NKE: We buy 6 Dec6 91 calls pay $1.67 and sell 6 Dec6 96 calls at $.26 paying $1.41 for the spread

To Close or Not To Close

One of the hardest things for even the most experienced traders to understand is when to close a position. I have heard all the rules in the book: let your winners run and cut your losers short, have a certain return both down and up as a goal and take it when you get it, kill it when you reach it. We talk to newer traders about absolute max loss, a level that a position should NEVER touch no matter how bad things gap down or up. There are those that say, don't manage each trade, simply manage the dollars in each trade, then do more good trades than bad. I have heard the opposite, manage really tightly losers and you will have more losers than winners BUT you will make so much on winners that you don't care.

So what is the answer? The truth is there is no answer. However, I can tell you about the best trader I know. His name is Larry. What makes him better than everyone is he is a machine. If a trade is bad he kills it. If trade is making him money, he also kills it. He manages winners, he manages losers. He also has an inane sense on when he is positioned wrong and right.

The former portion, being a machine, every trader can learn. The second portion, having a sense of when a trade is going to be a winner or a loser, is also something traders can learn. While he is the 'Michael Jordan' of traders, you can still learn to 'ball out' by just grasping the fundamentals of volatility really well and shutting off the emotions of trading.

I bring this up because I have trades that I really liked that I have closed, AMTD in particular. I also really liked BABA....but I took the money. JNJ, I was losing and did not get out. The reason: the volatility said not to. I could write a whole letter on trades I want to get back into. I could get back in one of those soon in this letter (almost flipped BABA back on Friday), but for now I want this letter to teach and produce. Regurgitating the same trade over and over, does not teach, it only trades. While it might make money, it's not the way to help you folks get better at this business.

Markets Thoughts:

The S&P is at a new all-time high. The reason:

1. Earnings have been mostly strong

2. There is legitimate optimism on trade (maybe the Chinese are seeing Warren as the front runner and deciding they would rather dance with the devil they know).

3. The Fed seems to be aggressively intervening, momentarily right now.

In the next week, we learn ALOT more about whether we should be at all-time highs. We have the busiest earnings week of the quarter, we have the FOMC meeting, and we have non-farm payrolls on Friday. THERE IS A LOT of information to take in this week.

Thus, with the market at an all-time high, all of this data coming out, AND the VIX settling below 13 for the 1st time in a long time on Friday:

I would not be surprized to see the VIX up all week. Not in a MAJOR way but in a way that says I am worried about Wednesday and Friday. The being said, I would NOT be looking for a nasty move in the VIX curve unless the FOMC takes a huge swing and a miss and in the tone of their statement and/or press conference. The current VIX curve is SCREAMING, the market is going to be calm.

Option Pit Market Indicators:

SPX: Green

VIX: Yellow

SPX IV: Yellow

VIX IV: Green

We see a market that could be up at the end of the week, but is setting up for some chop. We also see room for VIX to go up, although it could fall by Friday. We will write up a full description of our traffic light model next week.

Just Buy It:

Nike has had one of its best years, in a long time, from a sales perspective. The company is making money hand over FIST and absolutely BLEW THE DOORS off of earnings. The company is catching up to LULU on athleasure wear while owning everyone else in actual sportswear. In shoe department, in particular, it seems at any given time they have one rival; but over time that rival is put to pasture. That rival has been Reebok, New Balance, Puma, Converse, Under Armour, and is currently Addidas. None of these 'hot names' seems to be able to supplant Nike at the top of the shoe chain for very long.

Recently Nike announced the return of the Air Force 1. If you think that is not going to be a HUGE seller, then let me remind you that this is a shoe that was SO big it got its own Nelly Song (even Michael Jordan didn't get one about his shoes).

(If you want to hear the song: https://youtu.be/BfzsMQGqrt0)

Take a look at a chart of NKE over the last year:

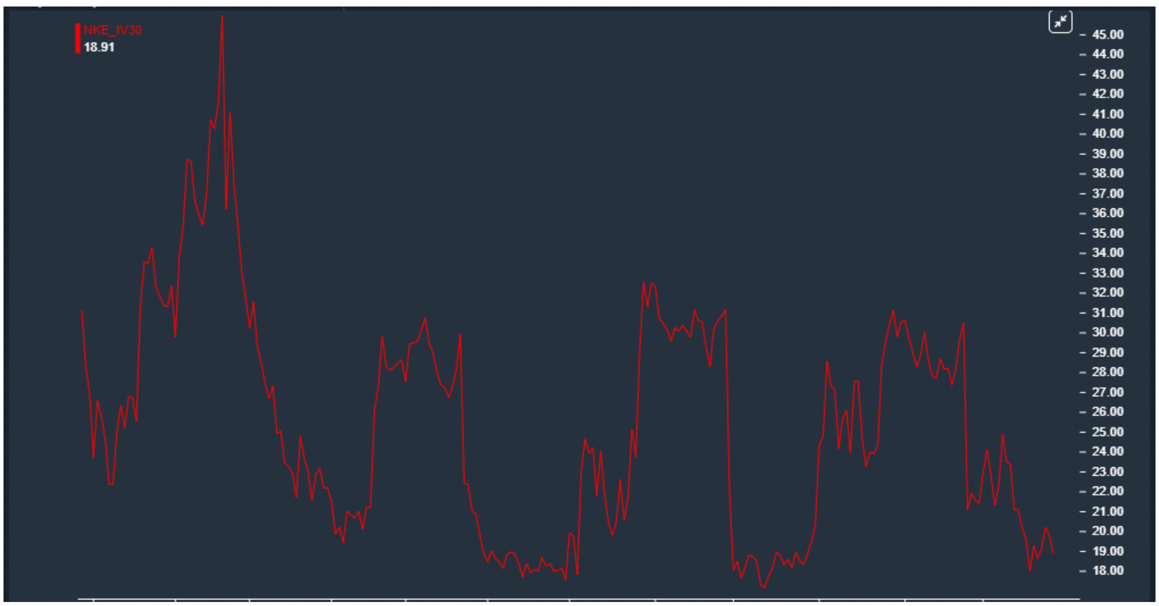
After its last earnings, the stock absolutely SHOT up from the high $80s, gapping up over $90 and running near $100 (it traded over briefly intraday). What stopped this force of a momo stock? Darryl Morey. Without making comment to the situation in Hong Kong, I will say this: It is being proven time and time again that if you say something, and you mean it, and you are famous, DO NOT

APPOLOGIZE PUBLICLY. Nothing good can happen.

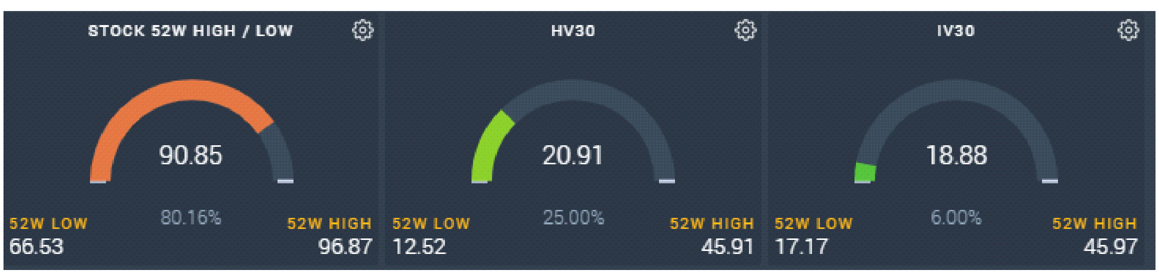
From the NBA's perspective, they wish he had not opened his mouth. They might wish as much that they had kept their own mouths shut after the fact and 'back channeled' the situation with China. Nike, which has a huge relationship with the NBA probably, wishes the same. Heck, the Chinese probably wish they had not made a stink because it made them look soft and weak and petty. NOTHING good came of the whole situation other than maybe some Americans figuring out where Hong Kong is on a map.

Anyway, if you are looking at the stock and asking why has this stock taken a dive the last 6-7 days, the answer is China. From Darryl Morey, to the NBA, to Nike and out of the stock holders pockets. However, if there is one thing I know, it's that news driven stock sell offs do not last when the stock has good fundamentals and a good story. Nike has that. I like the stock to break $100 in the next month or so maybe $110 by the end of the year, as time passes and money feels safe investing in Nike again.

Looking at the movement and the volatility of Nike, and given the land mines Nike is trying to avoid, the premium in the options is shockingly cheap:



The IV is right near a 52 week low. At the same time the stock is actually moving around. The HV is low, but not floor low and is actually running hotter than the cost of options:

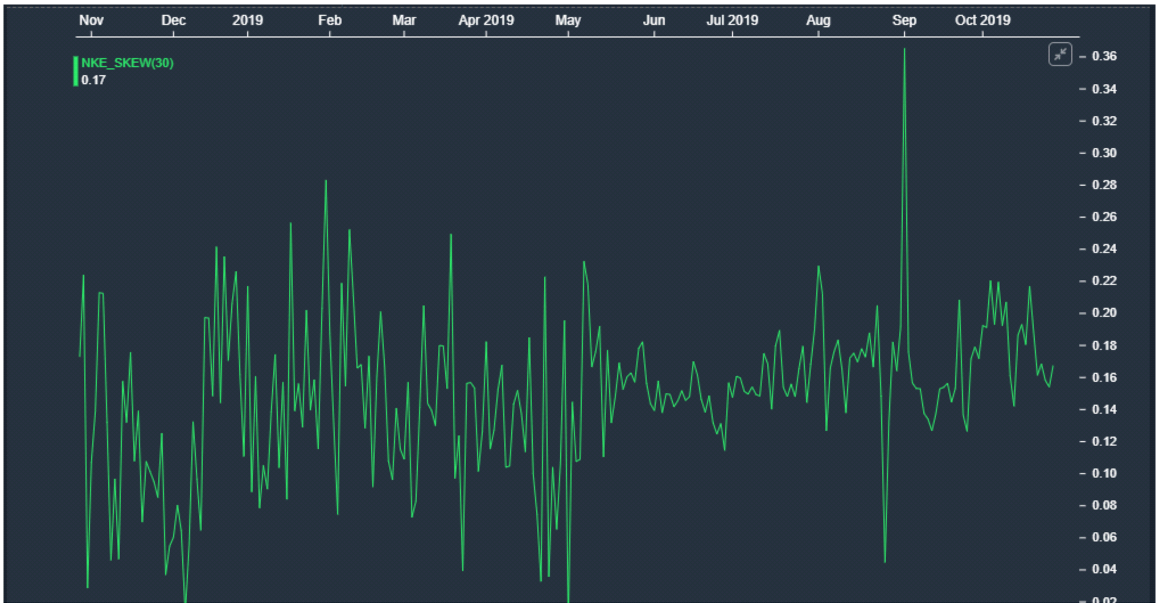


Premium could get cheaper, but not by much. Movement could drop, but if that happens the stock is probably going up NOT down, which helps our initial basis of a trade in NKE. Thus, I want to buy this name and I want to buy options.

Looking at term structure of NKE options, I will say that January is the cheapest month to own that has any real duration to it. If I do not want to have to deal with an earnings cycle, than I could actually look at the December 6th weekly (which might make some sense).

Nov01(W)	Nov08(W)	Nov15	Nov22(W)	Nov29(W)	Dec06(W)	Dec20	Jan17'20	Apr17'20
20.66	19.11	18.97	19.03	18.81	18.58	23.61	22.66	23.78
2.20	0.30	0.10	0.10	-0.10	-0.30	0.50	-0.30	-0.20

The next question is whether there is any way to work the skew curve in my favor:



I am going to say now: puts are somewhat cheap compared to calls, but not crazy. The skew is relatively low because IV is low and the curve is pretty flat. Out of the money calls and puts are about the same IV as ATM with a weak slow of falling IV for calls and vice versa for puts.

For more advanced traders I think I like calendar spreads. Buying Dec6 and selling other contracts in front of it seems to have edge to it. For this letter's purposes we are going to go in a more simple direction (which we will always lean towards) and buy a call spread. We could buy in January, but I think the move higher will be quicker. Thus I do not mind holding December 6 call spreads to take advantage of the rebound in NKE that I see coming

I would be a buyer of 6 NKE Dec6 91 calls for $1.67 and a seller of 6 Dec6 96 calls for $.26; paying $1.41 for the spread.

Payout is about 2 to 1. If this spread drops below $1.00 I have to do something, especially if the upside call gets too cheap. I could also create a butterfly of some sort if I was willing to sell a 96-100 call spread against this. Given the skew, I like that as a trade.

My profit target on this is going to be at least $500.00, at which point I will begin to close spreads. My downside risk is $846.00, but I will trade out of this spread before it reaches that point. I am willing to incur about $300-$400 in losses before I will have to do something to mitigate the exposure of this trade.

Hope you all have a great week, I will see you today at 11:00 AM CT

Mark Sebastian