

How to Generate Trade Ideas for Potential Profits

19/04/2017

> **Examples of Fundamental Themes Driving Equities Markets & Trade Ideas for Q2**

- EPS is rising / catching up to price and the market is paying the price ahead of time.
- NIRP in Eurozone, Japan, Switzerland and rising rates in the U.S. is causing dislocation – There are very few places to hide money!
- Additionally, interest rates in the U.S. are expected to rise over the next 2 years and each rise is a given.
- The Fed will continue to increase rates for the foreseeable future but they have a lot of catching up to do!
- Whether you love him, hate him or you're not bothered, Trump's fiscal helicopter money plans with the simplification of the tax code, raising of the lower-end tax threshold, lowering of corporate tax, repeal of Obamacare, infrastructure projects and lowering of regulations puts significant dollars back into the pockets of consumers and businesses in the U.S. and could also cause large repatriations of USD.
- This puts a base under U.S. equities earnings and on a relative basis versus the ROW, money has to go into the U.S. !!!
- Money is chasing earnings growth on a global relative scale!
- It is much more likely that if companies hit consensus earnings they will continue to rally or even jump aggressively due to additional catalysts identified on earnings calls by management.

> Remember ...

> We are not providing investment or trading advice here.

> Nor are we making recommendations with respect to investing in or trading i.e. purchasing or selling specific securities.

> We are highlighting how the trade idea generation thought process works and using the current examples as a guide as to how the trade idea generation process can be put into practice.

> The examples shown in this presentation are a narrow sub-set of multiple trades / positions that could be implemented via stocks that exhibit similar fundamentals.

> You must always do your own work. We encourage you to do so by expanding on these highlighted themes to try and find other positions that could exhibit good risk/reward.

> If you decide to use the information in this presentation to take positions in your trading account, you are at risk and there is no guarantee of a return. You could lose some or all of the money in your trading account, depending on how well thought out your trade ideas are and how much risk you take.

> The Institute of Trading & Portfolio Management and TradeStation are not responsible for any losses that you incur in your trading account from using any of the information of this presentation.

➤ **Examples of Fundamental Themes Driving Equities Markets & Trade Ideas for Q2**

- **Theme 1 – Buy upside in “Expensive” Bank Stocks near all time highs**
- Capture earnings but get additional catalysts of Dodd Frank / Volcker Rule repeal and lower regulatory announcements
- Go for the investment banks
- Names like Goldman Sachs (GS), Bank of America Merrill Lynch (BAC) are obvious choices on 9-year highs
- Names like Royal Bank of Canada (RY) and Bank of Montreal (BMO), i.e. BMO Capital Markets, are less obvious but could have much more explosive upside.
- Buy 5% OTM monthly calls or look for good risk/reward plays in monthly's / quarterly's i.e. the 5%-10% OTM call spreads that capture earnings and enough time to digest additional regulation commentary and updates from Congress and management.

BMO Option Chain

QUOTES OPTION CHAIN
 BMO Spread Type: Single Exp Date: Fri Jun 16 2017 (M) Strike Int: 1 Exp Int: 1 Str

Bank Of Montreal Last: 76.75 Net Chg: 0.19 Bid: 76.75 Ask: 76.76 High: 77.08 Low: 76.37 Volume: 320,561

CALLS

IMP VOLATILITY	THETA	GAMMA	DELTA	VOLUME	NET CHG	LAST	BID SIZE	ASK SIZE	BID	ASK	STRIKE
21.92%	-0.01	0.03	0.81	0	0.00	7.50	179	209	6.50	7.80	70
14.43%	-0.01	0.07	0.65	0	0.00	2.95	135	58	3.00	3.30	75
13.88%	-0.01	0.06	0.30	3	0.04	0.86	67	177	0.75	1.00	80
22.70%	-0.01	0.03	0.21	0	0.00	0.00	0	100	0.00	1.00	85
24.30%	-0.01	0.02	0.11	0	0.00	0.00	0	87	0.00	0.50	90
29.25%	-0.01	0.01	0.09	0	0.00	0.00	0	85	0.00	0.45	95

- Since earnings are late May, the June 80 strike calls may be an upside play
- Offered at \$1, not a lot of downside and low (not cheap) implied volatility at sub-14
- Should the stock rally 15% to \$88, you will make 7x your money.

> Examples of Fundamental Themes Driving Equities Markets & Trade Ideas for Q2

➤ Theme 2 – Get Downside Exposure to improving Economic conditions in U.S. inner cities.

- The obvious trade would be to look one dimensionally at improving credit quality / credit scores in sub prime
- They will be the beneficiaries but it could be a crowded trade with few catalysts. Think of who will suffer from this short term and who has potentially crowded long positioning from yield hunters of 2015 and 2016 ???
- Food Stamps (SNAP) !!! – Analysts are not aggressively changing numbers to reflect the reality of a big decrease in SNAP participation
- The cracks are already starting to appear...
 - Target Profit Warning (January 2017) – Large decrease from in-store sales versus online
 - Dollar General (DG) & Dollar Tree (DLTR) profit warning (Aug & Dec 2016) due to decreased commodity prices (price war) and decrease in SNAP participation.
- Walmart (WMT), Costco (COST), etc.
- Look for good risk/reward plays in monthly's / quarterly's leaving enough time for potential downgrades from analysts into and after numbers..., i.e. 3-4 month 5%-10% OTM put spreads

WMT Option Chain

WMT Spread Type: Exp Date: Strike Int: Exp Int: Strike Proximity:

Wal-Mart Stores Last: 70.03 Net Chg: -0.06 Bid: 70.03 Ask: 70.04 High: 70.45 Low: 69.71 Volume: 3,592,171

CALLS										PUTS											
TA	GAMMA	DELTA	VOLUME	NET CHG	LAST	BID SIZE	ASK SIZE	BID	ASK	STRIKE	BID	ASK	ASK SIZE	BID SIZE	LAST	NET CHG	VOLUME	DELTA	GAMMA	THETA	IMP VOLATILITY
01	0.02	0.90	0	0.00	12.41	111	230	12.35	13.25	57.5	0.17	0.21	488	43	0.22	0.00	0	-0.05	0.01	-0.01	25.10%
01	0.02	0.87	0	0.00	10.30	501	956	10.10	10.85	60	0.30	0.34	485	51	0.34	-0.01	36	-0.08	0.02	-0.01	23.33%
01	0.03	0.89	0	0.00	7.90	1,044	170	7.80	8.05	62.5	0.52	0.56	104	37	0.56	-0.01	22	-0.14	0.03	-0.01	21.71%
01	0.04	0.81	5	-0.04	5.71	1,209	454	5.60	5.90	65	0.90	0.95	348	21	0.94	-0.02	22	-0.22	0.04	-0.01	20.45%
01	0.06	0.69	0	0.00	3.95	76	727	3.85	3.95	67.5	1.54	1.61	660	16	1.58	-0.06	295	-0.33	0.05	-0.01	19.58%
01	0.07	0.53	47	-0.17	2.30	186	161	2.30	2.38	70	2.55	2.63	606	37	2.57	-0.30	241	-0.47	0.06	-0.01	19.05%
01	0.07	0.36	107	-0.04	1.27	130	149	1.23	1.28	72.5	3.95	4.10	1,221	250	4.10	0.15	21	-0.61	0.06	-0.01	19.20%

- Since earnings are late May, the June 67.5/62.5 Put spread might be a good play
- You could pay \$1.09 for the spread with an upside of \$5 (profit of \$3.91) a payoff of more than 3.5 to 1 per spread, should the stock come off 10.75%
- You also take advantage of the skew as you are buying a lower vol option and selling an option, 2 vols higher
- It makes more sense to do a spread, rather than outright. If you don't get the catalyst in WMT itself but from a competitor you probably get drift to 62.5.
- In this trade we ideally want WMT to have a price drift to 62.5 by buying a spread we hedge ourselves by this NOT happening and WMT drifting lower over competitors.



Build Better Websites FREE
Froala Design Blocks



Start Building



Froala

➤ Examples of Fundamental Themes Driving Equities Markets & Trade Ideas for Q2

- **Theme 3 – Corporation Tax - Get Upside Exposure to SME Bottom Lines Improving and Subsequent B2B Growth Spending**
- SaaS companies that provide SME's with data / intelligence to help them as they grow and who have superior products, market share and brand recognition.
- Look for super “expensive” companies that are trading on extremely high PE multiples because they are re-investing all profits back into gaining market share, i.e. they are not earnings stories - they are revenue stories.
- Good examples include Salesforce (CRM) and similar SaaS companies.
- Or look for aggressive turnaround stories with much lower market cap and who are losing money like Tableau (DATA)
- Higher market cap look for monthly's / quarterly's 5%-10% OTM call spreads or 10% OTM calls as an outright bet.
- Lower market cap look for monthly's / quarterly's that are very OTM and just have an outright directional bet., so at least 10% OTM if not 20% OTM.

DATA Option Chain

QUOTES x OPTION CHAIN x

DATA Spread Type: Single Exp Date: Fri Jan 19 2018 (M) Strike Int: 1 Exp Int: 1

Tableau Software Inc Last: 48.77 Net Chg: -0.06 Bid: 48.76 Ask: 48.78 High: 48.96 Low: 48.43 Volume: 778,3

CALLS

IMP VOLATILITY	THETA	GAMMA	DELTA	VOLUME	NET CHG	LAST	BID SIZE	ASK SIZE	BID	ASK	STRIKE
58.30%	-0.01	0.01	0.82	0	0.00	18.80	163	297	15.40	17.50	35
50.27%	-0.01	0.01	0.75	0	0.00	16.00	137	187	11.90	13.40	40
48.68%	-0.01	0.02	0.66	0	0.00	12.84	52	308	9.30	10.50	45
46.91%	-0.01	0.02	0.57	0	0.00	8.27	46	375	6.80	8.00	50
45.61%	-0.01	0.02	0.48	0	0.00	7.90	83	573	4.70	6.00	55
42.64%	-0.01	0.02	0.38	2	-0.51	3.66	106	469	3.20	4.10	60
42.90%	-0.01	0.02	0.30	0	0.00	4.10	159	521	2.05	3.10	65
42.81%	-0.01	0.02	0.24	2	0.14	1.76	214	537	1.25	2.30	70

- DATA has fallen nearly \$80 from its high (\$129 in the summer of 2015) to current levels.
- In an aggressive turnaround, you want to give yourself time, so Jan 2018 upside calls may be a good play.
- The Jan 60, 65 or 70 calls offer huge upside should the stock retrace even half its losses
- At sub \$4bln Market Cap, DATA may be a target of acquisition by CRM, ORCL or another software company given the amount of M&A in the sector

> The Necessary Approach to Generating High Quality Trade Ideas

