

FLS Playbook 01.11.16

Note: The Format For This Week's Report Is Different Due To Last Week's Historic Shellacking. Thankfully, FLS Made Money Last Week & Is Very Well Positioned For A Very Strong 2016 And Beyond!

The Only Thing That Matters - Easy Money

Before we get into the market and everything else. We want to take some time and reiterate what we have been saying for the past few years: **the primary driver of this entire 6.75 year bull market was easy money from the Fed and other central banks.** Don't take our word for it, let's look at the facts (full QE timeline below). Shortly after QE 1 was announced, stocks bottomed (in March 2009) and soared while QE 1 was in place. Then, stocks fell sharply when QE1 ended. Nothing to worry about because within no time, the Fed announced a second round of money printing (QE 2) and that triggered a huge rally on Wall Street. Once again, stocks fell hard until the Fed announced operation twist. You guessed it, stocks rallied then when that ended, stocks fell again until QE 3 began in September 2012. This time, the market didn't respond well. So the Fed doubled up QE 3 in December 2012 and that led to a huge rally on Wall Street for 2013 and most of 2014. Then when QE 3, ended in Oct 2014, the QE trade morphed because Japan and Europe started printing. Initially, stocks in the US rallied but that little bump was short lived have been treading water since. In fact the major indices are now at or below where they were in Sep of 2014, right before QE 3 ended. In the process, the S&P 500 hasn't gone anywhere during that time and instead has formed a huge topping pattern (see below). To make matters worse, the Fed decided in their infinite wisdom to raise rates a few weeks ago in Dec 2015 and once again, stocks fell with a vengeance. These are the facts, not opinions and since the 2008 financial crisis the primary driver of this entire, now aging, bull market has been easy money from the Fed and other central banks. Everything else is noise. Now that the stock market is falling once again, we wouldn't be surprised to see the Fed back peddle and bring rates back to zero and even announce another round of money printing (QE 4) if conditions continue to deteriorate. Remember, they are "data dependent." We hope our point is made. Keep that in mind during 2016 because the game doesn't change. We updated the following table courtesy of our friends at CNBC:



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Now, Let's Look At The Market:

Charts Of The Week:

S&P 500 Has Formed A Major Top Since QE 3 Ended



The Russell 2000 Is Already Flirting With A Bear Market



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Market Update: Stocks Mauled On Global Recession Fears

In our intra-week note we wrote, *"Allow us to be clear, the major indices are in the process of topping out and barring some large unforeseen reversal to the upside - we are headed into a long overdue bear market for stocks (and possibly a global recession). A few of the major indices are now in correction territory (defined by a decline of 10% from a recent high) while several important sectors (transports, commodities, biotechs, just to name a few) are already in bear market territory. Thankfully, our defensive/cautious stance has been right on the money since last summer (for our newer members, we first turned cautious before the big crash in Aug 2015 and have been very selective since)."* Stocks continued to plunge causing the first week of 2016 to go down in history as the weakest first week on record. The popular indices were crushed this week with the small cap Russell 2000 breaking below last year's low and it is now down 19% from its record high. Remember, the media defines a bear market as a decline of 20% or more from a recent high. Leadership is virtually nonexistent which means it is just a matter of time until the major indices "officially" enter bear market territory. Now that the jobs report is behind us, the market will shift its focus to earnings season. As always, we want to pay attention to how the market reacts to the numbers. Remember, stocks soared from 2009-2015 and nearly every earnings season was lackluster at best.

Global Bear Market And a Global Recession

Commodities and nearly all major currencies (except for the USD) are already in a bear market which usually means we are headed into a global recession and a bear market for stocks. Oil prices tumbled a whopping 10% last week and Chinese stocks continued to plunge which triggered fresh concerns about a slowing global economy. Meanwhile, several important sectors are already down over 20% from their highs such as the Transports (IYT), Biotechs (IBB), and Retail (XRT), just to name a few.

Portfolio Update & How To Short:

Thankfully, the FLS portfolio had a very good year in 2015 and will look to short strength in the near future. The market plunged last week and is deeply oversold in the near term so there are no working orders today. As a quick reminder, in downtrends, the rules we use to buy are simply reversed. Meaning, instead of buying a breakout above resistance, we short a breakdown below support. Instead of buying using our early entry points (a short down trendline in a longer uptrend), we short when a shorter upward sloping trendline is broken in a longer downtrend. Finally, those of you who like patterns can, in most cases, simply reverse the bullish patterns.

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Analyzing The S&P 500's Latest Moves (Up & Down)

Nearly every pullback over the past few years has been shallow in both size (small percent decline) and scope (short in duration) which is normal bull markets. The opposite is true during bear markets so we'll see if this changes.

Pullback				Rally			
	High	Low	% Change		Low	High	% Change
SPX	2116.5	1918.46	-9.36%	SPX	1993.3	2081.56	4.43%
SPX	2104.3	1993.26	-5.28%	SPX	2019.4	2104	4.19%
SPX	2116.5	2019.39	-4.59%	SPX	1871	2116.48	13.12%
SPX	2020	1871	-7.38%	SPX	1867	2020	8.19%
SPX	2132.8	1867	-12.46%	SPX	2044	2126.64	4.04%
SPX	2134.7	2044.02	-4.25%	SPX	2039.7	2134.72	4.66%
SPX	2129.9	2056.32	-3.45%	SPX	1980.9	2119.59	7.00%
SPX	2134.7	2085.67	-2.30%	SPX	1972.6	2093.55	6.13%
SPX	2119.6	2039.69	-3.77%	SPX	1820	2079.47	14.26%
SPX	2093.6	1980	-5.42%	SPX	1904	2019.26	6.05%
SPX	2079.5	1972.56	-5.14%	SPX	1814	1991	9.76%
SPX	2019	1820	-9.86%	SPX	1737	1897	9.21%
SPX	1991	1904	-4.37%	SPX	1646	1850	12.39%
SPX	1897	1814	-4.38%			Avg Gain	7.96%
SPX	1850	1737	-6.11%				
SPX	1729	1646	-4.80%				
		Avg Pullback	-5.81%				

Year-To-Date Scorecard

Nasdaq -7.3%, S&P 500 -6%, DJIA -6.2% Russell 2k -7.8%

Key Points

- Uptrend: Short-Term Down, Intermediate & Long-Term Toppy
- SPX Resistance: 2134.72
- SPX Support, 1867.01
- Sarhan's Crowd Behavior Index: **Bearish**
(Proprietary market indicator that measures crowd sentiment: Bullish Bearish or Neutral)

Global Macro Update

- **Stocks:** Sideways
- **Bonds:** Sideways
- **Currencies (Euro/USD):** Sideways
- **Softs:** Downtrend
- * **Energy:** Downtrend
- * **Metals:** Downtrend
- * **Grains:** Downtrend

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Monday-Wednesday's Action: Sellers Shows Up With A Vengeance

Stocks tanked on Monday after a new round of selling began in China. Overnight, Chinese stocks plunged a whopping 7% which triggered a worldwide sell-off. Stocks in China were halted after new circuit breakers were introduced. Monday was the first trading day for the month, quarter and year and the worst opening day for Wall Street since 1932! Stocks were relatively quiet on Tuesday as the market paused to digest Monday's very sharp sell-off. Reuters reported that the People's Bank of China (PBOC) injected nearly \$20 billion into money markets to help calm markets. That was the largest cash injection since September 2015. This led people to be concerned that China's central bank was interfering with markets again and using state banks to prop up the yuan at the same time. In the U.S., motor vehicle sales pointed toward a record year. Stocks tanked again on Wednesday as the selling continued to hit markets across the globe. Oil prices plunged over 5% and Gasoline futures plunged over 8% which illustrates how weak global demand is right now. On the economic front, the ADP said private employers in the U.S. added 257k new jobs in December, beating estimates for 190k. Factory orders slid by 0.2% in November matching Briefing.com's consensus estimate. Finally, the ISM Service Index fell to 55.3 in December missing estimates for 56.4.

Thursday-Friday's Action: Jobs Report Beats Estimates; Stocks Fall

Stocks opened sharply lower on Thursday after China's stock market was closed 29 minutes after the when it plunged another 7%, triggering circuit breakers...for the second time this week. China removed the circuit breakers which was just put in place on Monday. Around mid-day Reuters reported that China may devalue its currency by another 10-15% (a huge amount) to help stimulate their lackluster economy. Before Friday's open, the government said U.S. employers added 292k new jobs, beating estimates for 200k. The stronger than expected jobs report is normal for this point of the cycle (late stage).

Market Outlook: Bull Market Continues To Top Out

This bull market is aging by any normal definition and will celebrate its 7th anniversary in March 2016. The last two major bull markets ended shortly after their 5th anniversary; 1994-2000 & 2002-Oct 2007. ***As always, keep your losses small and never argue with the tape.***

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12.8% Of Stocks in the S&P 500 Are Above Their Respective 50 DMA (Market Tends To Turn When This Reading Gets Above 70% or Below 40%)

Observation: Readings above 70% usually (not always) correspond with a short term pullback Conversely, reads below 40% usually (not always) correspond with a short term bounce



FLS Leaders:

We don't like the way the market is trading right now. A few stocks still look strong (see our Big Cap and Small/Mid Cap Leaders List In The Body Of The Email With This Report) but in bear markets - the rules change.

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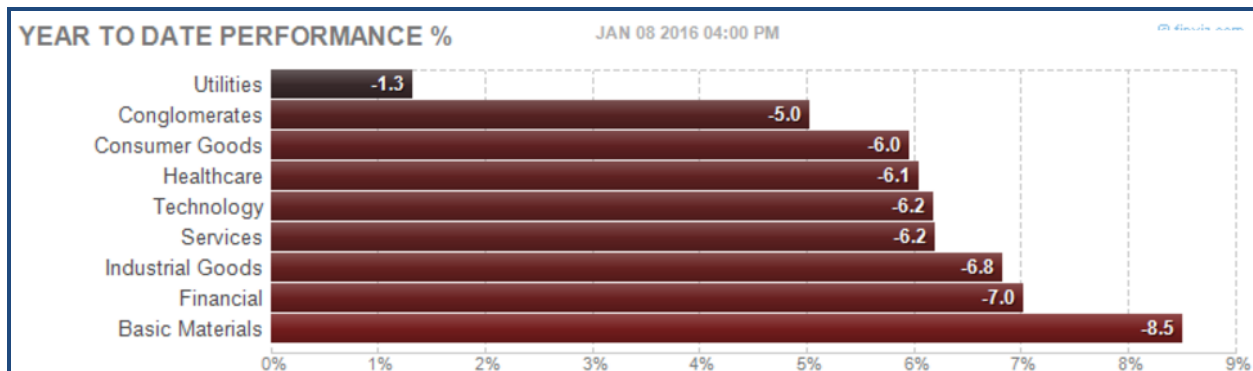
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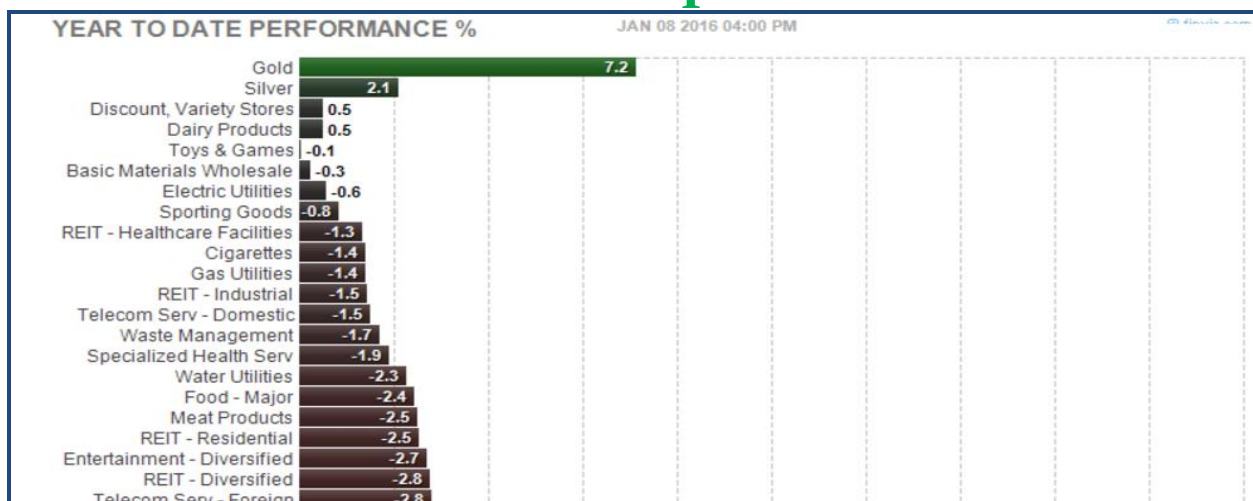
No New Setups This Week

The Market Is Very Oversold and Earnings Season Is About To Begin So There Are No New Setups This Week

Year To Date Sector Performance



Year To Date Group Performance



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Strongest Stocks Over The Past 12 months - Not Year To Date

These are the top 20 strongest performing tickers that are trading over \$5, average daily volume over 1M and have a market cap >300M (Small cap-Mega Cap)

No.	Ticker	Perf Week	Perf Month	Perf Quart	Perf Half	▼ Perf Year
1	DYAX	0.32%	1.04%	68.78%	37.74%	158.49%
2	SRPT	-6.87%	-2.36%	-4.97%	19.69%	146.77%
3	NFLX	-2.61%	-12.28%	-3.08%	14.57%	133.13%
4	SWHC	2.96%	5.80%	24.82%	37.65%	122.74%
5	AMZN	-10.19%	-10.38%	13.86%	36.87%	102.04%
6	TXMD	-19.19%	-7.51%	32.81%	5.28%	98.11%
7	W	-11.49%	-8.15%	6.84%	12.85%	96.96%
8	ATVI	-7.75%	-9.27%	12.54%	40.81%	87.41%
9	PBY	0.22%	13.19%	44.48%	50.61%	87.31%
10	CSC	-9.73%	-2.74%	71.59%	66.02%	76.31%
11	PACB	-3.96%	29.87%	67.91%	138.83%	63.13%
12	CVC	-2.79%	5.26%	-6.57%	16.96%	60.35%
13	HRL	-1.15%	0.58%	20.49%	37.52%	53.90%
14	NVDA	-10.10%	-11.71%	13.65%	51.23%	51.67%
15	FSLR	-0.56%	11.09%	28.36%	49.03%	50.40%
16	RAI	2.10%	2.32%	2.67%	24.65%	48.99%
17	PBF	-1.11%	-4.46%	8.59%	19.19%	48.51%
18	SERV	-2.42%	-2.30%	12.39%	4.39%	44.87%
19	BYD	-6.49%	-1.75%	3.51%	15.98%	44.70%
20	BLDR	-14.53%	-26.82%	-34.91%	-25.37%	44.36%

“Never argue with the tape and always keep your losses small.”

***Trade wisely,
Adam Sarhan***

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FLS Approach:

Rules-Based Discretionary Approach

The actionable items for the week are at the very top of this report. The rest of the report is available for those of you who want more information, new ideas, trade setups, and a deeper analysis on the market.

Please know that FLS employs a rules-based discretionary approach to trading/investing in capital markets. FLS employs a tactical long/short intermediate term trading strategy. FLS views trading/investing as an art, not an exact science.

Capture The Bulk Of The Move, Not The Top or Bottom

FLS strives to capture the bulk of the move in bull and bear markets, not pick an exact top or bottom. That is why FLS does not use the same rules and/or definitions (for patterns, entry/exits, pyramiding etc) as other people and instead looks for the essence of the concept/pattern. FLS has conducted its own private study of every major prior market and economic cycle (economic cycles go back to the 3rd century & are available on the Market History tab on FindLeadingStocks.com). This process has led FLS to develop its own proprietary trading/investing strategy (D.A.M.P- available on the Strategy page) to navigate capital markets for you each week in real-time.

Advanced Entry/Exit Points & Type of Orders

Two critical points of difference: FLS uses advanced entry/exit points to enter/exit ahead of the crowd and always looks to define/reduce its risk in the market. Before a trade is entered, the service will tell you the exact entry and exit price before the market opens each week. All the FLS orders (buy and sell) are entered as GTC stop orders that remain open and are resting at all times. Once the first order is entered the protective GTC exit begins working and is also resting at all times. This is the best way that allows for full transparency and accountability with our members. In addition, throughout the report there are several more trade ideas & setups that readers can use (if they want more ideas). The dotted line (advanced entry point) is designed to provide an earlier entry point (ahead of the crowd). Typically, the crowd is only buying on a traditional breakout (classic) pivot/buy point. Each person is free to use the ideas anyway they like. One buy, two/three buys (pyramid), or wait for the classic entry point.

Position Sizing & Risk Management

Typically, the maximum risk is 1% of a portfolio on any one idea from entry to exit. Alternatively, you can use the 10% rule. Meaning, you divide your portfolio into 10 tranches and every time you buy a stock you buy with 10% of your capital and place a stop 10% below your entry price. This way, if wrong, you will still lose 1% of your overall portfolio per idea. Protective stops are always advertised in advance and only tightened, never widened. In uptrends, FLS prefers buying in a base (near support, downward trendline, or classic breakout) not only above resistance. This approach helps you get in ahead of the crowd, buy leaders on weakness, not just on strength, and allows for fewer stop outs. If at any time you have any additional questions, please send us an email.

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Our Job & General Info

Our job is to provide our members with a steady flow of good ideas in all market environments. We know that we work for you and that is why we do our best to go above and beyond - all time. You are free to use the ideas anyway you like and discard the ones that do not appeal to you. Keep in mind that investing and trading involves risk. The value of your investment will fluctuate over time and you may gain or lose money. Since each person has different objectives, time-frames, goals, etc, please note that everything we provide is for informational, educational and/or illustrative purposes only and we DO NOT provide specific advice of any sort (investing, trading, tax, etc). *Please read our disclaimer below and on our website for more.* Charts are courtesy of FreeStockCharts.com, ThinkorSwim, and StockCharts.com. If you haven't already done so, please watch our free educational webinars by visiting FindLeadingStocks.com- then click on the Webinars page.

A Closer Look At Reversals:

Positive/Negative Reversals

A negative reversal occurs when an underlying investment (market, stock, currency, bond, commodity, ETF, etc) opens higher and turns/closes lower in the same bar- on any time frame (daily, weekly, monthly, etc basis). This action typically suggests downward price action will follow. The basic concept is that the current bar you are looking at opened higher and closed lower. A positive reversal is the exact opposite (occurs when the underlying investment opens lower and turns/closes higher- and has bullish ramifications).

Upward/Downward Outside Reversals

An outside reversal occurs when the highs and lows of the current bar (any time frame you choose) are higher and lower than the previous bar (same time frame). Typically, the outside reversal is more meaningful than a normal reversal and the same applies (upward outside reversals tend to be bullish while a downward outside reversals are bearish).

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