

STOCKWORLDWEEKLY

THE EXECUTIVE'S SUMMARY | OF THE GLOBAL MARKETS

| | |
|--------------|----------------|
| Dow Jones | 12,442 (-0.6%) |
| S&P 500 | 1,331 (-0.2%) |
| NASDAQ | 2,797 (-0.2%) |
| NYSE | 8,386 (-0.3%) |
| Russell 2000 | 836 (+0.8%) |
| Oil | 100.75 (+0.6%) |
| Gold | 1,537 (+1.5%) |

THIS WEEK'S NEWSLETTER:

MONDAY MARKET MOVEMENT - THE LOW RANGER

Euro drops, Dollar soars, markets stumble

TEMPTING TUESDAY - DIP BUYING OR DIPS BUYING?

Fifth District Manufacturing number drops 16 points

WHICH WAY WEDNESDAY - RUSSELL 815 OR BUST! TEPCO confirms meltdowns in three reactors at Fukushima

THRILL-RIDE THURSDAY - FAKE, FAKE, FAKE

Reports that China will purchase European debt boosts the Euro

TGIF - DOLLAR DONE DIVING OR DESTINED TO DROP?

Fitch cuts rating on Japanese debt

THE WEEK AHEAD

BONUS SECTION: DETAILS OF AN ADVANCED OPTIONS TRADE

The pattern of “when the Dollar drops, the markets pop” continued this week. The chart of the Dow versus UUP (U.S. Dollar proxy) shows the striking inverse correlation between the two. The Dollar spiked up over the weekend of May 21-22 as the downgrade of Grecian debt by Fitch on Friday, May 20, from BB+ to B-plus [four notches below investment grade] sparked a powerful Dollar rally. Gaining over 1.8%, the Dollar climbed from Friday’s low of 74.97 to a high of 76.36 late Sunday, May 22. Although the Dollar sold off hard the rest of the week, it was strong on Monday and the equity markets dropped in response.



The drama continued surrounding the resignation of former International Monetary Fund (IMF) Director Dominique Strauss-Kahn. French Finance Minister Christine Lagarde emerged as a leading candidate to replace him. The finance chiefs of Britain and Germany have both endorsed Lagarde’s candidacy, with German Finance Minister Wolfgang Schaeuble commenting that Lagarde is “outstandingly qualified... appreciated in the entire financial world.” (Germany, Britain back Lagarde to lead IMF)

Lagarde is an outspoken opponent of restructuring Greece’s debt and her appointment would likely mean a turn around at the IMF. At a press conference this month, Lagarde affirmed, “Restructuring, rescheduling [Greek debt is] off the table. A restructuring or a rescheduling, which would constitute a

default situation, what we would call a credit event, are off the table for me.” Thus, while Lagarde is favored by Wall Street, bankers and bondholders, she may not be a great choice for everyone else. (En Garde, Legarde!) Nevertheless, Lagarde’s appointment does not preclude restructuring. Pimco’s Mohamed El-Erian opined, *“The probability of Greece having a debt restructuring and a debt default has gone up after the stunning news (of Strauss-Khan’s arrest).”*

In the Washington Post, Howard Schneider described Strauss-Kahn as *“leading the (IMF) through a fundamental rethinking of its economic theory...a broad summary of the conclusions: State regulation of markets needs to be more extensive; global policies need to create a more even distribution of income; central banks need to do more to prevent lending and asset prices from expanding too fast.”* In an address at George Washington University in early April, Strauss-Kahn had remarked, *“Globalization has delivered a lot...but it also has a dark side, a large and growing chasm between the rich and the poor. Clearly we need a new form of globalization to prevent the ‘invisible hand’ from becoming an ‘invisible fist.’”* The departure of Strauss-Kahn is indeed welcome

news to those who oppose reforming the current model of globalization.

As obstacle to becoming director of the IMF, Lagarde is under investigation for her role in intervening in a legal dispute that ended in a large out-of-court settlement paid to Bernard Tapie, stemming from his having been ripped off by Credit Lyonnais bank. Objections have arisen because the bank’s liabilities have been taken over by the state, i.e. taxpayers. “Judges will take a decision on whether to prosecute Ms Lagarde on June 10 - at a critical moment in her campaign to succeed Strauss-Kahn at the IMF.” *(Not a care in the world, Christine? French minister tipped as next IMF head facing prosecution over financial sleaze)*

Popular anger about the dismal state of world economies, and tensions caused by higher prices in commodities and foodstuffs, have triggered unprecedented political and social instability. Already this year, there have been massive protests (Spain, Portugal, Ireland, Bahrain, Greece, India) multiple revolutions (Tunisia, Egypt) violent and bloody crackdowns by authorities (Syria, Bahrain) large-scale strikes (China, USA) and civil wars (Libya, Yemen). Many countries are reeling in the wake of the global financial crisis and the subsequent unleashing of inflation. Many are struggling with high unemployment rates and very unpopular austerity measures.

A popular theme expressed eloquently by the protestors in Spain with the phrase “We are not anti-system, the system is anti-us,” is that the system is simply not working for the general public any longer. In multiple countries, the plight of the dwindling middle-class is extreme



unemployment, a widening chasm between “haves” and “have-nots,” and a growing perception that the playing field is **tilted and the game is rigged**. Social and political pressures are reaching the boiling point. The frog in the proverbial pot is waking up to the notion that it is being cooked alive and frantically trying to jump out.

In the U.S., persistently high oil prices have put a damper on an already anemic economic recovery. Consumers must drastically cut items from their budgets when oil prices rise above \$105 a barrel. High oil prices decrease the demand for oil and gasoline. But the oil futures market, used to drive up the price of oil, is not subject to normal constraints of supply and demand.

The shenanigans played in the oil futures market distort ordinary price discovery and create a casino where speculators can rake in money at other people’s expense. Knowing how this game is played has enabled us to short oil (USO) profitably this week, but we’d prefer to see the manipulation end. Consumers are being fleeced at the pumps by oil companies and speculators. Manipulation of the oil market has had a very detrimental effect on our economy.

We covered the oil scam in depth on Thursday, and have included an excerpt below from Phil’s article that illustrates the magnitude of the problem.

“(On Thursday, May 26) I put up a trade idea in Member Chat to short oil futures at the \$101.45 line with a stop over \$101.50. If the manipulators want to pretend they want to buy barrels for \$101.45, we are very happy to agree to sell barrels for that price because WE KNOW THEY ARE LYING! How do we know? Because last month, the June NYMEX contract finished with 20,000 contracts (20M barrels) open for delivery. That makes sense because Cushing, OK, where the barrels are delivered, can only handle about 40M barrels, and it is pretty full now. Oil finished out that contract down near \$96 a barrel. How did the oil future traders get it back to \$101.50 in a pre-holiday week, where that \$5 a barrel translates to \$2 a tank from every driver in America? By PRETENDING to be interested in buying - get this - 406 MILLION barrels for July delivery:

| Month Click for chart | Session | | | | | | | | Pr.Day | | Options |
|--|---------|--------|--------|--------|---------------|------|------|-------|--------|-------|--|
| | Open | High | Low | Last | Time | Sett | Chg | Vol | Sett | OpInt | |
| Jul 11 | 101.24 | 101.90 | 100.48 | 101.40 | May 26, 08:54 | - | 0.08 | 47873 | 101.32 | 4E+05 | Call Put |
| Aug 11 | 101.74 | 102.37 | 100.98 | 101.93 | May 26, 08:54 | - | 0.11 | 4363 | 101.82 | 93036 | Call Put |
| Sep 11 | 102.23 | 102.80 | 101.50 | 102.38 | May 26, 08:54 | - | 0.14 | 3240 | 102.24 | 99149 | Call Put |
| Oct 11 | 102.49 | 103.09 | 101.71 | 102.67 | May 26, 08:54 | - | 0.13 | 1203 | 102.54 | 47470 | Call Put |

“It is simply not physically possible for 400M, or even 40M barrels, of oil to actually be delivered to Cushing. I can tell you FOR A FACT that over 90% of those contracts will not only be cancelled before the expiration date in June, but that they will then be rolled over to August, where the CRIMINALS (alleged by the CTFC) at the NYMEX will then FAKE demand for another 400M barrels of oil. That is TEN TIMES actual demand. Do you think that affects prices? Of course it does. It’s a \$2.5 TRILLION Dollar Global Oil Scam, and shame on you if you read this and just think someone else should do something about it. WRITE TO CONGRESS - STOP THIS CRIME!!!” - Phil

Monday Market Movement - The Low Ranger

Stocks traded lower on Monday as turmoil in Europe helped levitate the Dollar. Traders sought out relative safety in the face of increasing uncertainty for the future of the Euro. The five major indexes we track (the Dow, S&P 500, Nasdaq, Russell 2000 and NYSE) all ended sharply lower.

| 5/23/11 | Dow | S&P | NAS | NYSE | RUT |
|----------|--------|-------|-------|-------|-------|
| TODAY | 12,381 | 1,317 | 2,759 | 8,237 | 814 |
| PREVIOUS | 12,512 | 1,333 | 2,803 | 8,358 | 829 |
| % CHANGE | -1.14 | -1.20 | -1.57 | -1.45 | -1.81 |

Greece's debt crisis dominated the news. [Socialist Prime Minister Papandreou](#) maintained his strong stance against proposals to restructure the country's debt, in spite of violent civil unrest and lack of public support. [Polls show 80% of Greeks are unwilling to make any further sacrifices in exchange for bailouts.](#)

As European finance ministers struggled with Greece's debt crisis, Antonis Samaras, head of the main opposition conservative party, forcefully rejected new austerity measures. Earlier this month, he called for a renegotiation of the bailout deal. Echoing the will of the people, Samara refused ["to back new austerity measures designed to tackle the crippling debt crisis."](#) He argued that the measures would cause further recession. *"The government lacks the courage to restart the economy and is not considering a renegotiation. It is repeating the same mistake, and exceeding the limits of the Greek economy and of our people. We remain opposed."* [\(Greek opposition party rejects new austerity plan\)](#)

In Spain, voters dealt an angry rebuke to the ruling Socialist Party in last Sunday's elections. The center-right Popular Party achieved a landslide victory, beating the ruling Socialist Party in every region. Tens of thousands of demonstrators, crowding the Puerta del Sol

plaza in Madrid, expressed their profound dissatisfaction with Spain's political system and the woeful state of the economy. They see little difference between the two dominant parties, neither one is responsive to their needs. [\(Spain's socialists swept from power in elections\)](#)

Not surprisingly, European stocks fell, and exchanges closed near their lows. Jeremy Batstone-Carr, research director at Charles Stanley, proclaimed, *"It was a bad weekend for the eurozone and in particular for those politicians and financial authorities trying desperately to keep the euro project together."* [\(European debt crisis shakes markets again\)](#)

Chinese stocks also took a beating. The Shanghai Composite lost 2.9% after the release of a preliminary report showing that China's manufacturing activity slowed to a 10 month low in May. Recent efforts by the Chinese government to rein in high inflation, by raising interest rates and restricting lending, have been paying off. Vice Premier Wang Quishan has repeatedly stated that the government's top priority is to contain inflation. [\(China Manufacturing May Slow on Tightening Steps, PMI Shows\)](#)

“So how screwed up is the rest of the World? Remember, the rest of the world competes with the US, which has set the bar at "very screwed up." We thought we were guaranteed a spot in the finals, but already we've been leapfrogged by Ireland, Spain, Greece AND Portugal in Europe, as well as Egypt, Tunisia, Libya, etc. And if you think things are great in China, you are just not paying attention.” - Phil

Tempting Tuesday - Dip Buying or Dips Buying?



Stocks continued in a downdraft. The Dollar opened at a high of 76.2 but sagged to 75.8 - likely mitigating losses in equities.

| 5/24/11 | Dow | S&P | NAS | NYSE | RUT |
|----------|--------|-------|-------|-------|-------|
| TODAY | 12,356 | 1,316 | 2,746 | 8,252 | 810 |
| PREVIOUS | 12,381 | 1,317 | 2,759 | 8,237 | 814 |
| % CHANGE | -0.20 | -0.08 | -0.47 | +0.18 | -0.49 |

The Richmond Fed released May's Fifth District Survey of Manufacturing Activity which showed the seasonally adjusted composite index falling sixteen points to negative 6 from April's reading of 10. (Readings above 0 indicate growth.)

J.M. Smucker Company, the #1 U.S. maker of packaged coffee, announced its decision to hike prices it charges to merchants by 11%. The company cited rising costs of green coffee beans as the reason. This is the second time Smucker Co. raised coffee prices this year; it increased prices 10% in February.

Adding to the drama unfolding in Greece, Moody's released a statement: *"The longer the current state of uncertainty affecting Greece persists, the greater the temptation on the part of both the Greek and the euro area authorities to try to undertake some form of debt restructuring."* Alastair Wilson, a chief credit officer for Moody's told Reuters *"a Greek default would be highly destabilizing and would have implications for the creditworthiness of issuers across Europe...there could potentially be multi-notch downgrades to the weakest sovereigns."* (Greek default would hit others in euro zone)

The result of widespread uncertainty throughout the European Union, accompanied by civil unrest in Greece and Spain (photo below) is that it makes the U.S. Dollar look rather solid by comparison. That helps the Dollar. And as Phil wrote, *"It continues to be all about the Dollar, and the Dollar is all about the Euro and the Yen, so the simple question to ask yourself is: Are Europe and Japan looking like better investments now than they were 3 months ago? Six months ago? Twelve months ago? No, no way. Is America a worse-looking investment than it was 3 months ago? Six months ago? Twelve months ago? Maybe a little but, generally, there is nothing new to be worried about - we're the same freakin' mess we were in last year."*



(Protestors in Madrid Photo Credit: <http://fotograccion.org> via Wikipedia)

Which Way Wednesday - Russell 815 or Bust!

The [April Durable Goods Advance Report](#) came in showing new orders for manufactured goods down by 3.6%. Goldman Sachs announced it was cutting its forecast for U.S. Q2 GDP growth to 3% from its previous estimate of 3.5%, but the markets shrugged off bad news and responded to the downward move of the Dollar. The Dollar dropped 0.4%, from a high of 76.2 early in the day, to a low of 75.9 at the close. Dollar weakness gave the markets a nice upward move for the day.

| 5/25/11 | Dow | S&P | NAS | NYSE | RUT |
|----------|--------|-------|-------|-------|-------|
| TODAY | 12,395 | 1,320 | 2,761 | 8,295 | 821 |
| PREVIOUS | 12,356 | 1,316 | 2,746 | 8,252 | 810 |
| % CHANGE | +0.31 | +0.30 | +0.54 | +0.52 | +1.36 |

In Athens, Maria Damanaki, The European Union's Commissioner for Maritime Affairs and Fisheries was quoted by the Athens News Agency as saying, *"I am forced to speak openly, either we agree with our lenders to a programme of tough sacrifices...or we return to the Drachma."*

Karl Denninger had a simple reply: "Do it." He argued that Greece would be no worse off returning to the Drachma than it would be staying in the EU, and it would most likely end up in a better position. *"Here's what happens if [Greece returns to the Drachma]: The Drachma would be devalued against the Euro. Sovereign debt denominated in the Euro would be recast into Drachmas, instantly haircutting them by whatever the devaluation is...therein lies the solution for Greece - its external debt which has become impossible to pay suddenly becomes payable, as it's cut by 20, 30, even 50% overnight. This is a forced restructuring crammed down the creditor's throats... What I actually expect to happen is that Greece will "agree" to do more "tough*

“I’ve been saying all week - if we rally off a declining dollar then I won’t like it. That’s all this is, and I do not like it!” - Phil

things" and fail, there will be more and more threats, and eventually the Greek people will force the issue by simply refusing to work, either going on strike or worse, initiating a revolution. Then the tough choice will be taken because it will be either that or the government literally dies." ([Here Come The Threats \(Greece\)](#))

TEPCO announced that the Fukushima nuclear reactor complex suffered a triple meltdown in the aftermath of the March 11 earthquake and tsunami. Computer simulations indicate that holes had formed in the bottoms of the containment chambers due to molten fuel burning its way through. Attempts to control the reactors by injecting thousands of tons of water have created a situation where there is now a massive amount of water that needs to be decontaminated before it leaks into the environment. Initial estimates of the cost of this effort, by itself, run over \$500 million. ([Fukushima faces 'Massive Problem' From Radioactive Water](#))

“While Wednesday’s gains may have seemed meaningful, they were nothing more than EXPECTED bounces off our resistance levels - bounces we had predicted back in April, at the same time we predicted the 5% pullback in the first place. That kept us from buying the dips on Wednesday. Consolidating near the bottom of our FIRST 5% drop is no reason to go on a buying spree.” - Phil

Thrill-Ride Thursday - Fake, Fake, Fake



A report that [China and other Asian investors are interested in buying Portuguese bailout bonds](#) boosted the Euro against the Dollar early Thursday. Those gains were pared later after the President of the Eurogroup of finance ministers said that [Greece won't reach its 2011 budget deficit goal](#), meaning that the IMF may withhold additional bailout funds.

| 5/26/11 | Dow | S&P | NAS | NYSE | RUT |
|----------|--------|-------|-------|-------|-------|
| TODAY | 12,403 | 1,326 | 2,783 | 8,342 | 831 |
| PREVIOUS | 12,395 | 1,320 | 2,761 | 8,295 | 821 |
| % CHANGE | +0.06 | +0.45 | +0.80 | +0.56 | +1.22 |

Microsoft (MSFT) rose on Thursday in the aftermath of comments by hedge fund manager David Einhorn calling for Steve Ballmer to step down as CEO. Einhorn, known for his prescient warnings about Lehman Brothers before it collapsed, declared, "his continued presence is the biggest overhang on Microsoft stock." Microsoft has been strongly challenged by Apple and IBM, and is playing catch-up in technologies such as the search and mobile markets. ([Microsoft CEO Ballmer Still Has Board's Support: Director](#))

Thursday's Q1 GDP estimate was disappointing (1.8% versus 2.2% expected). [Higher than expected unemployment numbers came in at 424,000](#), an increase of 10,000 from the previous week's revised figure of 414,000. *"The usual 424,000 people lost their jobs last week, and that's not actually good as we're heading into what should be a busy holiday weekend where you would think that hotels, restaurants, airlines, retail, etc. would WANT to have employees on hand."* (Phil) This news, combined with dismal reports from the housing and manufacturing sector, may have boosted expectations that QE3 will happen, regardless

of the Fed's current position on ending quantitative easing with the expiration of QE2.

“*The Dollar is being driven down by QE3 talk, of course, because the news is SO BAD, it's GOOD.*” - Phil

Unrest in the Middle East and North Africa (MENA) continued percolating this week. Yemen's President Ali Abdulla Saleh reneged on his earlier agreement to voluntarily leave office in the face of popular opposition to his regime, and renewed protests escalated into street battles leaving dozens dead. The Yemeni air force dropped bombs on armed tribesmen after the tribesmen defeated forces loyal to Saleh's regime and seized a military camp located about 100km from the capital. Considering the involvement of armed insurrectionists, military formations and air strikes, this conflict has now escalated to a civil war in all but name. ([Yemen heads toward civil war as Saleh escalates fight with major tribal leader](#))

Syria is also struggling with massive civil unrest, which al-Assad's regime is violently suppressing. "The 10-week protests in Syria have evolved from a disparate movement demanding reforms to a resilient uprising that is now seeking President Bashar Assad's ouster." Syrian security forces fired live ammunition at hundreds of protestors marching in a nighttime demonstration in the southern city of Deraa, which has been the scene of repeated acts of brutality recently, as al-Assad has attempted to maintain order. Protestors have been opting for a strategy of nighttime demonstrations and candlelight vigils, when the security forces have thinned out. ([Syria Security Forces Fire On Protest](#))

TGIF - Dollar Done Diving or Destined to Drop?

Equities were up on Friday, as the Dollar dropped about 0.5% during the stock market's trading hours. The National Association of Realtors reported that its April Pending Home Sales Index dropped to 81.9 in April, down from the revised March reading of 92.6. This is down 11.6% for the month, and down 26.5% year-over-year. The U.S. Department of Commerce released the [Personal Income and Outlays report for April](#), showing that personal income was up 0.4%, but that gain was negated by higher food and energy prices.

| 5/27/11 | Dow | S&P | NAS | NYSE | RUT |
|----------|--------|-------|-------|-------|-------|
| TODAY | 12,442 | 1,331 | 2,797 | 8,386 | 836 |
| PREVIOUS | 12,403 | 1,326 | 2,783 | 8,342 | 831 |
| % CHANGE | +0.31 | +0.37 | +0.50 | +0.52 | +0.60 |

In other news, Russia abandoned its former ally Colonel Gaddafi and offered to mediate a deal for the Libyan leader to leave the country he has ruled for over 40 years. President Barack Obama and Russian President Dmitry Medvedev discussed the crisis in Libya on the sidelines of [this week's G-8 summit meeting in France](#). Medvedev joined with NATO in calling for Gaddafi to give up power. He said that Moscow would not offer him shelter, although other countries might. ([U.S. backs Russia role in Libya Crisis: White House](#))

Ratings agency Fitch cut its outlook on Japanese debt, warning that the vast cost of rebuilding after the massive earthquake and tsunami of March 11, combined with unknown costs for the cleanup of the nuclear disaster, will strain Japan's already shaky finances. Fitch cut its outlook to negative from stable and affirmed its AA- local currency rating. Responding to the news, the Japanese government offered assurances that it would continue trying bring its debt under control.

“This week’s action is fake, Fake, FAKE. We are waiting for the pump-job today to run it’s course and, as long as we remain below our 2.5% lines, we’ll be adding shorts into the long weekend because we think 75 will hold on the dollar, and then the Dollar will have nowhere to go but up. Speaking of UUP, we like playing it long again this morning. The Jan \$20 calls are only \$1.85 (now \$1.74), which is very little premium with UUP at \$21.62 (now \$21.44). If pressed, we can sell short calls against the calls, but UUP was at \$23.40 in January with the Dollar at 81, so that would be perhaps a 50% gain in the UUP calls if the Dollar goes up 7.5%. We’ll be very happy to take \$2.20 (20% gain) and run on a good pop.” - Phil

Japan is struggling with a public debt that is over twice the size of its GDP, the highest debt-to-GDP ratio in the industrialized world. The cost of the recent disasters is certain to add to its enormous debt. ([Fitch cuts Japan credit rating outlook to negative](#))

On Wednesday, May 5, Phil set our [new watch levels](#), based on Fibonacci lines calculated using the recent consolidation and adjusting for the Dollar. (See chart on page 9) These levels have been very useful.

The markets traded in our “Must Hold” and 2.5% ranges all week, although the NYSE and the Russell 2000 briefly failed the ‘Must Hold’ levels before quickly regaining them.

While the sharp rise in the Dollar on Monday smacked the stock market down, the Dollar proceeded to lose all its gains and more.

Equities finished the week with only minor losses. Explaining the lackluster performance of the Dollar, Royo Wolverson, in TIME magazine online, concluded: "Amid its massive bond-buying program, a fiery debt debate in Washington, and a declining dollar, people simply don't trust the Fed. And Americans aren't the only ones. The disappointing first quarter U.S. growth numbers Thursday were followed by a sell-off of U.S. dollars. So even as all hell broke loose in the eurozone over a

potential Greek default, the euro made gains against the dollar." (Is the U.S. Economy Worse Off than Europe?)

“We are having a good old time playing this volatile market which is actually doing a fantastic job of obeying our 5% rule.” - Phil

Friday's Levels

| 5/27/11 | Dow | S&P | NAS | NYSE | Russell |
|-------------|-------|------|------|------|---------|
| FRIDAY | 12442 | 1331 | 2797 | 8386 | 836 |
| 5% LEVEL | 12801 | 1365 | 2877 | 8694 | 856 |
| 4% LEVEL | 12688 | 1352 | 2850 | 8611 | 848 |
| 2.5% LEVEL | 12505 | 1333 | 2808 | 8487 | 835 |
| 1.25% LEVEL | 12353 | 1317 | 2774 | 8384 | 825 |
| MUST HOLD | 12200 | 1300 | 2740 | 8280 | 815 |



The Week Ahead

Michael Hudson, President of The Institute for the Study of Long-Term Economic Trends, a Wall Street Financial Analyst, Research Professor of Economics at the University of Missouri, and distinguished author, has written about the financial turmoil in Europe in his recent, illuminating article, [“EU: Politics Financialized, Economies Privatized.”](#) He discusses Iceland’s rejection of “financial bullying,” and asks if this is the model that should be followed by Greece and Ireland. Below is an excerpt from his work:

“At issue from Europe’s vantage point - at least that of its bankers - is a broad principle: Governments should run their economies on behalf of banks and bondholders. They should bail out at least the senior creditors of banks that fail (that is, the big institutional investors and gamblers) and pay these debts and public debts by selling off enterprises, shifting the tax burden onto labor. To balance their budgets they are to cut back spending programs, lower public employment and wages, and charge more for public services, from medical care to education.

[...]

“The problem is that privatization and regressive tax shifts raise the cost of living and doing business. This makes economies less competitive, and hence even less able to pay debts that are accruing interest, leading toward a larger ultimate default.

“The textbook financial response of turning the economy into a set of tollbooths to sell off is predatory. Third World countries demonstrated its destructive consequences from the 1970s onward under IMF austerity planning. Europe is now repeating the same shrinkage.”

“*Third World countries from the 1960s through 1990s were told to devalue in order to reduce labor’s purchasing power and hence imports of food, fuel and other consumer goods. But Eurozone members are locked into the euro. This leaves only the option of “internal devaluation” - lowering wage rates as an alternative to scaling back payments to creditors atop Europe’s economic pyramid.*” - Michael Hudson

[...]

“What ‘helping Greece remain solvent’ means in practice is to help it avoid taxing wealth (the rich aren’t paying) and help it roll back wages while obliging labor to pay more in taxes while the government (i.e. ‘taxpayers,’ a.k.a. workers) sells off public land and enterprises to bail out foreign banks and bondholders while slashing its social spending, industrial subsidies and public infrastructure investment.

“One Greek friend in my age bracket has said that his private pension (from a computing company) was slashed by the government. When his son went to collect his unemployment check, it was cut in half, on the ground that his parents allegedly had the money to support them. The price of the house they bought a few years ago has plunged. They tell me that they are no more eager to remain part of the Eurozone than the Icelandic voters showed themselves last month.

“The strikes continue. Anger is rising. When incoming IMF head Christine Lagarde was French trade minister, she suggested that: ‘France had to revamp its labor code. Labor unions and fellow ministers balked,

and Ms. Lagarde backtracked, saying she had expressed a personal opinion.’ This opinion is about to become official policy - from the IMF that was acting as ‘good cop’ to the ECB’s ‘bad cop.’

“I suppose that all that really is needed is for people to understand just what dynamics are at work that make these attempts to pay in vain. The creditors know that the game is up. All they can do is take as much as they can, as long as they can, pay themselves bonuses that are ‘free’ from recapture by public prosecutors, and run to their offshore banking centers.” (This article is an excerpt from Professor Hudson’s upcoming book, “Debts that Can’t be Paid, Won’t Be,” to be published later this year.)

We are paying close attention to the events in Europe. If the European debt crisis deteriorates to the point where investors have serious concerns about the future stability or even viability of the European Union, then the Euro will become less attractive as a reserve currency. The

Inside Member’s Chat:

“Selling C 2013 \$30 puts for \$2.10 is a net \$27.90 entry with (according to TOS) just \$3 in net margin. So that’s 70% in 18 months if C can hold \$30.” - Phil

ramifications of the breakup of the European Union would be enormous. We believe it is currently unlikely that the situation will disintegrate so extensively. However, the more concerns investors have about the Euro, the better the Dollar looks, and as Phil has repeatedly said, “It’s all about the Dollar.”

We have a trade idea this week from our resident pharmaceutical expert Pharmboy:

“Savient Pharmaceuticals (SVNT) is specialty biopharmaceutical company that focuses on developing KRYSTEXXA, a biologic PEGylated uricase used in the treatment of chronic gout in patients refractory to conventional therapy. Savient also sells and distributes branded and generic versions of oxandrolone, an anabolic steroid used to promote weight gain. It sells its products directly to drug wholesalers. There are several competitors in this field, and enough patients to go around.

“I like buying SVNT at the current price [\$8.18] and selling a December \$8 call and put for \$2.30 or better.” Pharmboy sells one call and one put per 100 shares of stock, and takes small, partial positions.



(Protestors in Athens Photo Credit: “linmtheu” via Wikipedia)

Bonus Section: Details of an advanced options trade

Netflix (NFLX) was the subject of a lengthy discussion in Member's Chat on Saturday, May 28. The trades that follow are complicated options strategies but serve to illustrate some of activity that goes on during the day in Member's Chat.

Phil began on Tuesday noting "NFLX seemed to be settling into a range between \$225 and \$250, but then it got a "Facebook pop" as someone floated a rumor on 'Fly on the Wall.'" The "rumor" was reported by [Bloomberg](#) - Netflix and Facebook were discussing ways to integrate social-networking tools.



Phil continued: "This is idiotic. Is Facebook now the new China, where companies can get 5% pops on hints they may do business there? The last time NFLX got a big pop was when Whitney Tilson abandoned his NFLX short position. That sent the stock from \$220 to \$247 in mid-February, but it was back to \$189 after the Japan quake. The moves have little to do with NFLX itself, but it gives you an idea of what can happen to the stock in a weak market (down 25%). It was already at \$200 (down 20%) before Japan's natural disaster.

"As with many short call plays we take, the stock may go higher but we figure a 10% pop over the top of the prior range

will eventually give us a retest when the top of the old range (\$250) is tested. Our first trade on NFLX was from Tuesday"...As follows:

“NFLX/Ethan - It's very hard to buy puts on MoMo stocks where you pay the premium, so how about SELLING premium like this: Buying 3 Sept \$295 calls at \$8.40 and selling 4 June \$250 calls for \$8.40, which yields a net \$840 credit. That's about the same as going short one call, but it's a lot easier to adjust as the 4 June \$250s can be rolled (bought back and exchanged for different calls) to July \$265s (now \$7.50) and probably Aug \$290s, and then Sept \$305s and, in between, you can just add one long call to fix your delta if NFLX breaks over \$250. If it finishes below \$250 at June expiration, anything left on your long position is a bonus over the \$850 you already have in your pocket.”

"On Wednesday, NFLX went up more (triggering the 4th long call in the above trade). As a new play, we went with:

“NFLX/RDN - Selling NFLX calls is always fun. You can sell 5 June \$255 calls for \$9.70 (\$4,850) and buy 3 Sept \$275 calls at \$17.20 (\$5,160) for net \$310 on the spread. If NFLX goes over \$260, you must add another call and, over \$265, you must add another call and you can stop them back out below. That should keep you from getting burned on a move up.”

“Notice the extra \$10 move up let us drop the contingency of adding a full cover but we also tightened the spread from \$45 to just \$20. No change in attitude Thursday as NFLX topped out at \$265 and I put up a new trade idea but really the same trade idea as Wednesday with \$10 more cushion and now, no contingency. We’re REALLY starting to doubt this move has legs:

“NFLX/Etrad - I don’t think they are worth \$150, let alone \$250 so any plan to short them looks good to me. Yesterday’s spread is “in trouble” at the moment but that means you can take it at a higher level like selling 5 June \$265s for \$8.60 (\$4,300) against 3 Sept \$85s at \$17 (\$5,100) so it’s about the same trade at net \$800 so not quite as good as ours but \$10 more likely to work is the trade-off.”

“It’s obviously still a good idea to cover as the stock breaks higher - that is ALWAYS true of ratio backspreads, but on Wednesday I felt we needed to PLAN to do that, while on Thursday (with \$10 more cushion above where we think it should come back) it’s more of a contingency, and by Friday, I didn’t even mention it as it seems so unlikely (and we have a tighter spread, so less dangerous).

“Because \$250 was a good resistance line, we had all day Tuesday and Wednesday morning to catch that move over \$250, on the break over \$250, the Sept \$295 calls jumped to \$10.50 so it cost another \$1,050 to up the coverage to 4/4 on the first trade, but we had an \$840 credit so now it’s a fully covered trade at net \$210. Did it fix the delta as planned? Well, now we have 4 Sept \$295 calls at \$13.60 with a delta of .36 (\$5,440) and the 4 June \$250 calls are \$17.90 with a .76 delta (\$7,160) so now \$1720 and we’re down \$1,930.

“Should we panic? Not really because NFLX is at \$264.50 so \$14.50 is the “right price” and that means there’s \$1,360 of our unrealized loss right there. As a roll, the July \$265 calls are \$14.40 so we expect to eventually get a near-even roll to there and, you could play this aggressively by taking the \$5,440 off the table on the long calls (selling into the excitement). How much did we pay for those long calls? \$210 out of pocket. That then leaves us with \$5,230 in our pocket and - as we do in the \$25KP, we have the “problem” of the short calls to wear down over time.

“So the aggressive move is to go naked and do the roll now, take the \$3.50 hit on the 4 rolls (\$1,400) and that leaves us short 4 naked July \$265 calls for a credit of \$3,830 or \$9.57 per caller (all premium, which means they don’t get their \$9.47 (which is in our pockets) until NFLX is at \$274.57). Looking ahead, the September \$295 calls are \$13.60 and I’m pretty sure we’d be happy to DD on that roll so we’re not really worried until the July \$265s are a 2x roll to the Sept \$295s - other than that, we can patiently wait for reality to catch up to NFLX.

“Staying in the spread, you can still do the roll and spend \$1,200 to knock out \$6,000 of margin requirement if you feel the need but I’d just keep an eye on the roll and not let it get too expensive, keeping in mind you lose .40 x 400 (\$160) for each dollar NFLX goes up anyway (from the delta differential).

“Also, once you mentally commit to a 2x roll in September, the question becomes, why wait? In a more aggressive posture, you can roll the 4 June \$250 callers at \$17.90 to 8 June \$265 callers at \$8.60. That’s \$280 out of pocket and we’ve shoved the caller to 100% premium already and NFLX needs \$273.60 in 20 days just for the caller to get

all of his money back (and that money is in our pockets otherwise). Those 8 June \$265s can be rolled to 8 July \$280s (now \$8.20) and those to 8 Sept \$315 (now \$8.30) so NFLX has to get over \$320 (+30%) before we're in trouble.

“By the way, always keep in mind that if NFLX pops \$265 and you have the 8 short calls, there's nothing stopping you from slapping on something like 8 next week \$265 calls (\$4.20) as a momentum play. Those are going to have a better delta and if NFLX moves up to \$275, you'll keep pace with the callers while having the additional benefit of being able to take more profits off the table once the music stops. If you take them off on a pullback to \$273 (20% of the run) and then they go over \$275 - what do you do? Just buy the \$275 weeklies and DO IT AGAIN. In the very least, you are collecting money to pay for rolling the callers up to a higher strike.

“The Wednesday spread triggered the additional long on Thursday morning at \$19.50 (\$1,950), which raised the net to \$2,260 on a 4/5 spread. 4 Sept \$275s are now \$21 (\$8,400) and the 5 June \$255s are \$14.40 (\$7,200) so this trade is down to a \$1,200 credit, down \$1,060 but the callers still have \$2,500 in premium so not even worth worrying about at this stage. Keep in mind that's WITH the stock moving \$10 against you! The same aggressive strategy could be applied here as well as TAKE THE MONEY AND RUN is a well-known, ancient expression for good reason....

“Thursday's trade is actually still playable - we haven't really moved off those prices but, if you are going to go for it - be prepared for a wild ride!

“The shorter answer (maybe I should have led with that!) is that we want to keep the callers in as much premium as we can for as long as we can in the shortest time-periods (Theta) that we can. If you only enter these spreads in amounts where you can comfortably roll to 2x and 4x down the road, you can usually give yourself over 33% of headroom and if you couple that with some shorter-term call buying to cover momentum moves higher - you can fund additional rolls along the way and stay out of trouble (unless you get a huge pre-market spike like GMCR - then you are screwed!).

“And yes, we are adding the long calls as covers so we stop them out even at all times or, you can be brave and just take the money and run on the additional call(s) if you don't want to risk going fully naked.”

Next Week's Economic Calendar

| Monday 30 | Tuesday 31 | Wednesday 1 | Thursday 2 | Friday 3 |
|---------------------------|--|--|---|---------------------------------------|
| US Holiday: Memorial Day. | 9:00 AM: Case-Shiller Home Price Index | 7:00 AM: MBA Purchase Applications | 6:00 AM: Monster Employment Index | 8:30 AM: Employment Situation |
| All Markets Closed | 9:45: Chicago PMI | 7:30 AM: Challenger Job-Cut Report | 8:30 AM: Jobless Claims | 10:00 AM: ISM Non-Manufacturing Index |
| | 10:00 AM: Consumer Confidence | 7:45 AM: ICSC-Goldman Store Sales | 8:30 AM: Productivity and Costs | |
| | 10:00 AM: State Street Investor Confidence Index | 8:15 AM: ADP Employment Report | 9:00 AM: 3-Year, 10-Year Note and 30-Yr Bond Announcements | |
| | 11:00 AM: 4-Week Bill Announcement | 8:55 AM: Redbook | 10:00 AM: Factory Orders | |
| | 11:30 AM: 3-Month Bill Auction | 10:00 AM: ISM Manufacturing Index | 10:30 AM: EIA Natural Gas Report - 11:00 AM: EIA Petroleum Report | |
| | 11:30 AM: 6-Month Bill Auction | 10:00 AM: Construction Spending | 11:00 AM: 3-Month and 6-Month Bill Announcements | |
| | 3:00 PM: Farm Prices | 10:00 AM: 4-Week and 52-Week Bill Auctions | 4:30 PM: Fed Balance Sheet and Money Supply | |
| NO POMO TODAY | POMO DAY (\$1.5Bn - \$2.5Bn) | POMO DAY (\$6Bn - \$8Bn) | NO POMO TODAY | POMO DAY (\$6Bn - \$8Bn) |

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