

The "SectorTrends" Newsletter

Generated on 01/11/2007

This weekly newsletter represents technical outlook and short-term picks found for you by OptionSmart. We use our state-of-the-art mathematical models to identify technical signals and select stock/option picks with better chances to win.

We take into consideration both technical analysis and option mathematics so that you can reduce risk and enhance return of your portfolio.

There are two ways to use this newsletter.

First, you can check the corresponding sector trend before entering any stock or option position to avoid fighting it. Second, you can ride sector trends. Sector rotating play becomes very popular nowadays. Sector movements are more predictable, less volatile and have excellent trading vehicles - exchange traded funds and their options.

We consider the following sectors, industries and Exchange Traded Funds:

- **Consumer Discretionary**
- **Consumer Staples**
- **Energy**
- **Financial**
- **Health Care**
- **Industrial**
- **Materials**
- **Technology**
- **Utilities**
- **Telecommunications**
- **Networking**
- **Software**
- **Biotechnology**
- **Semiconductor**
- **Biotech**

Every module of this newsletter covers a swing type implemented with a stock and one of the most effective and popular option strategies:

- BULLISH SWING: **Buy Stock, Buy Call Option and Open Call/Put Spread.**
- BEARISH SWING: **Sell Short Stock, Buy Put Option and Open Call/Put Spread.**

Each rec consists of basic risk/reward parameters. We even calculate these parameters per \$1 invested to allow you an easy comparison of various picks. We also recommend that you pay attention to the daily and weekly technical signals for each sector.

Please feel free to email to mail to: swings@optionsmart.com if you have questions about this newsletter and option trading in general.

DISCLAIMER: Information for the stock observations was obtained from sources believed to be reliable, but we do not warrant its completeness or accuracy, or warrant any results from the use of the information. Your use of the stock observations is entirely at your own risk and it is your sole responsibility to evaluate the accuracy, completeness and usefulness of the information. You must assess the risk of any trade with your broker and make your own independent decisions regarding any securities mentioned herein.

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Industry & Sector Ratings

Sector	ST Rating	LT Rating	ST Outlook	LT Outlook	ST Strength	LT Strength
Consumer Discretionary	Buy	Buy	Bearish	Bullish	Up	Up
Consumer Staples	Hold	Hold	Bearish	Bearish	Up	Down
Energy	Hold	Hold	Bearish	Bearish	Down	Down
Financial	Hold	Hold	Bearish	Bullish	Up	Up
Health Care	Hold	Hold	Bullish	Bearish	Up	Down
Industrial	Hold	Hold	Bearish	Bullish	Up	Up
Materials	Hold	Hold	Bearish	Bullish	Down	Up
Technology	Buy	Buy	Bullish	Bullish	Up	Up
Utilities	Hold	Hold	Bearish	Bullish	Down	Down
Telecommunications	Hold	Hold	Bearish	Bearish	Down	Down
Networking	Hold	Hold	Bullish	Bullish	Up	Up
Software	Hold	Hold	Bullish	Bearish	Up	Down
Biotechnology	Hold	Hold	Bullish	Bullish	Up	Down
Semiconductor	Hold	Hold	Bearish	Bearish	Up	Down
Biotech HOLDERS	Hold	Hold	Bullish	Bullish	Up	Up

Buy Stocks (Exchange Traded Funds):

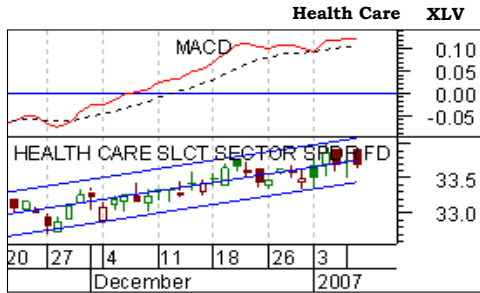
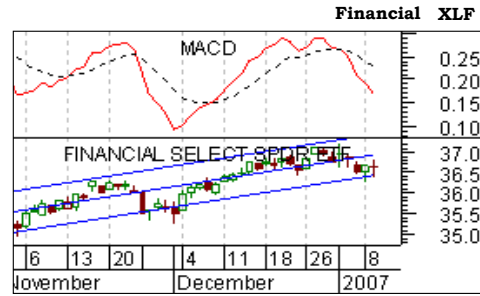
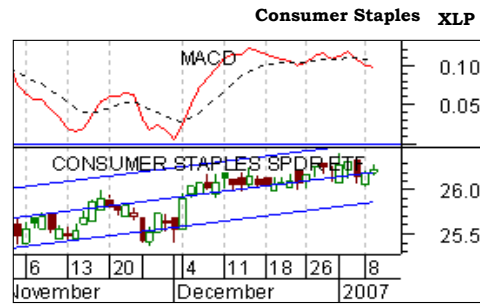
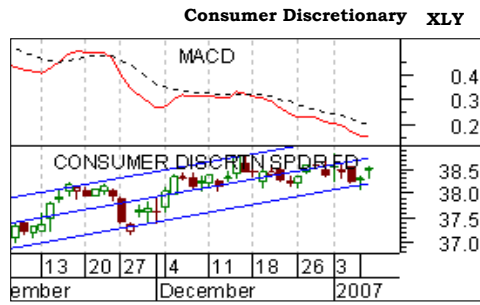
Sector	Symbol	Last	Target	Stop
SPDRs	SPY	141.1	143.1	139.2
Consumer Discretionary	XLY	38.52	38.84	37.72
Technology	XLK	23.60	23.85	22.69

Sell Short Stocks (Exchange Traded Funds):

This module is empty because the picks found had very low probability to be profitable.

Sector	Symbol	Last	Target	Stop

Long-Term Trends for Featured Sectors



BULLISH PLAY: Buy Call Strategy

Symbol	Last	Buy to Open			Last	Target	Stop	1)	2)	Time Value	Sector	Symbol
SPY	141.08	Mar-07	135.0	Call at 7.80	8.30	8.50	4.70	64%	0.26%	2.22	SPDRs	SFBCE
BBY	49.04	Jan-08	45.0	Call at 9.60	9.60	10.20	5.80	62%	0.18%	5.56	Consumer Discretionary	WBYAI
QCOM	37.84	Jan-08	35.00	Call at 8.00	7.60	8.60	4.70	63%	0.21%	4.76	Technology	WLUAG

1) "No Loss" Probability. 2) Expected 1-Day Return.

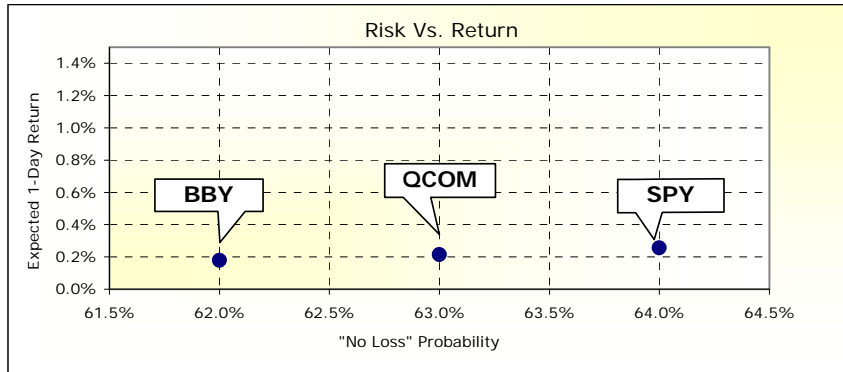


Chart courtesy of StockCharts.com

BULLISH PLAY: Buy Call Strategy

BBY



QCOM



Chart courtesy of StockCharts.com

TOP THREE STOCKS THAT ARE MOVING THE INTERNET SECTOR NOW

Product Name	Symbol	% of Market Value	Short-Term Tech Signals		Sector	Short-Term Industry Trend	Short-Term Sentiment
			MACD	Stochastic Oscillator			
Ebay Inc	EBAY	32.4%	Bearish	Bearish	Consumer, Noncyclical	Bearish	Bullish
Yahoo! Inc.	YHOO	28.4%	Bullish	Overbought	Technology	Bullish	Bearish
Amazon.com, Inc.	AMZN	13.4%	Bearish	Oversold	Consumer, Cyclical	Bearish	Bullish
Overall Sentiment:							Bullish

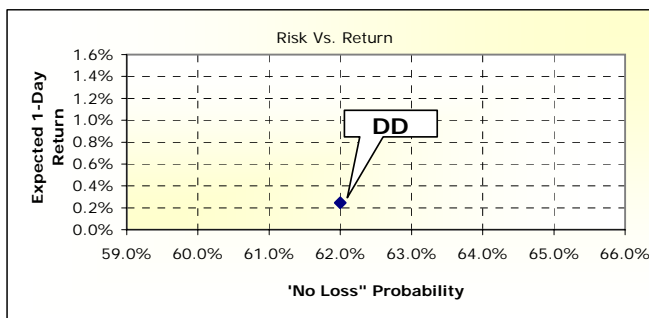


BEARISH PLAY: Buy Put Strategy

This module is empty because the picks found had very low probability to be profitable.

Symbol	Last	Buy to Open	Last	Target	Stop	1)	2)	Time Value	Sector	Symbol
DD	48.38	Apr-07 55.0 Put at 7.00	6.90	7.60	3.90	62%	0.24%	0.08	Materials	DDPK

1) "No Loss" Probability. 2) Expected 1-Day Return.



BULLISH CALL SPREAD STRATEGY

Symbol	Expirat Month	Buy Strike	Sell Strike	Debit	Max Profit	Break-Even	Max Loss	Profit/Loss	Sector	Buy Side Symbol	Sell Side Symbol
SPY	Mar-07	131.0	136.0	4.20	0.80	135.20	4.20	0.19	SPDRs	SFBCA	SFBCF
BBY	Mar-07	40.0	45.0	4.20	0.80	44.20	4.20	0.19	Consumer Discretionary	BBYCH	BBYCI
QCOM	Apr-07	30.0	35.0	4.00	1.00	34.00	4.00	0.25	Technology	AAODF	AAODG

BULLISH PUT SPREAD STRATEGY

Symbol	Expirat Month	Buy Strike	Sell Strike	Credit	Max Profit	Break-Even	Max Loss	Profit/Loss	Sector	Buy Side Symbol	Sell Side Symbol
SPY	Mar-07	131.0	136.0	0.50	0.50	135.50	4.50	0.11	SPDRs	SFBOA	SFBOF
BBY	Mar-07	40.0	45.0	0.72	0.72	44.28	4.28	0.17	Consumer Discretionary	BBYOH	BBYOI
QCOM	Apr-07	30.0	35.0	0.95	0.95	34.05	4.05	0.23	Technology	AAOPF	AAOPG

SPY



BBY



Chart courtesy of StockCharts.com

BULLISH PUT SPREAD STRATEGY

QCOM

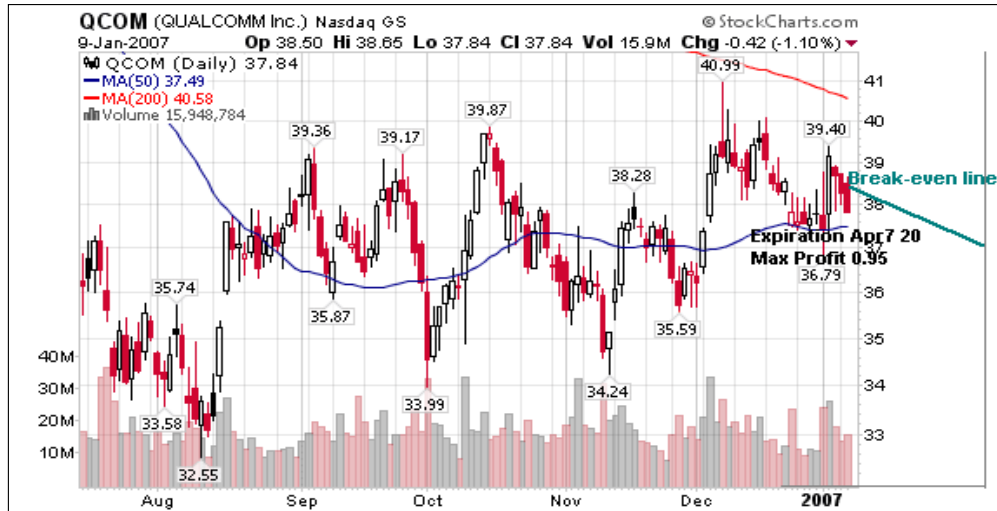


Chart courtesy of StockCharts.com

BEARISH CALL SPREAD STRATEGY

This module is empty because the picks found had very low probability to be profitable.

Symbol	Expirat Month	Buy Strike	Sell Strike	Credit	Max Profit	Break-Even	Max Loss	Profit/Loss	Sector	Buy Side Symbol	Sell Side Symbol
DD	Apr-07	55.00	50.00	1.00	1.00	51.00	4.00	0.25	Materials	DDDK	DDDJ

BEARISH PUT SPREAD STRATEGY

This module is empty because the picks found had very low probability to be profitable.

Symbol	Expirat Month	Buy Strike	Sell Strike	Debit	Max Profit	Break-Even	Max Loss	Profit/Loss	Sector	Buy Side Symbol	Sell Side Symbol

Pros and Cons for Our Bullish Picks

Symbol	Bullish Factors	Bearish Factors
SPY	<ul style="list-style-type: none"> • near-term support at 140, • intermediate-term support at 135-138 , • stoch (daily, weekly) - oversold, • intermediate-term bullish trend. 	<ul style="list-style-type: none"> • short-term bearish trend, • nearest resistance at 142.50, • bearish (daily, weekly) MACD
BBY	<ul style="list-style-type: none"> • near-term support at 48, • intermediate-term support at 45, • low PEG, • stoch (daily, weekly) - oversold, 	<ul style="list-style-type: none"> • near-term resistance at 200-MA, • short-term bearish trend, • bearish trend since Oct-2006, • EPS revisions trend – down,
QCOM	<ul style="list-style-type: none"> • near-term support at 50-MA, • intermediate-term support at 34-35, • high profit and operating margins, • low PEG, • EPS revisions trend – mixed, 	<ul style="list-style-type: none"> • near-term resistance at 200-MA, • short-term bearish trend, • bearish (daily, weekly) MACD,

Pros and Cons for Our Bearish Picks

Symbol	Bullish Factors	Bearish Factors
DD	<ul style="list-style-type: none"> • near-term support at 50-MA, • high dividend yield, • EPS revisions trend – up, 	<ul style="list-style-type: none"> • near-term resistance at 50, • stoch (daily, weekly) – overbought, • bearish (daily, weekly) MACD, • high PEG, P/S, P/B

SHORT GLOSSARY

Buy -	JCPBE	Feb	25	Call	@ 1.05
Position	Symbol	Expiration Month	Strike	Option Type	Recommened Entry Price

Break-even. Point at which gains equal losses. This is the market price that a stock must reach for an option to avoid loss if exercised. For a call, the break-even equals the strike plus the premium paid.

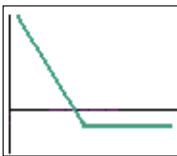
BUY CALL

WHEN TO USE: You are very bullish on the stock. The more bullish you are, the higher the strike should be. No other position gives you so much leveraged advantage with limited downside risk.

PROFIT: increases as stock rises. At expiration, break-even point will be option strike A plus premium paid. For each point above break-even, profit increases by an additional point. **LOSS:** is limited to the premium paid. Maximum loss realized if the stock ends below A. For each point above A, loss decreases by additional point.

RISK: Limited. **REWARD:** Unlimited. **MARGIN:** Not required.

TIME DECAY: This position is a wasting asset. As time passes, value of position erodes toward expiration value. If volatility increases, erosion slows; if volatility decreases, erosion speeds up.

BUY PUT

WHEN TO USE: You are very bearish on stock. The more bearish you are, the more out-of-the-money (lower strike) should be the option you buy. No other position gives you as much leveraged advantage in a falling stock (with limited upside risk).

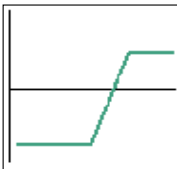
PROFIT: increases as stock falls. At expiration, break-even point will be option exercise price A less premium paid. For each point below break-even, profit increases by additional point.

LOSS: limited to amount paid for option. Maximum loss is realized if the stock ends above option exercise A. For each point below A, loss decreases by additional point.

RISK: Limited. **REWARD:** Unlimited.

TIME DECAY: This position is a wasting asset. As time passes, value of position erodes toward expiration value. If volatility increases, erosion slows; if volatility decreases, erosion speeds up.

BULL SPREAD Call option is bought with a strike price of A and another call option sold with a strike of B, producing a net debit. **OR** Put option is bought with a strike of A and another put sold with a strike of B, producing a net credit.



WHEN TO USE: you think the stock will go up somewhat or at least is a bit more likely to rise than to fall. Good position if you want to be in the stock but are unsure of bullish expectations. This is the most popular bullish strategy.

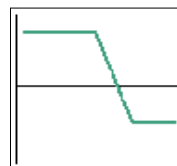
PROFIT: limited, reaching maximum if stock ends at or above the higher strike B at expiration. If call spread used, difference between strikes minus initial debit. If put spread used, net initial credit.

LOSS: maximum loss if stock at expiration is at or below A. If call spread used, maximum loss is net initial debit. If put spread, difference between strikes minus initial credit.

RISK: limited. **REWARD:** limited.

TIME DECAY: if stock is midway between A and B, no time effect. At B, profits increase at fastest rate with time. At A, losses increase at maximum rate with time.

BEAR SPREAD Put option is bought with a strike price of A and another put option sold with a strike of B, producing a net debit. **OR** Call option is bought with a strike of A and another call sold with a strike of B, producing a net credit.



WHEN TO USE: you think the stock will go down somewhat or at least is a bit more likely to fall than to rise. Good position if you want to be in the stock but are unsure of bearish expectations. This is the most popular bearish strategy.

PROFIT: limited, reaching maximum if stock ends at or below the lower strike B at expiration. If put spread used, difference between strikes minus initial debit. If call spread used, net initial credit.

LOSS: maximum, if stock at expiration is at or above A. If put spread used, maximum loss is net initial debit. If call spread, difference between strikes minus initial credit.

RISK: limited. **REWARD:** limited.

TIME DECAY: if the stock is midway between A and B, no time effect. At A, profits increase at fastest rate with time. At B, losses increase at maximum rate with time.

Call Option. The right, but not the obligation, to buy the stock at a predetermined price (also known as the strike) at any moment before the expiration date for a paying a premium.

"No losses" Probability. Once you set a certain minimum level for this parameter, you can reject the picks that go beyond your desired risk level.

Expected Profit is computed using the probability of profit and option prices over the projected probabilities. It is equal to the probability of profit multiplied by the price and sum over all possibilities.

Example.

Outcome 1. Probability = 0.1, Profit= \$6

Outcome 2. Probability = 0.3, Profit= \$4

Outcome 3. Probability = 0.2, Profit= \$1

Outcome 4. Probability = 0.2, Profit= -\$1

Outcome 5. Probability = 0.1, Profit= -\$2

Outcome 6. Probability = 0.1, Profit= -\$3

Expected wins = \$2.00 = $0.1 * \$6 + 0.3 * \$4 + 0.2 * \$1$, Expected losses = $\$0.70 = 0.2 * \$1 + 0.1 * \$2 + 0.1 * \3 .

Expected profit equals the wins minus the losses, or \$1.30. Next, to compute the odds of the trade, the expected wins are divided by the expected losses. In this case, the odds of success equal 2/0.70 or 2.9 to 1.

As a rule, when searching for picks, two of the three variables - odds of success, No losses probability, and expected profit should benefit the trade. Generally speaking, traders struggle for odds higher than 1:1. A ratio of 3:1 tells the trader that he or she is risking \$1.00 for the potential of making \$3.00. In the same way, most traders make every effort to find picks that have positive expected profits.

Expiration Date. The day when an option contract becomes void (the Saturday after the third Friday of the expiration month).

In-the-Money Option. An option that has intrinsic value. A call (put) option is in-the-money if the strike is less (greater) than the current market price of the stock.

Intrinsic Value: The value of an option if it were to expire immediately with the underlying stock at its current price or the amount by which an option is in-the-money. For call options, this is the difference between the stock price and the striking price, if that difference is a positive number, or zero otherwise. For put options it is the difference between the striking price and the stock price, if that difference is positive, and zero otherwise.

"No losses" Probability. Once you set a certain minimum level for this parameter, you can reject the picks that go beyond your desired risk level.

Sector Trends and Strength. We distinguish short-term and intermediate-term time horizons, based on various technical indicators for daily and weekly charts.

Stock Technical Signals are based on various technical indicators for daily and weekly charts. Usually, swing traders check weekly charts to avoid fighting longer-term trends, while investors check daily charts for better timing of entry/exit points.

Stock Strength is also very important in decision-making. Any given stock fluctuates against its sector. For example, imagine that you bet on an upward move of a stock in a rising sector. Are you sure this stock is really strengthening in this sector at the moment? A common approach here is to base a pick on the size of the company or the strength of its brand, which can lead to a major mistake. Almost any stock can outperform its sector for a while. However, if it temporarily underperforms, you will lose.

Clearly, you should bet on a leader. But how can you recognize who will be the leader between your entry and exit points? We can help you. Our charts represent both short-term swings and intermediate-term fluctuations and assist you in selecting the best entry and exit points.

Put Option - the right, but not the obligation, to sell stock at a predetermined price (also known as a strike) at any moment before the expiration date.

Spread. A position with long and short options of the same type on the same underlying stock or index.

Striking Price. The price at which the option holder may buy or sell the underlying security, as defined in the terms of his option contract.

Time Value. Amount by which the current market price of an option exceeds its intrinsic value (the difference between the stock price and the strike). This additional value of an option is due to the volatility of the market and the time remaining until expiration.

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