

TUESDAY TRADE IDEA: WE BUY 4 JNJ November 29th 130 calls for \$3.60

Speak Loudly and Carry a Tiny Stick

The market sure can make a lot of noise. At any given time, there are news reports on TV about Brexit, Trump Impeachment, Recession, Inflation, too slow growth, too much growth, too much China trade, and not enough China trade. You name it, there is someone on air, in a magazine, or in the paper complaining about it. And yet take a look at the S&P 500, its sitting at 3000....again. This is why watching financial news is a waste of time.

In the mornings, a guy in my office named Jimmy sends me a list of procured stories that he thinks matter for the day. Generally speaking, he is right. However, it's not like he is pulling up crazy research papers from BAML or Goldman; he is just looking at headlines on Yahoo, CNBC, and Bloomberg. It's a God send because it saves me from having to go to CNBC myself. It's not that browsing there is hard, it's just I do not want to read all the other noise on that site.

I am lucky to have Jimmy send those stories, it's just something nice he does for people he fills paper for, and he happens to include me in his blast he sends. You can have something similar. I know twitter gets a bad rap for being toxic...this is because it is. However, I would encourage you to open up a new 'trading twitter account' and follow fewer than 50 active users (your Aunt Millie does not count). Have it be users that are thought leaders with either no political inclination or, if you must, leaders both conservative and liberal. Additionally, these people HAVE to be involved in markets. That means they work for a bank, are someone like me, or are reporters for the WSJ, FT, Bloomberg, etc. I mean reporters, NOT opinion people, no one from an editorial board. Also stay away from the crazies and conspiracy sites.

Use this feed as a way to source news and manage the information that comes to you. If the news coming to you is something that stirs emotion that is UNRELATED to how it will affect your trading, you are following the wrong account. My hope is that something like this will keep your trading in perspective. As for Financial TV, I do have a great station that will improve your trading: CBS from 10-Noon ET (Let's Make a Deal and the Price is Right) then on to the Game Show Network. See if you can pick out and beat the probability games, it will help your trading.

Mark Sebastian

Overall Market

The S&P 500 is back at 3000, we think it COULD head higher over the next few weeks. With earnings season underway, if all goes well, the market could make a turn higher. So far, earnings have been pretty darn good, especially, in the financials. If earnings stay strong, China stays on the back burner, the Fed continues to ease, and markets STILL do not rally from here, there is some really scary stuff looming that smart money is paying attention to that we are NOT seeing. Thus, I like the S&P to make

another nice leg higher, it currently seems to have some really nice slow momentum, a t least over the last week and a half or so.



Since touching below 2900, the S&P has had two strong days, and a whole lot of slow progression higher. I get bullish when I see a market that makes a move higher and then breaths, then makes another move higher. That is the feel of the last couple of weeks.

Adding to my bullishness is a VIX curve that has completely normalized. The VIX is in contango, but not TOO steep a contango that I am worried we are setting up for a turnaround (although if it gets any wider that might change). The VIX curve is in that sweet spot that says to me "things could be boring here for a few weeks."



Now obviously a bad turn for earnings or some crazy news could turn things upside down for a short period. But all things being equal, I predict a new SPX high by the end of earnings season.

OPTION PIT VOL SIGNAL

SPX: GREEN

VIX: RED

SPX IV: RED

VIX IV: Yellow

CANCER LAWSUITS!!!



I mean could this billboard, despite how serious Mr. Pintas might be, scream any louder, 'I AM CHASING AMBULANCES!!!'? Yet, this type of billboard has cost Johnson and Johnson a massive amount of market cap over the last year. JNJ had lost about 20% of its value because of talcum powder.



First, JNJ ate it because there are accusations that Baby Powder could cause ovarian cancer. I do not know if this is true or not. JNJ says it is not and is defending itself pretty aggressively. Lawyers say it is and are moving to try to class action JNJ.

You can see the 'Baby Drop' that took place in December of last year. Since then, there has been another giant candle relating to earnings, and now a new one from ANOTHER issue with talc. JNJ is recalling talc that had trace amounts of asbestos (obviously a bad thing).

Baby powder has put JNJ on its back a couple of times in the last year. Looking at the chart from the first time, you can see the stock took a HUGE DIVE, touching just above \$120, down about \$30. It then rallies 95% of the way back before giving it up again on earnings and then pushed lower on this latest talc news.

The question is what's next? JNJ is, generally speaking, a great company. Widely held, well liked, and pays a HUGE dividend of \$.95 a quarter. We can almost see the 'div hawks' fly in on this name when the yield gets high enough. With this drop below \$130, one has to wonder if we have another visit from the div hawks in the near future. At \$130 a share, the yield on JNJ is just under 4%, that is REALLY high for a company with a market cap over 100 billion dollars.

I think this is a name that will, at a minimum, see some bottom fishing buyers ahead of its dividend in late November. With the stock losing so much last week, I think we could see a quick bounce back above \$133. Thus, I am strongly bullish JNJ in the near term.

The Vol

What is interesting is, that despite the crazy moves we have seen this year and all the headline risk associated with JNJ, the options are NOT very expensive.



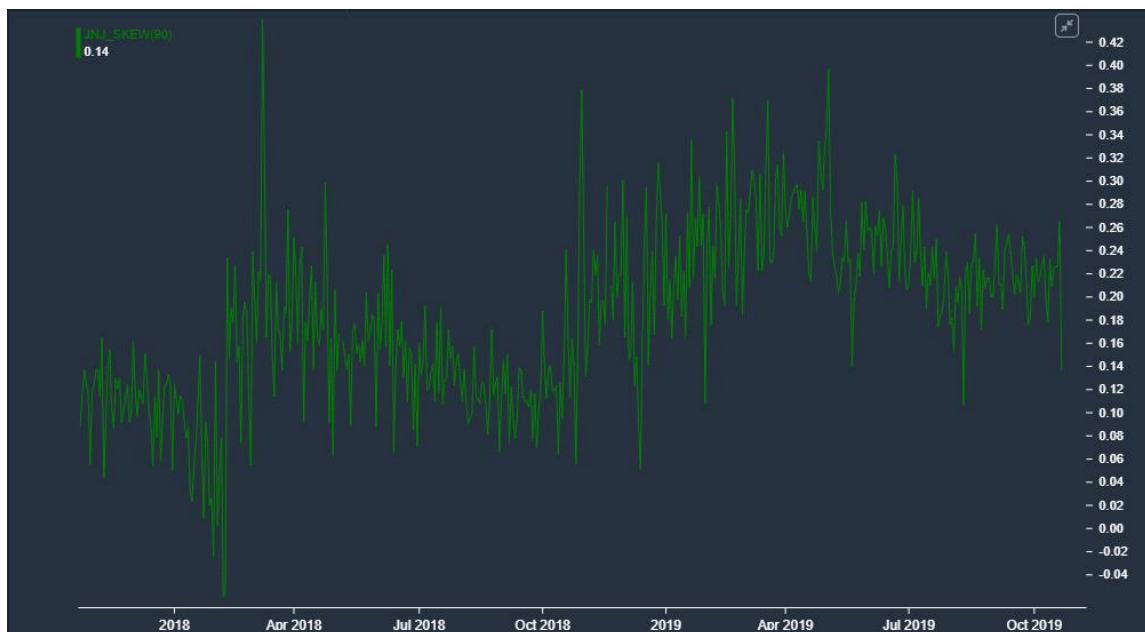
30 day IV in JNJ is only about 19%. That is not even crazy high for JNJ when they are NOT involved in multiple baby powder related lawsuits. Its only in the 27% percentile, meaning that 73% of the time in the last year, IV has been higher than it is right now. This is a stock that lost about 5% last Friday.



To me, this points toward the market thinking that the stock is NOT going to retest lows. It points toward traders selling puts to get into the stock or putting on covered writes with IV 'elevated.' With the stock moving around, and IV low, I am a buyer of JNJ options. I am probably more toward the shorter-term end of the spectrum because as stated above, dividend buyers are going to see that yield, the recent drop, and the price action the last time this company had talc news and push the buy button.

Skew:

With the IV at about 18%, one might expect to see skew somewhat steep, meaning calls are cheap relative to put. However, that is not the case; generally speaking, it appears that calls are expensive or puts are cheap.



Reviewing the IV itself, the answer is actually the latter. There does not appear to be a huge bid for OTM puts in JNJ. Traders seem pretty darn happy selling puts to market makers on this big down turn. All told though, volume has been surprisingly light, from an options perspective, in JNJ since Friday.

The main thing I gather after reviewing the IV's is that I am not really afraid to own anything, and that there isn't anything in particular that looks like a great sale.

Looking at Term Structure, we can see there are CLEARLY some pockets where IV is cheaper than in other places.

Options Chain												
<<	<	Nov15	Nov22(W)	Nov29(W)	Dec20	Jan17'20	Mar20'20	Apr17'20	Jun19'20	Sep18'20	>	>>
		18.65	18.70	17.88	18.83	18.64	19.38	19.45	19.71	20.48		
		-2.80	-2.20	-2.90	-2.30	-1.80	-0.50	0.30	0.30	0.50		

One nice thing about JNJ is that markets are pretty tight, even in the weeklies; meaning week of the 29th. If you have not watched last Friday's chat, Andrew and I walked through owning dividend calls (you can watch it here). As a bonus, the week of the 29th also happens to be a cheap time to own premium relative to the weeks around it.

The JNJ 129 calls on the Nov29 contract cost about \$3.60. I think the stock running back to \$133 will hopefully breathe some life into the skew and these calls will be worth \$5.00-\$5.50 a piece. Thus, I would be a buyer of the JNJ Nov29 129 calls for \$3.60.

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The RISK

Call ownership is pretty cut and dry risk.



One way to reduce the risk is to slowly buy these calls in a larger account. Since this account is buying 4 calls, I might buy 2 on the open and then 2 later in the day, or 2 today and 2 more tomorrow. The point being I am able to reduce my risk by not trying to time the trade.

I am going to get out of these calls if they lose 1/3 of their value. I will begin selling them when they get over \$5.00 with a target average price of \$5.50.

THIS trade's risk rating is a 7 out of 10 for being unhedged, shorter dated, and aggressive.

Have a great day

Mark

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