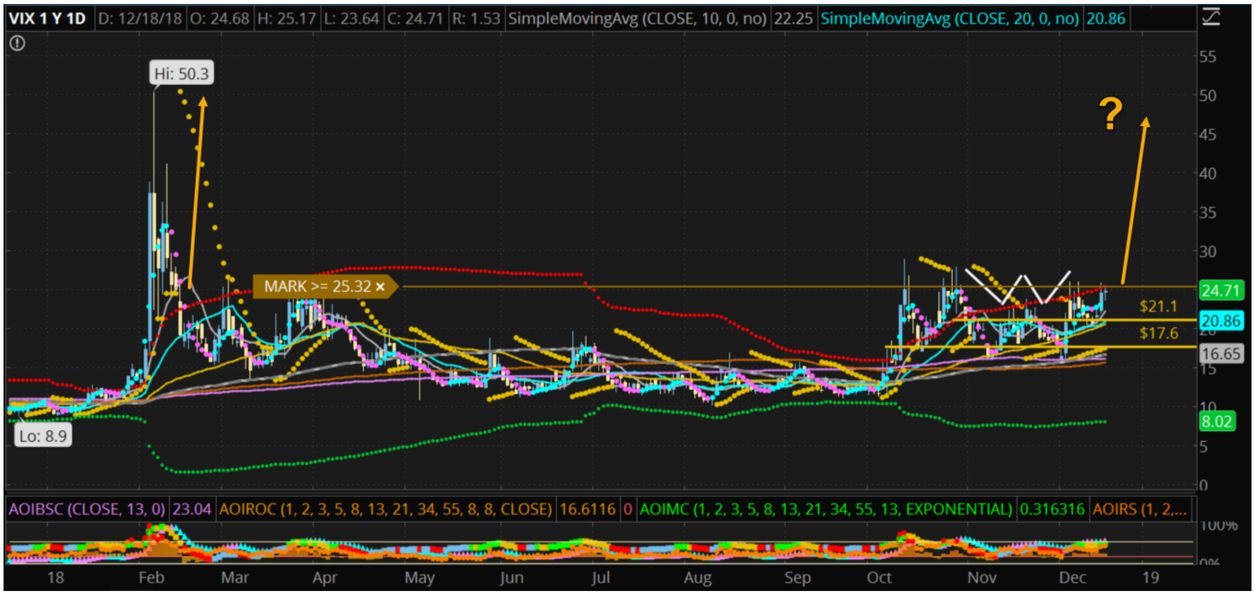
Last week’s **Market Outlook** wasn’t alone in acknowledging that the bears had to be given the benefit of the doubt as here’s our last line from **BTR**:

Until then and as noted above, we must give bears their due.

MARKET TRACTION

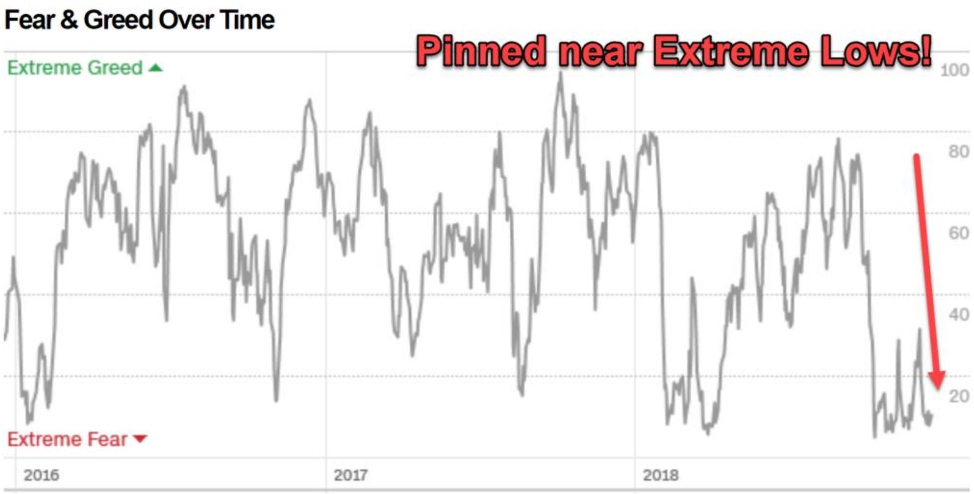
The wildcard this week is of course, various forms of dramatic market-moving news in the form of the FED announcement etc. Clearly, the FED could produce fireworks in either direction. As long as the SPYs are below $260.00 on a closing basis in the near term, we must treat matters as if the bull market is still in the process of failing. However, we know how volatile it can become in both directions during breakdown periods. There can be no doubt that the markets remain on edge and are challenging at best for bulls yet, and this isn't trying to have it both ways, many, many stocks are dramatically oversold. A FED pause on rate hikes may create the *mother of all short-squeezes* and just in the nick of time. Absent that, it's hard to see how we move much more to the upside beyond a brief relief rally.

Coverage beyond the S&P 500 is redundant this week. Correlations have really tightened up among the indices. The **VIX**, remains a whisker from a launch to much higher levels:



China and Europe continue to weaken and the "global growth story" can't buy you a cup of coffee right now. Key sectors like Energy and Financials continue to plumb new lows.

It will take something that's very dramatic to reverse all this in a meaningful way despite these extremely-oversold in the short-run readings:



But, that's exactly what news that this week will bring could do. Without it, the selling continues as we see it.

To sum up, bulls that have buying stocks on the way down (as pros are forced to do) have probably never wanted a FED announcement to be made more quickly and to deliver the goods for them like this one in at least 10 years. We expect more volatility hence last week's "Volatility Maelstrom" headline. Remain vigilant because some news event, perhaps a "**FED Pauses Surprise**" is possible and exactly what the ***Street of Schemes*** is banking on to save their bacon!

There are some big headliner-type reports due out this week, but we've got to assume that it's the ***Jerome Powell Show*** that will or won't do the trick…

MARKET TRACTION

This Week's Economic Calendar

TIME (ET)	REPORT	PERIOD	ACTUAL	MEDIAN FORECAST	PREVIOUS
MONDAY, DEC. 17					
8:30 am	Empire State index	Dec.	10.9	--	23.3
10 am	Home builders index	Dec.	56	--	60
TUESDAY, DEC. 18					
8:30 am	Housing starts	Nov.	1.256mln	1.230mln	1.217mln
8:30 am	Building permits	Nov.	1.328mln	--	1.265mln
WEDNESDAY, DEC. 19					
8:30 am	Current account	Q3		--	-$101bln
10 am	Existing home sales	Nov.		5.17 mln	5.22 mln
2 pm	FOMC statement & projections			2.25-2.50%	2-2.25%
2:30 pm	Jerome Powell press conference				
THURSDAY, DEC. 20					
8:30 am	Weekly jobless claims	12/15		218,000	231,000
8:30 am	Philly Fed	Dec.		14.0	12.9
10 am	Leading economic indicators	Nov.		--	0.1%
FRIDAY, DEC. 21					
8:30 am	GDP revision	Q3		3.5%	3.5%
8:30 am	Durable goods orders	Nov.		1.0%	-4.3%
8:30 am	Core capex orders	Nov.		--	0.0%
10 am	Personal income	Nov.		0.3%	0.5%
10 am	Consumer spending	Nov.		0.4%	0.6%
10 am	Core inflation	Nov.		0.2%	0.1%
10 am	Consumer sentiment index	Dec.		97.2	97.5

Below the Radar

After finding some potentially timely information on the timing window for a "Santa Claus" rally, we went full **BTR** mode and ended with the "Top Ten reasons why we may be entering a Bear Market."

Here's the line that led into that concluding section:

As for going with a flow that looks scary right now*, here's a great Top Ten list from Lance Roberts but inspired by Doug Kass:*

Then, we added this paragraph to conclude **BTR**:

*Just as with last week, we weren't able to find a lot but what we did find gets the job done****. We had to close out BTR on a bearish note because we won't even begin to believe that the Santa Rally (which we've also speculated about) is underway until we see a close above $270.00ish in the SPYs at some point soon. Until then and as noted above, we must give bears their due.***

We share the same sentiments this week, but we also must acknowledge that the markets are very oversold at this moment in time.

For much if not all this year in practical terms, we've harped on remaining nimble because we kept sensing that much could unfold in both directions. This year was much different than 2017. It turns out, this year was a very special one, and our senses were on it:

This is the most volatile year on record, and one strategist sees wild moves sticking around

PUBLISHED FRI, DEC 14 2018 • 12:56 PM EST

https://www.cnbc.com/2018/12/14/after-the-most-volatile-year-on-record-strategist-sees-more-to-come.html

We're onboard that train until further notice. The holiday weeks tend be listless and calm and so that could be the case even this year. Who knows? The bigger, longer picture though is one of turmoil and adjustment and that should keep volatility elevated. Positive signs emerging suddenly, maybe from the shopping season, could change our take but we're already concerned about next year because…

The backdrop though, continues to worsen and in the worst place possible:

https://wolfstreet.com/2018/12/11/us-bank-stocks-spiral-down/

https://wolfstreet.com/2018/12/13/us-banks-disclose-biggest-unrealized-losses-on-security-investments-since-q1-2009-fdic/

Those links are worth visiting but this one, which is quite long, is a very good read as to what MAY happen next year:

https://www.theinstitutionalriskanalyst.com/single-post/2018/12/18/Risks-2019-Quantitative-

MARKET TRACTION

Tightening-Eurobanks-China

The destruction of trillions in equity market valuation is creating a level of panic in the US markets not seen since 2016, when China fears caused the capital markets to seize up. We may be replaying that scenario again. With high yield spreads headed to the danger zone of 500bp over Treasury yields, that tells you that the policy message coming from Washington is off key. But it also means that the market for subprime debt, including leveraged loans and CLOs, is grinding to a halt. ***That sound you hear is Wall Street choking on conduits full of loans that cannot be sold.***

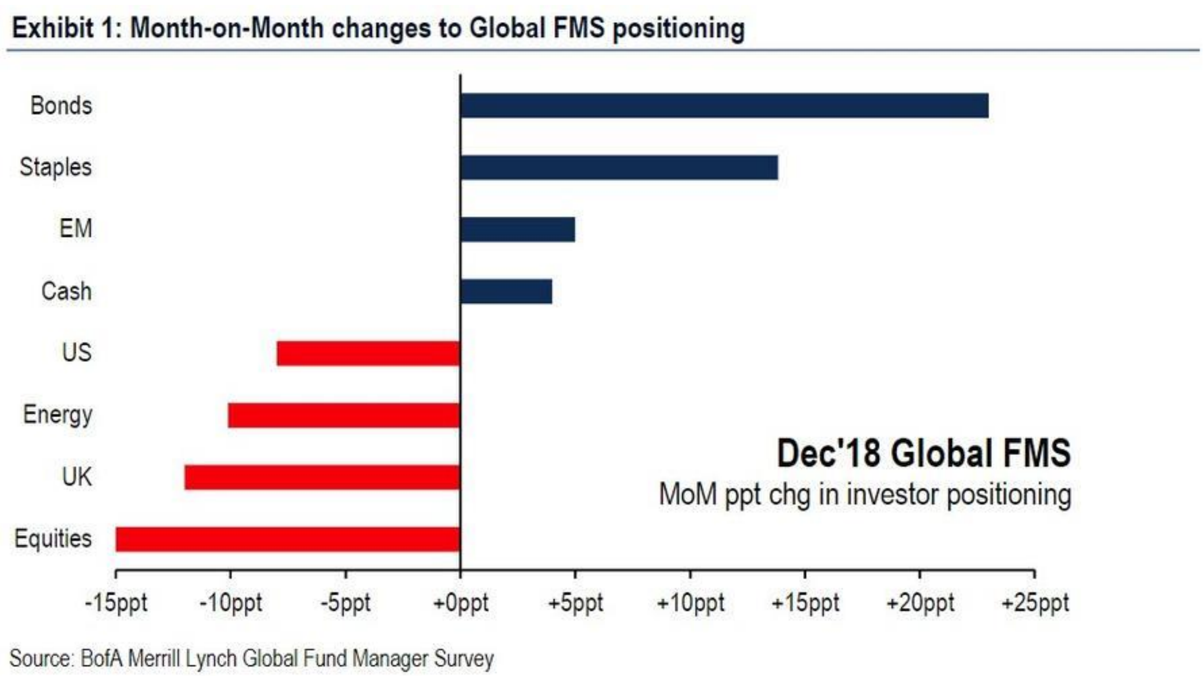
Feldkamp's First Law states that when spreads widen too much, debt markets stop functioning and equity markets lose value. *We talked about this in "Financial Stability: Fraud, Confidence and the Wealth of Nations." When the mix of policy and personalities is toxic, spreads blow out, debt markets freeze, and wealth as measured by the equity markets falls. Sadly, there are only a handful of people on the Street who get the joke. The majority is captive of a narrative where trade tensions are responsible for market weakness.*

Next on the string of worry beads is Europe. ***The European Central Bank just announced the end of its version of "quantitative easing"*** *or QE, but unlike the US the ECB intends to reinvest its bond portfolio indefinitely. There will be no "quantitative tightening" in Europe by actually allowing the portfolio to run off as in the case of the US Federal Reserve. We reported this to readers after our trip to Paris last March.* ***This past week, ECB Governor Mario Draghi confirmed our belief that EU banks cannot withstand a significant increase in rates.***

Those kinds of worries and a FED that's been, to this point, thought to be hellbent on over-tightening, is scaring the hell out of money managers and so they're seeking relative safety and exiting the equity market. Which is why "buy the dip" has recently become "sell the rally":

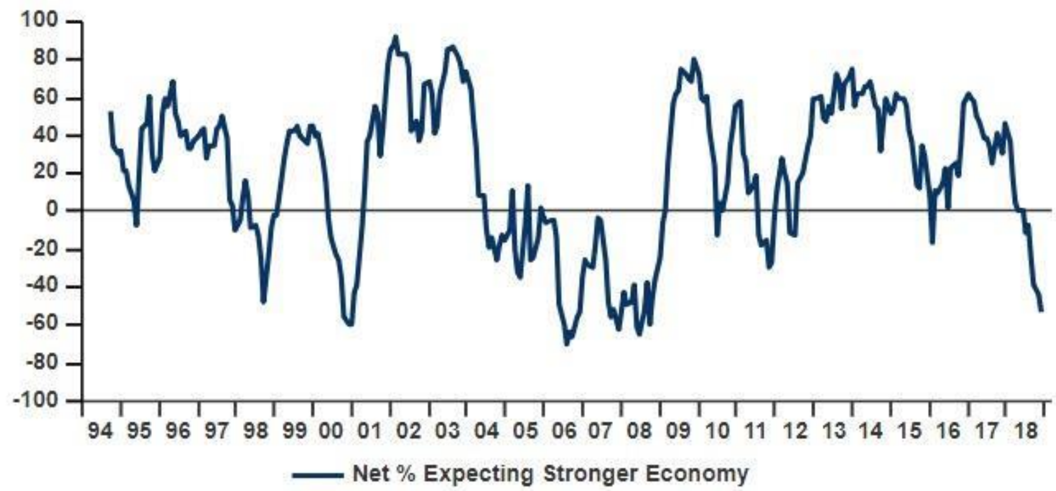
https://www.zerohedge.com/news/2018-12-18/wall-street-turns-apocalyptic-we-just-had-biggest-ever-rotation-bonds

Here's what they've been up to recently:



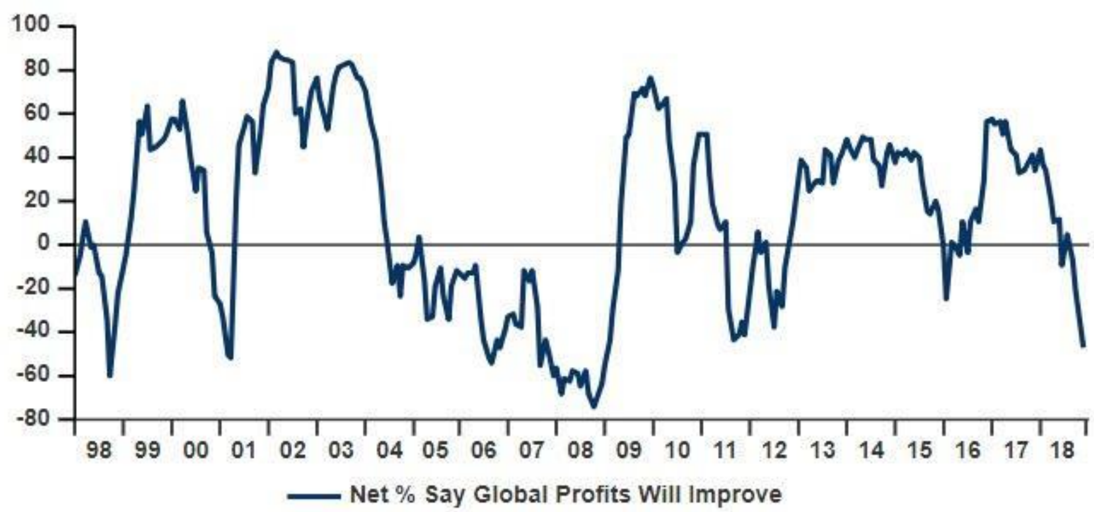
That’s stark but so are these glimpses at a few key areas as per fund manager survey responses:

Exhibit 7: How do you think the global real economy will develop over the next 12 months?



Source: BofA Merrill Lynch Global Fund Manager Survey

Exhibit 29: Profit expectations



Source: BofA Merrill Lynch Global Fund Manager Survey

Very similar and very ugly. Essentially, they expect to see pressure on revenues and profits worldwide. Can it be a surprise that so many are pressing the “sell button?”

If that doesn’t do it for you and you need more to really become concerned, how does “weaponizing stock selling” in a trade war strike you?

https://www.zerohedge.com/news/2018-12-18/nomura-sees-institutional-derisking-accelerating-fears-weaponization-stocks-trade

To make matters even worse, it hasn't been and won't be ONLY US money manager selling US assets, yea, it's global and they're selling everything:

https://www.zerohedge.com/news/2018-12-17/foreigners-dump-us-treasuries-they-liquidate-record-amount-us-stocks

How bad has it been lately? How unseasonal has November and December's action been? Pretty darn!

http://theeconomiccollapseblog.com/archives/stocks-are-on-pace-for-their-worst-december-since-the-great-depression-the-dow-is-now-down-over-3300-points-from-the-peak

And that's a very good item to consider. The Wall St. Gang had their entire year on the line (EOY bonuses) and they'd taken a rough hit early in the year but managed to walk stocks back to new highs in early October. They were set up nicely to *jamma, jamma, jamma* with respect to seasonality. Instead, we've witnessed the opposite. That tells us a lot. There must be very serious concerns being harbored in very many high places for the equity markets to be on the mat with less than two weeks left in the year!

As it has been for more years than we can remember, it's once again up to the FED to save Wall Street's pork bellies and in doing so their year and maybe many more years for all we know! The FED, from our vantage point, would appear very out of touch if they raise rates tomorrow with all that's unfolding around the world. If they continue raising rates this week most will see them as being near-blind to the worldwide deterioration of markets and economic conditions. Assuming they pause, is that enough to ignite and sustain an EOY / Santa / Save our Year End Bonuses / Oversold / Short Squeeze / Relief Rally? One would think! Stay tuned and be careful out there as the news of the week is likely to make or break!

Remain nimble my friends!

Bank and Roll!

Options Academy

Understanding Beta for your Portfolio – Creating a Diversified Portfolio with Beta

Keeping an eye on a stock's Beta and factoring that into your asset allocation plan within your portfolio will diversify your holdings and help to reduce overall risk.

Remember from last week that Beta is a risk measure that helps us to understand how volatile and correlated a stock's price action has been, over a certain period of time, in relation to an index of stocks (S&P 500). Market risk is market risk. It's typically referred to as "systematic risk", as in the risk associated with being a part of the system (being in the stock market). We can't diversify that type of risk away as it simply exists.

"Unsystematic risk" on the other hand is also known as "stock specific risk" and, to an extent, we can diversify that away. Consider this…

Let's say we were all lathered up about "FAANG" stocks (formerly the big tech leadership stocks) earlier this year. Things were going well but clearly the past few months have been very hard on FAANG. What if we'd owned some utility stocks too? Or maybe we owned defensive names like grocery chains. Owning those other areas of the market that haven't gotten pasted lower the way FAANG has would have diversified our holdings and cushioned the blow a little, at least potentially. The point is that not all stocks will act the same way and to the same degree as the market rises and falls. We know that. Some are simply more volatile and vulnerable while others are not. Owning areas beyond tech provides us with a more diversified basket to weather the storms.

One consideration when using Beta to help assemble your stock portfolio would be to evaluate your own risk appetite. You need to get a sense of what you're comfortable with owning and if that will get you to where you need to be in terms of your retirement plan given the number of years left until you retire.

Let's assume that you'd like to own some high-profile names like we alluded to above, for instance:

Apple

Google

Microsoft

Amazon

Netflix

Facebook

Priceline

Not all those stocks are super-high Beta but some of them do have a Beta greater than 1 and are thus more volatile (risky) than the market in general. So, what do you do? You need to balance things out with some other stocks and assets with Betas lower than 1. Think about picking up some defensive names like food and beverage companies, larger somewhat boring companies like JNJ (oops, minus the lawsuits), utility companies and of course the safe-haven lead actor: bonds. If you mix those in, they'll generally be *ho hum* on the way up but will feel like a warm blanket when the indices are cascading lower led by your big tech holdings.

It's critical to avoid too much of any one thing. Think about it, most oil stocks will react in similar ways to the price of oil per barrel. Most financials will be interest rate sensitive in similar way and degrees. It's fine to overweight an area of the market, but just avoid doing concentrating too much in one sector. If you do, make sure you use lower Betas (<1) and negative Betas (-1) before you're through fully constructing your portfolio.

The next part of the series will discuss how to Beta Weight your portfolio risk in specific terms.

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