MARKET TRACTION

IN THIS ISSUE:

Minutes, Speeches, Tweets and Conflicts…

This Week's Trade Ideas:

Bullish Ideas:

(View Webinar) Marvell Technology Group > MRVL* > $21.92** Last. Buy the Jun 1st 21.5 Calls for $1.17 or less with a close or anticipated close above $22.22 in an up market with expectations for continued strength in the major indices. (Earnings due out on May 31st after the close!!!)

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(View Webinar) KEY*, XLF*, MS*, USB*and STI* (FOMC minutes), ON.

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AND/OR:

(View Webinar) EBAY Inc. > EBAY > $37.77 Last. Buy the Jun 15th 39 Puts for $1.55 or less with a close or anticipated close below $37.69 in a down market with expectations for continued weakness in the major indices.

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Below the Radar:
The Russell 2000 of late looks a lot like the S&P 500 of January! Just as then, it seems that the money manager herd has chased up the price of smaller (mainly domestically focused) companies as if there's no tomorrow! They're all in, on one side of the boat it would seem. This is very interesting to us as this suggests that they're so concerned over a global slowdown, they're driving up prices in domestic stocks as at least a partial hedge! However, they may have driven them up too far and too fast. We'll soon see if the current breakout and trajectory are sustainable. To add to the intrigue, we present, the Dow Jones Transports ETF (IYT):

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Last week we after covering the covered call and a few trade scenarios related to that strategy, we alluded to another strategy that we strongly prefer vs. the covered call. That strategy is known as the Diagonal Strategy. We'll cover it in the same manner this week as we did the covered call last week. Hopefully, readers will see why we feel as we do after completing this week's *Grand Finale*.

Make sure to attend the ***Morning Call*** each Wednesday morning at 11:00am Eastern Time. This webinar is included in your subscription so there is no extra charge.

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We're noting this AGAIN!

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

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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 **Advantage Point Morning Call** webinar for full details with respect to these idea(s), last week's and options education.

Week 16 of our Special Note:

Things may finally be sorting out for the Markets and we may soon see All-Time Highs across the board and may be on our way to even more ATHs. We believe that significant risk remains in the markets at this time, and we're not quite there yet to issue an "All Clear". – We're getting closer, but we still plan to approach the markets with a great respect to current risks, so…

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! We've posted this with the **"All-Time Highs"** portion looking very unlikely at times and now it is looking at least like a possibility. That's how much we've had to contend with over the past several months!

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:

Last week: *"Right now, we're pulling back from short-term overbought levels."* That's where we were last Tuesday, and we stayed around those levels for a few days that followed. We put out updates covering the fact that the SPX was trapped between the 100 SMA as support, and a nearby resistance level, note the white oval:

After a few days of pulling back from overbought, the SPX began to move higher and is now trying to add another leg to its recent bullish run. We could be closing a gap, we could be double-topping, we could be about to scream higher! We're at a very interesting juncture currently.

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 we were a little more split on direction than we have been recently. We had a similar number of symbols to work with on either side, depending on if the bulls or bears became more aggressive. The market did try to move up and didn't fair too poorly on Wednesday and Thursday, but Friday brought a real fizzle! That was enough for us to trigger additional communication, and thus one of our updates noted that it might be time to take what was to be taken had you been playing the bull side for a few days. Playing the bear side wasn't up for consideration to that point, since the markets were trying to rally and simply refused to break down below the 100 SMA support on the SPX.

Official bullish idea, **TX**, looked good on Wednesday, maybe too good, and was OK on Thursday morning, but the rest of that trading day didn't treat it well. When we saw it struggle again on Friday along with the **SPX**, we put out another note suggesting prudence. In the end, **TX** couldn't break out, it stalled at the resistance that we noted was key and reversed and now could be producing a double-top. We have to chalk this up as a disappointment, but we have to view it in context of a market itself that couldn't break out last week. Sometimes, as was the case here, stocks just can't get rolling enough if the indices refuse to roll, and that's how we view **TX** and the **SPX**. **TX**, for those who may have traded it, was probably a small loser unless it was exited for a small profit near the resistance level we discussed but that would likely have required an early preference for that or watching it intraday and cutting and running once it lost its momentum on those charts. Now let's move on to our bullish mentions…

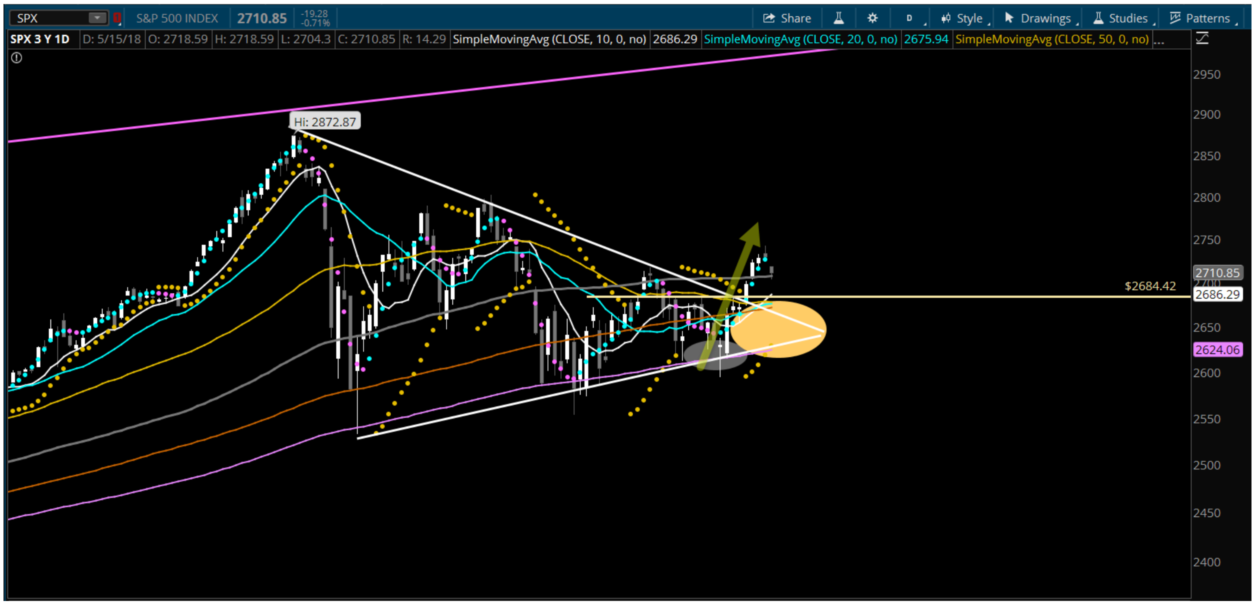
HAL, KEY, NYT, VOYA, and **ALB** were all bullish mentions**.** As if OFTEN the case, our mentions easily outperformed our main idea by and large!

HAL moved up a little over $2.00 from publication. **NYT** moved up about $1.50, which made us happy due to its low cost. **VOYA** moved up about $2.00 too. **ALB** was probably our standout as it moved up nearly $5.00 and maybe exceeded our expectations given the resistance level we discussed. **KEY** moved up small, very small, as it wasn't able to push through the nearby resistance level we hoped it would. With respect to these, we're happy overall. The market did rally, and most did move up with it. They didn't deliver huge moves but that's to be expected in a bottled-up market. We can never forget that the market environment we operate within is the most important factor of all.

Our bearish idea and bearish mentions, **KO,** and **JNK, VWO, MGM, CELG, SBUX, ED,** respectively, we're all out of consideration with the SPX trying to rally. If one were to go back and evaluate those charts since, it's clear that it is much better to have the market's wind at your back! A few fell off nicely, a few rose a little higher, and a few didn't do much. That's why we go with the flow of the indices and select from those names primarily!

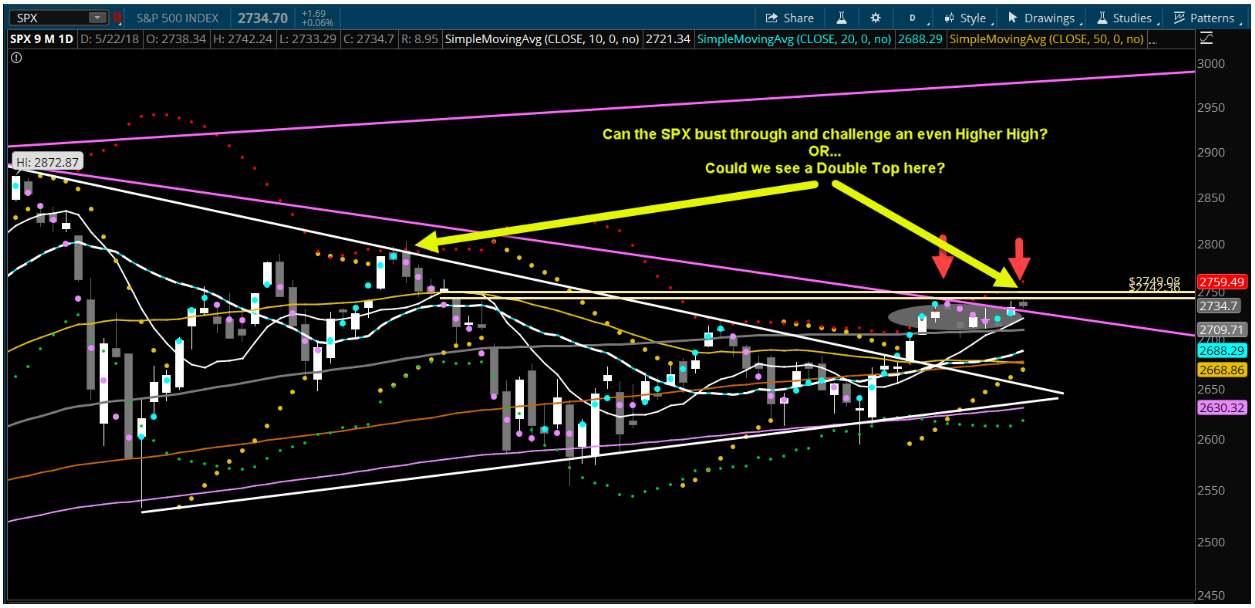
Market Overview

From last week:



So…now, the Gang has pushed things above the resistance line of the triangle. We've also made a higher high. Normally, that would bode well for bulls expecting more "recovery". However, are thoughts, as *they were last week, are that this still could be a false breakout. Additionally, we can't rule out a drop back to the resistance lines to convert them to support. Thus, we're still on guard for now.*

We're thinking that we sniffed things out to a fair degree as the market, by the end of the week, hadn't done much as Friday's close was just about the same as Tuesday's close when we covered it. It was only on this Monday, with the "China news", that the SPX was able to explode higher, as did the other major indices. However, we're not out of the woods…yet…:



The picture says it all, nearly… After finding support on the 100 SMA while retracing, the market doesn't have far to move to push past the recent top. There should be quite a bit of energy to propel the index through to possibly challenge the next key visual high. Things have stagnated as we write and not just in the SPX. FAANG is also just treading water. Thus, there's no follow through and that's a little troubling. We must remain prepared and nimble. That's all there is to it. This is a very interesting juncture and we have a suspicion that matters will be propelled forward on news to which we're not privy but will soon be introduced to, *a la* the China news.

So, as we noted last week: *With a higher high, the bulls have left their mark but now they need to hold the line, literally! The news cycle seems relentless these days and we don't expect it to suddenly peter out.*

We're nearly in the same place a week later. As for the Q's:

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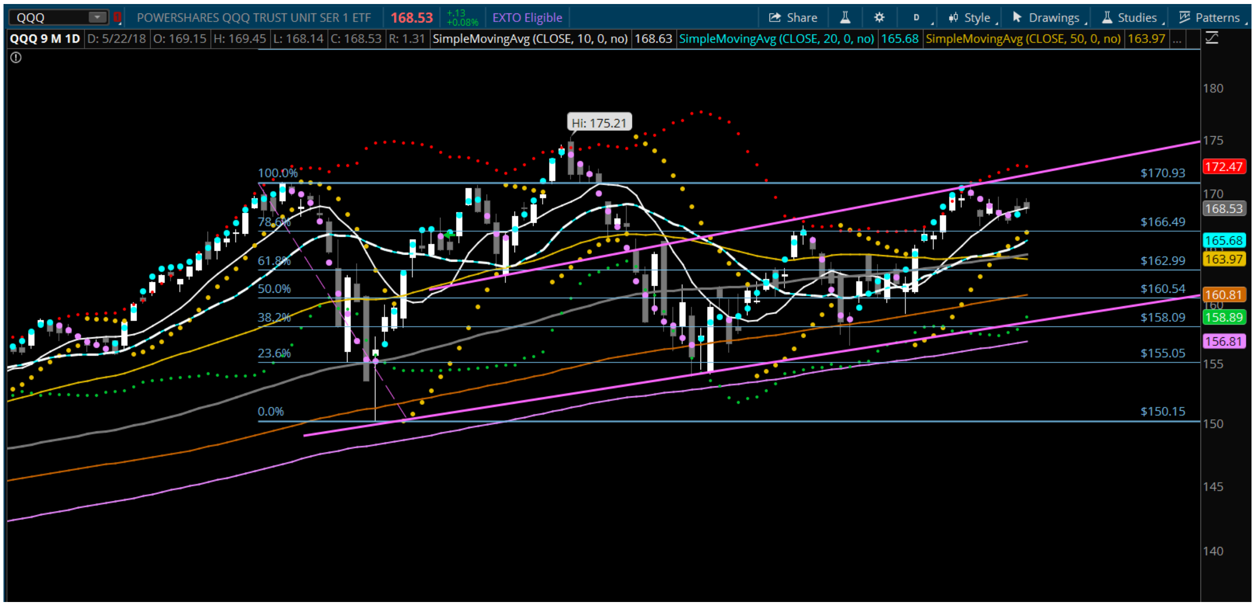


The channel we displayed last week has held itself intact. We're in *wait mode* there as well however. There's no much more we can draw on presently. We'll need to wait to see if Monday's rally continues or fades. We should know soon.

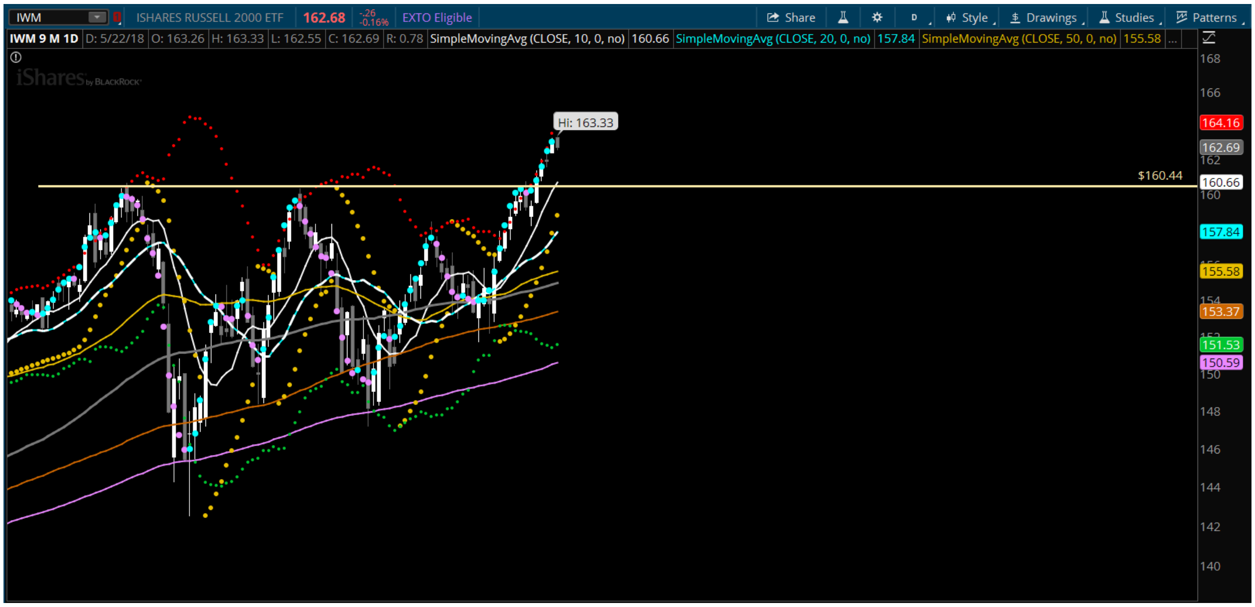
The Calendar, especially due to the FOMC minutes and various speeches, should once again help propel motion should the Wall St. Gang want it!

This Week's Economic Calendar

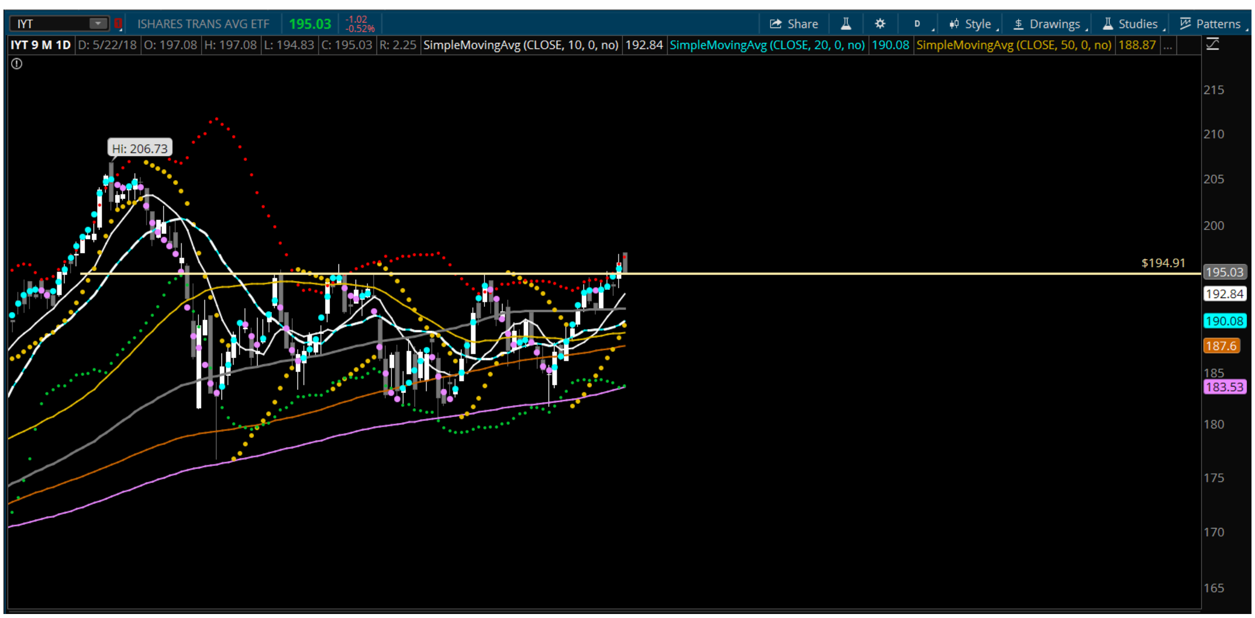
TIME (ET)	REPORT	PERIOD	ACTUAL	MEDIAN FORECAST	PREVIOUS
MONDAY, MAY 21					
8:30 am	Chicago national activity index	April	0.34	--	0.32
12:15 pm	Raphael Bostic speech				
2:15 pm	Patrick Harker discussion				
5:30 pm	Neel Kashkari discussion				
TUESDAY, MAY 22					
	None scheduled				
WEDNESDAY, MAY 23					
9:45 am	Markit manufacturing PMI (flash)	May		--	56.5
9:45 am	Markit services PMI (flash)	May		--	54.6
10 am	New home sales	April		682,000	694,000
2 pm	FOMC minutes				
THURSDAY, MAY 24					
4:15 am	William Dudley speech				
8.30 am	Weekly jobless claims	5/19		219,000	222,000
10 am	Existing home sales	April		5.50 mln	5.60 mln
2 pm	Patrick Harker discussion				
FRIDAY, MAY 25					
8:30 am	Durable goods orders	April		-0.8%	2.6%
8:30 am	Core capital equipment orders	April		--	-0.4%
9:20 am	Jerome Powell speech				
10 am	Consumer sentiment index	May		98.9	98.8
11:45 am	Charles Evans, Rob Kaplan panel				

Below the Radar

We’re including a little of our own charting material in **BTR** this week as *far out on the horizon* concerns are still capturing the headlines NOW. Just below is a plain but interesting look at the Russell 2000 ETF, IWM:



The Russell 2000 of late looks a lot like the S&P 500 of January! Just as then, it seems that the money manager herd has chased up the price of smaller (mainly domestically focused) companies as if there’s no tomorrow! They’re all in, on one side of the boat it would seem. This is very interesting to us as this suggests that they’re so concerned over a global slowdown, they’re driving up prices in domestic stocks as at least a partial hedge! However, they may have driven them up too far and too fast. We’ll soon see if the current breakout and trajectory are sustainable. To add to the intrigue, we present, the Dow Jones Transports ETF (IYT):



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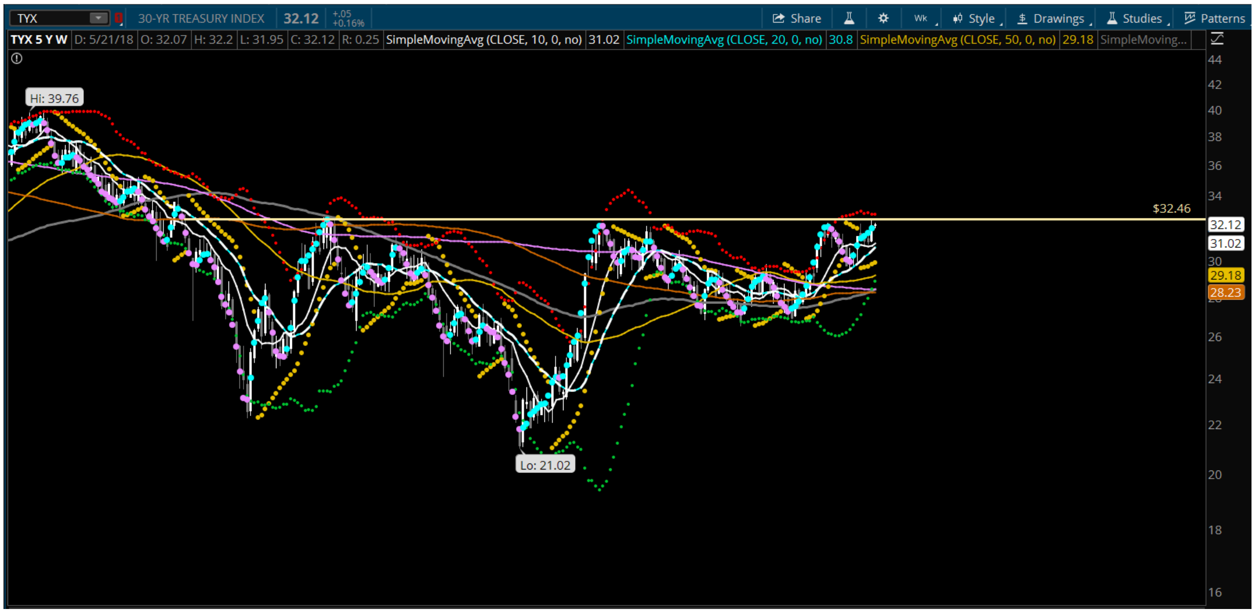
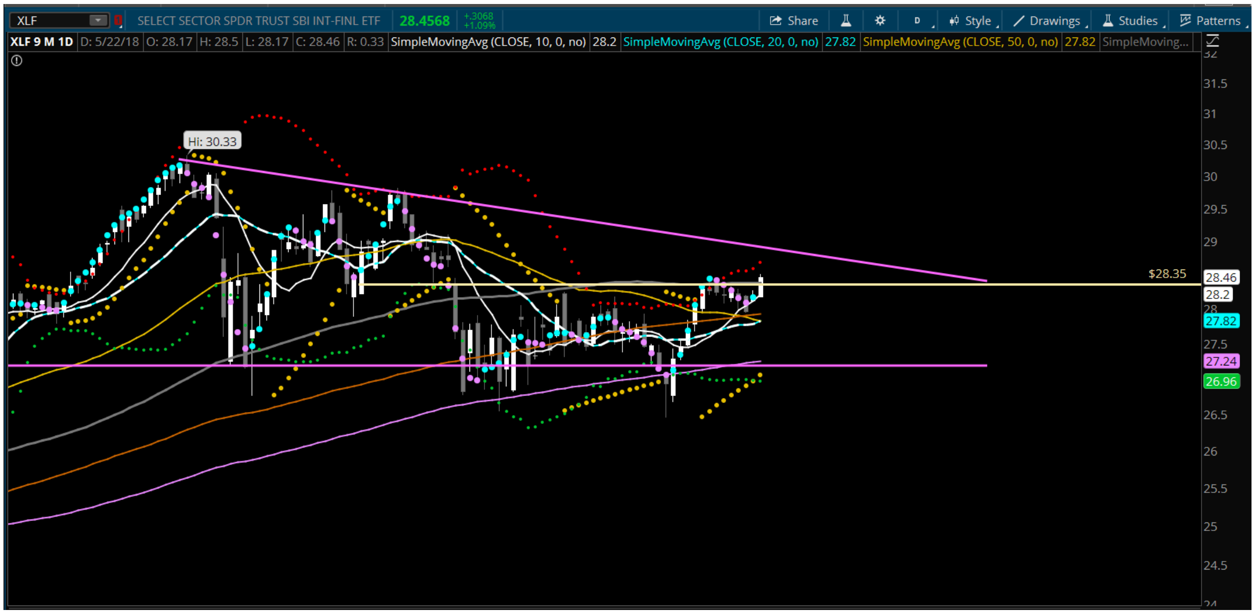
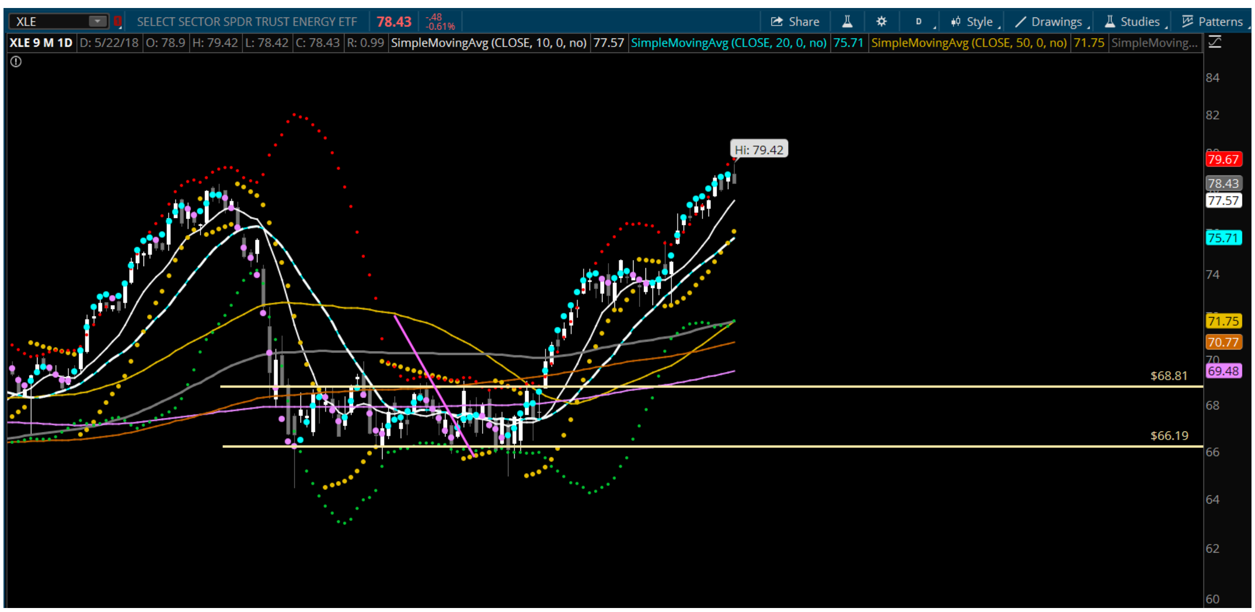
The IYT seems to be attempting to breakout presently. Transportation stocks acting well is normally a good sign for stock prices and the economy as it indicates that commerce is healthy and possibly even picking up. If this is the case, in the face of higher energy costs to boot, wouldn't this suggest that things are well and that there's no need to "hedge" in the Russell 2000? Have money mangers panicked to deeply into the Russell? OR, is it possible that things are BOTH picking up domestically and the international/global scene remains solid? If that's the case, why haven't the major indices rallied more? Did January's blow-off-jam-job price in far too much *goodness* far too quickly? OR, does something else explain the market's inability to jam to new all-time highs?:



Above we can see that the TYX (representing the 30-year Treasuries Yield), is threatening to break nearby upside resistance and that there may not be much in the way of resistance if in fact it does! That means, rates could be about to take a leap upwards! That could very well be tempering bulls' appetites for buying more shares at these prices, especially when we consider January's historic euphoria and valuation levels. When we add in ever-increasing debt levels of consumers, possible wage pressures from the lowest unemployment rates in a half century, already goosed energy prices etc., we can see why the major indices haven't yet moved unrelentingly higher but that can be on the verge of changing:



The financials are a very important sector and they're finally on the verge of moving higher, it would seem, as they're now at least trying to push above resistance as can be seen in the chart of the XLF ETF above. Higher rates, higher profits in financials is the current thinking. Higher rates, greater commercial activity occurring, at least in theory (not necessarily ours). The energy sector, while influenced by many factors, including geopolitical ones, seems have at least factored in some improvement in demand and thus growth:



Some may say, after viewing that chart, that maybe the XLE buyers have factored in a lot of growth! Clearly, that's made a new recent high. So…here in **BTR**, we're noting that the technical complexion of the markets continues to improve despite some conflicting information that's bubbling around in the news and in the charts. The problem may be, that nearly all charts look to be headed higher!

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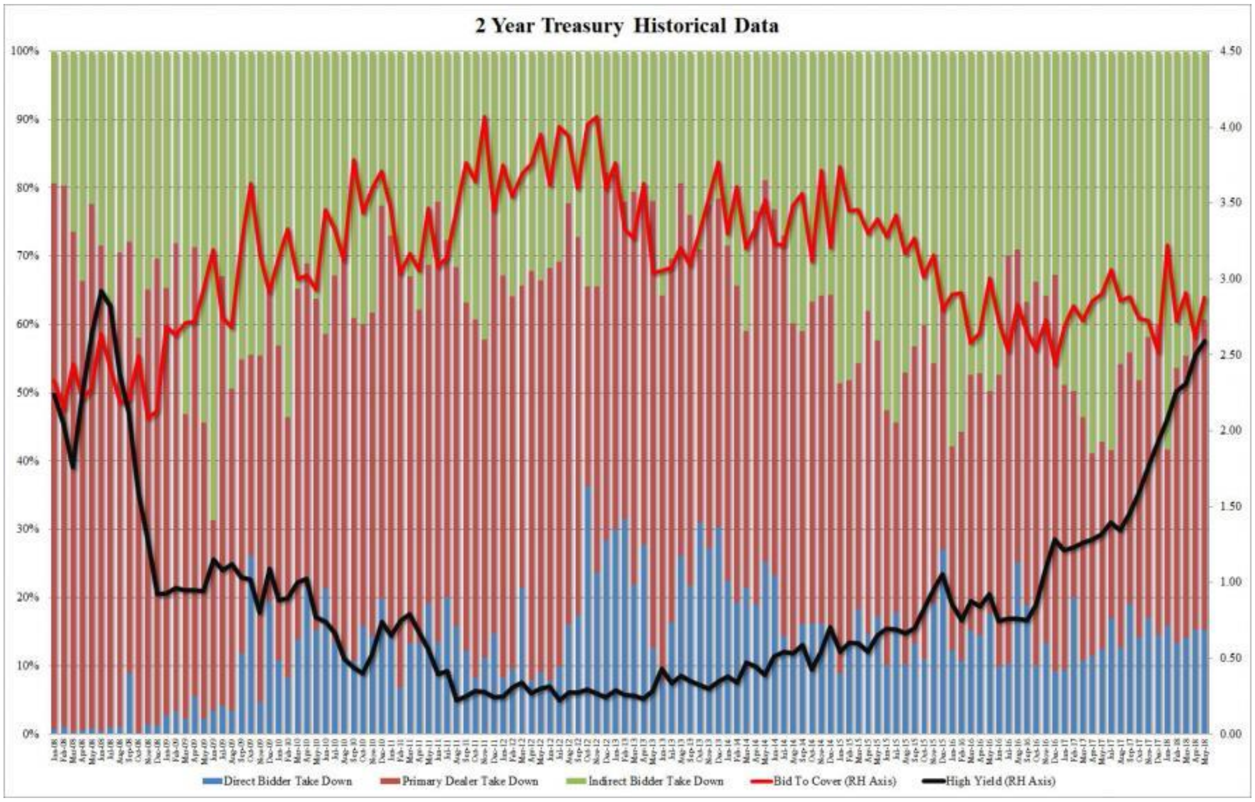
It’s clear that we’re much better off than a month ago and thus we’re trending deeper into greed but there’s a lot of room left before we get there.

Here’s a chart, that while hard to read due to compression, is more of the standard fare we normally serve up in **BTR**:

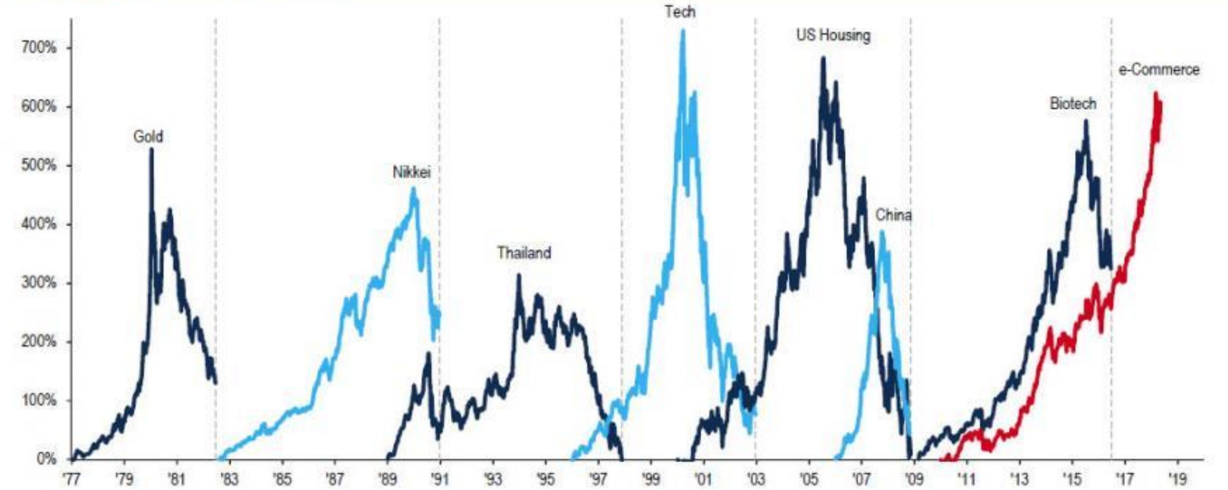


So, while we concluded above with our own charts, that things are improving now, we can’t say that we’re without concern. The takeaway, which is difficult to isolate, is that the 2 Year treasuries are now yielding 2.5% for the first time since 2008! Combine that with our 30 Year TYX chart above and it becomes clear as to where short and long-term rates are headed. Does this potential development choke off increasingly debt-dependent consumers and usher in the long-feared recession that's been talked about for so long that's not actually yet come to pass? Will rising wages, that have long-been pined for but of late been a source of inflation concerns, add fuel to the rate fire we may be on the verge of seeing?:

We've got nearly everything heading higher and something must give and give rather soon. Maybe not this week or next or even next month or the following month, but somewhere into the Summer or maybe early Fall, we may finally witness resolution of some of this seemingly conflicting data and trends of data. In addition, with financials on the verge of jamming due to rates, and energy already having jammed, there appears to problems developing for stocks in other sectors as the rising cost of energy and capital will be an issue in most places. With the US dollar bouncing of late and the tax cut seemingly discounted into stock prices, many could again be thinking that we've seen the best earnings performance we're likely to see and that paying near-record prices for the market at this juncture may not be a prudent move to make. And then there's this:

Tech: 3rd largest investment bubble of past 40 years

Chart 8: Asset price bubbles of the past 40 years



Source: BofA Merrill Lynch Global Investment Strategy, Bloomberg. Note: Gold (XAU Curncy), Japanese Equities (NKY Index), Thai Equities (SET Index), Tech (NDX Index), US Housing (S5HOME Index), Commodities (SHCOMP Index), Biotech (NBI Index)e-Commerce (DJECOM Index)

Would our mini-summary above be enough to pop the e-Commerce bubble as it is being called? Will news of government intervention and regulation of the tech giants be the flashpoint that finally triggers sizeable selling in those most-crowded/leadership stocks while all those other issues were building?

These are very interesting technical times. A short-term move higher in equities looks entirely possible and with just a little more push is likely to happen. Conversely, that could be exactly what lays the groundwork for future failure in the intermediate-term should the presumed rally not deliver enough. Should it play out that way, we'll need to see how much damage the intermediate-term selling triggers before contemplating what that may portend for the long-term trend. Then again, the charts could change dramatically if Wednesday's FOMC minutes are seized upon by market participants. We must remember that we're 3 to 4 months away from this becoming the longest US bull market on record…

Bank and Roll!

Options Academy

Last week we after covering the covered call and a few trade scenarios related to that strategy, we alluded to another strategy that we strongly prefer vs. the covered call. That strategy is known as the Diagonal Strategy. We'll cover it in the same manner this week as we did the covered call last week. Hopefully, readers will see why we feel as we do after completing this week's *Grand Finale*.

We'll use slightly different prices but the same date we used last week in MSFT. MSFT closed at $97.32 on May 15th, just a little higher than our simulation last week. We're going to adjust for that, but it really doesn't change much. This week, instead of buying shares of MSFT, we're going to buy an outer-month deep ITM call to serve as a proxy for shares. There are many ways to go about selecting this "anchor call", but for now, we're going to keep it simple and move out to just after the Summer and into a September contract. We'll then select the Sept. 21st 80 calls which we can buy for $18.15. This will serve as our replacement for 100 shares of the underlying MSFT stock as it effectively allows us to control 100 shares for several months and serves to cover the risk we'll entail when we sell our premium collection call next. Please note that this call purchase creates a $98.15 breakeven point* on this leg alone. Once again, let's lay out our 3 scenarios:

We can sell the very slightly OTM June 15th 97.5 calls for $1.97. (There are other ways to do this, but this one will work for us for now.) We selected that call as it brings in nice chunk of premium in just about 1 month (31 days). That will provide us with easy extrapolation for a full year (12 months). We can be more aggressive sellers by selling only 1 or 2 weeks out in time, but we're keeping it simple as the concept is more important than the mechanics at this point. We'll look at 3 outcomes of the many that are possible:

A: The stock *sits still*, and we collect the full $1.97 but it's not as straightforward as last week! Last week we utilized shares of stock to write this call against. Shares have no decay since it has not time value! It simply exists in perpetuity*. Options, though, do have decay associated with them, obviously. So, we have to account for that here on the one we own. There are other assumptions we're making as well but we're keeping this simple! So, for now, we must note that if MSFT sits at $97.32 on June 15th, our Sept. 80 call will have lost $0.59 due to decay. Thus, dollar wise, we're not up the full $1.97 but rather $1.38. Thus, on our $18.15 stock proxy call, we'd make $1.38 on that for the month: $1.38 / $18.15 = 7.6%! That's very, very darn-great compared to the covered call's 1.9% from last week! Now, let's project that out over 12 months but without any fancy compounding math. 7.6% x 12 months = 91.2% annual return! (simplified), vs. last week's 22.8%! We're crushing the covered call and once again we're doing it on what's considered a very safe stock which is a very important part of the process. It's much, much harder to knock this outcome and now much easier to knock last week's similar scenario, which, actually, looked pretty-good for a minute or two there!

B: The stock rises to $97.50 where it closes on expiration day. In this outcome, we net $1.55 because the stock is up a little and we're net long delta. We'll take it! Thus, $1.55 / $18.15 = $8.5% for the month! This is an ideal outcome which is similar but better than A. In this case, we keep the full $1.97 of premium on the short call but and lose less on our anchor call due to the stock price rising. Thus, we make $1.55 for the month. $1.55 / $18.15 = 8.5% per month x 12 months = 102% annually! Woohoo!

C: The stock drops $1.97 from where we bought it and closes there on expiration day. $97.23 - $1.97 = $95.26. Naturally, we keep the $1.97 but we'd lose on decay and on delta in our outer-month call for a total loss on it of $2.33 on it. Thus, we'd lose $0.36 to that point. NOW, had we owned the stock instead, we'd have lost $1.97 on our shares which would perfectly be offset by the $1.97 of short call income and thus our net would be $0.00 (Otherwise known as Kent Dorfman's GPA 😉) On this one, we'd lose a little more even though we had lower delta with our ITM call than stock. This is due to decay over 31 days.

As we noted last week, because we receive a credit on the sale of the short June call, our basis is lower than the $18.15 we paid for our anchor call in these scenarios, it's actually $16.18. Again, our performance was even better but we wanted to keep it very simple and so we're leaving that alone.

Moving on…there are many other scenarios that can play out but to keep it consistent we kept the same 3 as last week. In scenarios A and B, we dramatically improved our return percentage. If we committed the same amount of capital as we would have in the buy write/covered call scenario, we could have traded 4X as large and thus quadrupled our already far superior returns. In short, there's a lot to think about but it is very clear that a diagonal is far superior approach to the covered call even considering scenario C's slightly worse loss.

If you have questions, especially ones that are related to our (*s), ask away in this week's **Advantage Point Morning Cal**l webinar.