2014 Q2 STRATEGIES

SEASONAL SECTOR TRADES

JEFFREY A. HIRSCH
& JOHN L. PERSON

STOCK TRADER'S ALMANAC

WILEY

The Seasonal Sector Trades series features quarterly reports that use extensive research and analysis to identify the best-performing seasonal trades of all the major financial and commodity markets. Created for the busy, on-the-go trader and written by veterans of the trading industry, the in-depth analysis and data presented in the Seasonal Sector Trades reports will benefit novice traders and professionals alike.

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1 INTRODUCTION*

It is impossible to predict the future. That is why we rely on seasonal and historical analysis to help us understand, or better yet, to remind us what price trends have occurred in the past and how often these trends perform. These patterns typically occur as a direct result of perennial supply-and-demand changes year after year. Every year has differences, from changes in monetary and fiscal policies to global macroeconomic situations to presidential-election-year cycles to extreme weather and other exogenous events.

After seven lucky years of developing and delivering the annual *Commodity Trader's Almanac* we transformed our annual opus into a new, digital-only quarterly report to provide more timely actionable trading analysis to traders and investors in stocks & bonds, energy, metals, grains, softs, meats, and currencies.

John has created a brand-new proprietary tool for the new publication: *price projections based on seasonal expectations and recent trading activity*. The proprietary algorithm delineates the price projections for each trade presented at the time of this writing through Q2 2014. Three different scenarios are displayed so that you can better gauge the quality of each seasonality's trade setup and decide if and how to execute with respect to technical, fundamental, and market sentiment readings at the time.

Our Q2 Outlook is followed by our full-year Seasonal Trading Strategy Calendar and 2014 Q2 Top Seasonal Sector Trades. Each of the three months of Q2 2014 begins with a concise description of the trading patterns of the seven major complexes: stocks & bonds, energy, metals, grains, softs, meats, and currencies. The complete history and considerations of each top trade are then detailed, including a spreadsheet of the trade, price projection chart, correlated ETF or stock idea and chart, and the seasonal trend.

To give you a window into How We Trade, we have included several real-world examples of how we incorporate seasonal trade setups with technical and fundamental analysis.

Use this report as a reference guide and to compare current events against history. We have included the data, which allows the reader to distinguish which years had predominantly bigger price moves to compare where current prices and trends are against past historic data.

There are a great many tables and charts presented in this report, all including important data. For an up-close view of them, go to www.wiley.com/go/seasonalsectortrades (see end of report for more information). There you can also sign up to get notices about the next issue.

May all your trade executions be profitable!

Jeffrey A. Hirsch and John L. Person

PRICE PROJECTIONS WITHIN SEASONAL EXPECTATIONS

The purpose of *Seasonal Sector Trades* is to enhance and improve upon the work and analysis originally provided in the *Commodity Traders Almanac*. Many years ago, when we first began that publication, trading in commodities was becoming a more mainstream investment product. However, as *exchange-traded funds* (ETFs) took shape traders and investors began to lose focus on the seasonal supply-and-demand changes that many commodity markets demonstrated throughout the year. In addition, what we brought to the table and introduced investors to for the very first time in a publication was the various ETFs and stocks that held a tight correlation to the seasonal price swings of an underlying commodity product.

For example, there is a typical seasonal decline that occurs in early fall followed by the perennial rally that begins in mid-winter with Crude Oil prices and the relationship with (USO) the oil ETF or refiners like Exxon Mobile (XOM) or Conoco Phillips (COP) (see Figure 1). Many of our readers were impressed by the correlations in the Agricultural markets, such as the grain complex, and the moves associated with stocks in that group, like Monsanto (MON), John Deere (DE), and fertilizer names like Potash (POT) (see Figure 2). Individual retail speculators along with institutional traders found the research and analysis in the foreign markets extremely helpful, especially in light of the fact that many were unaware of the influences that create the seasonal factors on the various foreign currencies.

Figure 1 Crude Oil NY (Comb) Cont Liq @ NYMEX (Weekly bars)

Figure 2 Soybeans CBT (Comb) Cont Liq @ CBOT (Weekly bars)

As with any form of market analysis, the key issue to remember is there is no one single Holy Grail method. What we try to do is to improve our probabilities of success and to gain an edge over the market. Seasonal analysis does just that; it alerts us in advance of what the market might do based on past trends that a specific market has demonstrated. But present market conditions may have a magnified, muted, or negative impact on the seasonal influence of a product or market segment price move in the future. It is this reasoning that led John to develop his new proprietary analysis tool: *Price Projections Within Seasonal Expectations*.

This brand-new tool was introduced here to readers in our inaugural issue of *Seasonal Sector Trades*. Throughout this publication we provide to the reader three targeted price trends based on seasonal patterns and recent trading conditions at the time of publication: Bullish, Neutral, and Bearish.

Seasonal Sector Trades will provide on a quarterly basis the expected price targets based on a proprietary algorithm within those market condition assumptions. If the seasonal trend for a specific market is up, then the assumption is we should be in a bullish trend, and the price support and resistance projections are highlighted on the chart in green. If the market is in a seasonally strong period, but due to market conditions the price move is muted, we give a neutral price target or lower price support and resistance targets in blue. Finally, if bearish market conditions have a negative impact on a market, we give an estimated price target for downtrending price environment in red. See the example for the S&P 500 in Figure 3.

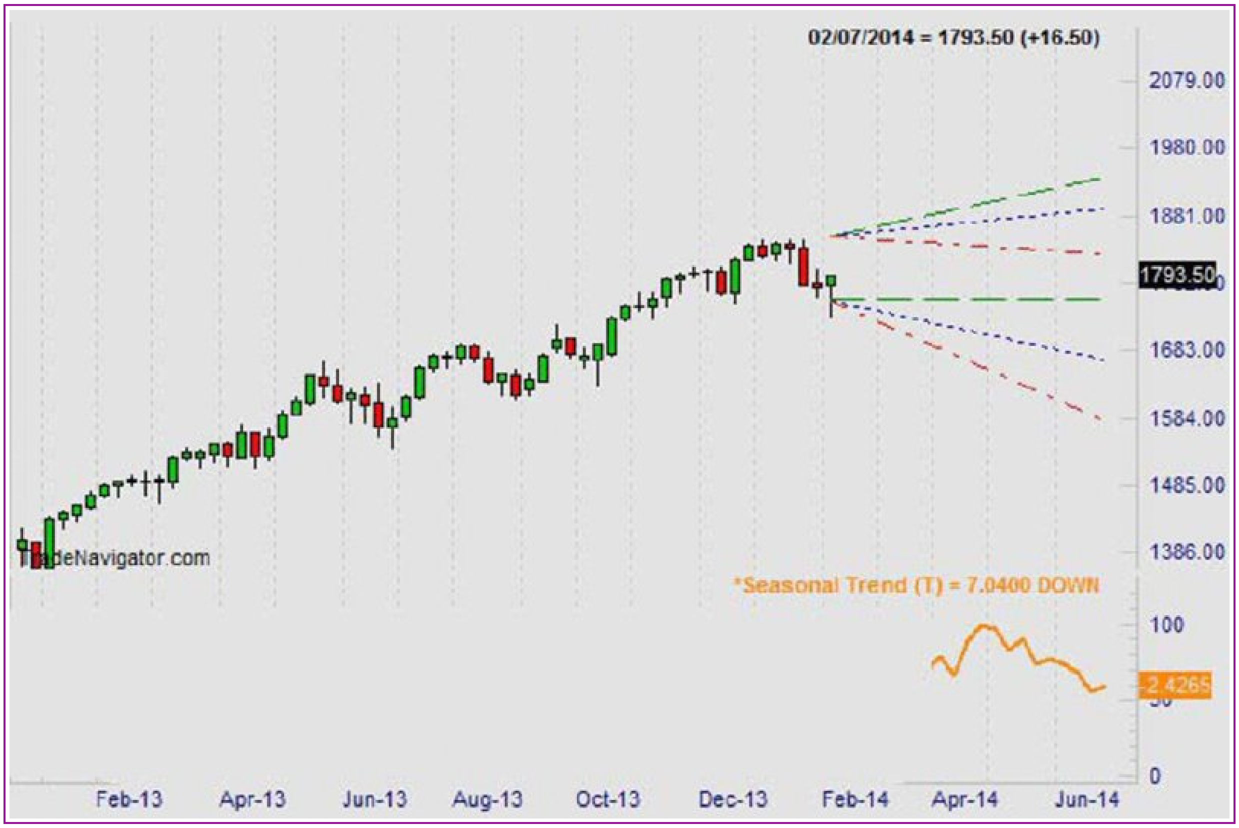


Figure 3 E-Mini S&P 500 Cadj Liq @ CME (Weekly bars)

Considering the complexities of a global economy, especially with many foreign central banks' intervening with loose monetary policies by means of *quantitative easing* (QE) and the current tapering of longstanding QE by the U.S. Federal Open Market Committee (FOMC), predicting or anticipating a market's moves or price trends has become even more difficult. That is precisely why we rely on our new *Seasonal Sector Trades* publication to pinpoint better trading opportunities. It alerts traders and investors to what the expected trend of the market is likely to be based on past price action and historical seasonal patterns. Projected price targets will help readers develop an institutional-type investment and trading plan based on the projected price targets and seasonal trends. Armed with this information you will now be able to anticipate the duration of a seasonal trend for a given quarter as well as the price assumptions under specific market conditions. Options traders can now look at the selected expiration dates and strike prices that meet these price outlooks.

This latest innovation in market research using price projections within seasonal expectations should enable you to set more manageable risk parameters as well as profit objectives in a timely manner in order to decide what type of trade or trading strategy to implement, whether using ETFs, futures, stocks, or complex options strategies.

NOTE

*To access online versions of all figures and tables, please visit www.wiley.com/go/seasonalsectortrades (password "season123").

2 OVERVIEW OF THE QUARTER*

Many of us find it difficult to plan or think about what may happen 30 days in advance, let alone an entire quarter or two or three or even a year or more. As for the markets, our goal in *Seasonal Sector Trades* is to help individual traders and investors alleviate that stress, and perhaps give valuable insights into potential trend changes for the various markets.

Throughout our combined 60 years in the business and the 47 years of the *Stock Trader's Almanac* we continue to be amazed at the commonly held delusion that markets and price structure will remain constant or in a certain condition and the utter surprise when these conditions repeatedly change on a dime with perennial regularity. The famous words of the twentieth-century philsopher, George Santayana, “Those who cannot remember the past are condemned to repeat it,” seemed so true after a major rally like the one the S&P experienced at year-end fell into the mid-January correction while many thought the world was coming to an end. This publication has been created to warn of these events before they unfold so as to prepare the savvy trader for potential opportunities.

With that stated, we expect the 2nd quarter of 2014 to remain in sync with the typical seasonal trend in U.S. equity markets. It will be a challenge for the U.S. Federal Reserve to completely wean off its quantitative easing bond-buying program, thereby giving undertoned support to the markets. We are also not convinced that we will have a major improvement in the unemployment numbers and a more unified government that is able to set a balanced budget, lower spending, and improve fiscal policies. This would make a less restricted and less cumbersome business environment that could allow major corporations and small businesses to expand their workforce. However, there is evidence of pockets of strength in the domestic economy, while we do see continued concerns in Emerging Markets and Latin American economies. Moreover, China recently came into the spotlight as its economy has shown signs of a slowdown.

Under this scenario we expect equity markets to maintain value in Q2, but be warned of the impending seasonal weakness that often begins in May. As discovered in 1986 by Yale Hirsch, founder of the *Stock Trader's Almanac*, the Best Six Months of the year end in April and the Worst Six Months commence in May, giving credence to the old adage, “Sell in May and go away.” In addition, midterm election-year politicking and mudslinging tend to ramp up in Q2, which can magnify perennial seasonal softness.

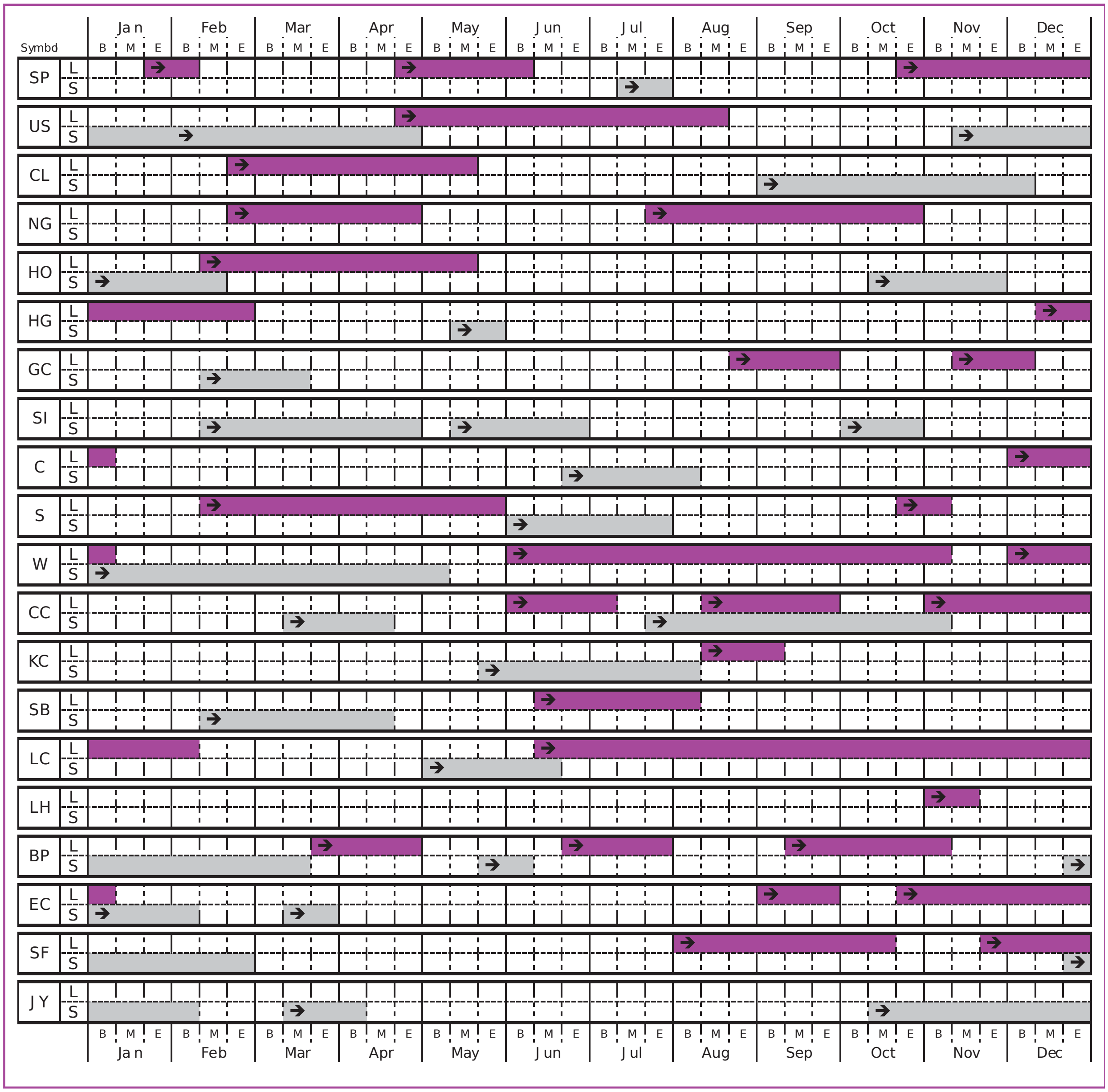
Bond prices are likely to remain flat to down as the yield in 30-year Treasury bonds inches higher as the Fed continues to taper its bond purchasing programs (QE) and should remain between 3.50% and 4.25%. The U.S. dollar in this period may also continue to be under pressure, which, all things being equal, creates a floor of support for dollar-denominated commodities like Gold and Crude Oil. This is intriguing, as Gold is typically weak in this time period while Crude Oil is in a seasonally strong phase.

The Federal Reserve's new Chair, Janet Yellen, should continue to keep interest rates low, in a through line of action from her predecessor, Ben Bernanke. This should give way to an increase in the Consumer Discretionary sector (XLY) and specifically to Home Builders like Lennar (LEN), Toll Brothers (TOL), and Pulte Home Group (PHM). Under this assumption, commodities such as Copper should remain firm through early April and stock traders will want to watch for these two issues, Freeport McMoran Copper & Gold (FCX) and BHP Billiton (BHP), to stabilize if not move higher into late April.

It will likely be prudent to focus on the typical upswing in crude oil prices in the 2nd quarter. Demand for summer-blend gasoline, diesel, and jet fuels increases in preparation for the early summer driving season. In the agricultural sector, Live Cattle prices typically tend to move lower, but due to heavy losses from an unseasonably cold winter, we do not see a major price decline during this time period this year—rather a price stabilization.

As you can see, we have several seasonal trade situations that develop due to either changes in weather conditions or seasonal shifts in the supply/demand equation. Armed with the new price projections in our featured markets, combined with correlated ETFs and equities, we look forward trading together with you!

Seasonal Trading Strategy Calendar*



*Graphic representation of the Top Seasonal Sector Trades. L = Long Trade, S = Short Trade, → = Start of Trade.

To access an online version of this table, please visit www.wiley.com/go/seasonalsectortrades.

2014 Q2 Top Seasonal Sector Trades

Commodity	Contract	Years	Trading Day	Hold Days	Success Rate	# Gains	# Losses	Total Gain	Best Gain	Worst Loss
April										
30-Year Bond Bottoms (Long)	U	1978–2013	18	81	69.4%	25	11	$88,766	$20,250	$17,031
S&P 500 Bottoms (Long)	U	1982–2013	18	28	65.6	21	11	13,525	23,075	33,175
May										
Cattle Peaks (Short)	V	1976–2013	2	30	65.8	25	13	17,260	2,808	2,470
Copper Peaks (Short)	N	1973–2013	8	13	63.4	26	15	22,288	7,513	6,600
Silver Peaks (Short)	N	1973–2013	10	29	68.3	28	13	83,925	19,750	13,000
Coffee Peaks (Short)	U	1974–2013	16	54	72.5	29	11	151,523	37,556	17,119
British Pound Peaks (Short)	U	1975–2013	20	8	64.1	25	14	13,663	7,125	1,938
June										
30-Year Bond Bottoms (Long)	U	1978–2013	2	10	63.9	23	12	$20,359	$5,156	$2,828
Cocoa Bottoms (Long)	U	1973–2013	2	24	63.4	26	15	17,610	2,980	4,130
Soybeans Peak (Short)	U	1970–2013	5	36	63.6	28	16	16,275	12,763	16,375
Wheat Bottoms (Long)	Z	1970–2013	6	105	54.5	24	20	20,439	12,025	15,300
Sugar Bottoms (Long)	V	1975–2013	11	32	61.5	24	15	22,411	5,398	5,869
Cattle Bottoms (Long)	J	1970–2012	14	160	67.4	29	14	42,320	15,270	11,600
Corn Peaks (Short)	U	1970–2013	18	25	63.6	28	16	21,781	8,975	9,050
British Pound Bottoms (Long)	U	1975–2013	20	16	71.8	28	11	33,131	8,406	7,188

To access an online version of this table, please visit www.wiley.com/go/seasonalsectortrades.

NOTE

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