An Options Approach to Sell in May and Go Away 2024

TOM'S TRADING ROOM

Tom Gentile

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SELL IN MAY AND GO AWAY – IF YOU HAVEN'T HEARD OF IT BY NOW YOU WILL

The adage Sell in May and Go Away can be argued by some as a market axiom whereas others may say it is more of a theory.

My job with this report is not to convince you what it is. To me it could be either or both. All I have is the data that I can pass on to you and tell you what I see can happen going forward and how I operate with my options trading taking into account the Sell in May and Go Away premise.

My intention with this educational report is to make you aware of the market tendency over this period of time so you can then be better prepared to discuss with your financial professionals what you may want to consider doing in your investing and/or options trading.

Sell in May and Go Away refers to the dates of May 1 to October 31 of a given year.

Being the end of the more bullish phase in the markets ends on October 31 it is sometimes referred to as the Halloween strategy or Halloween indicator.

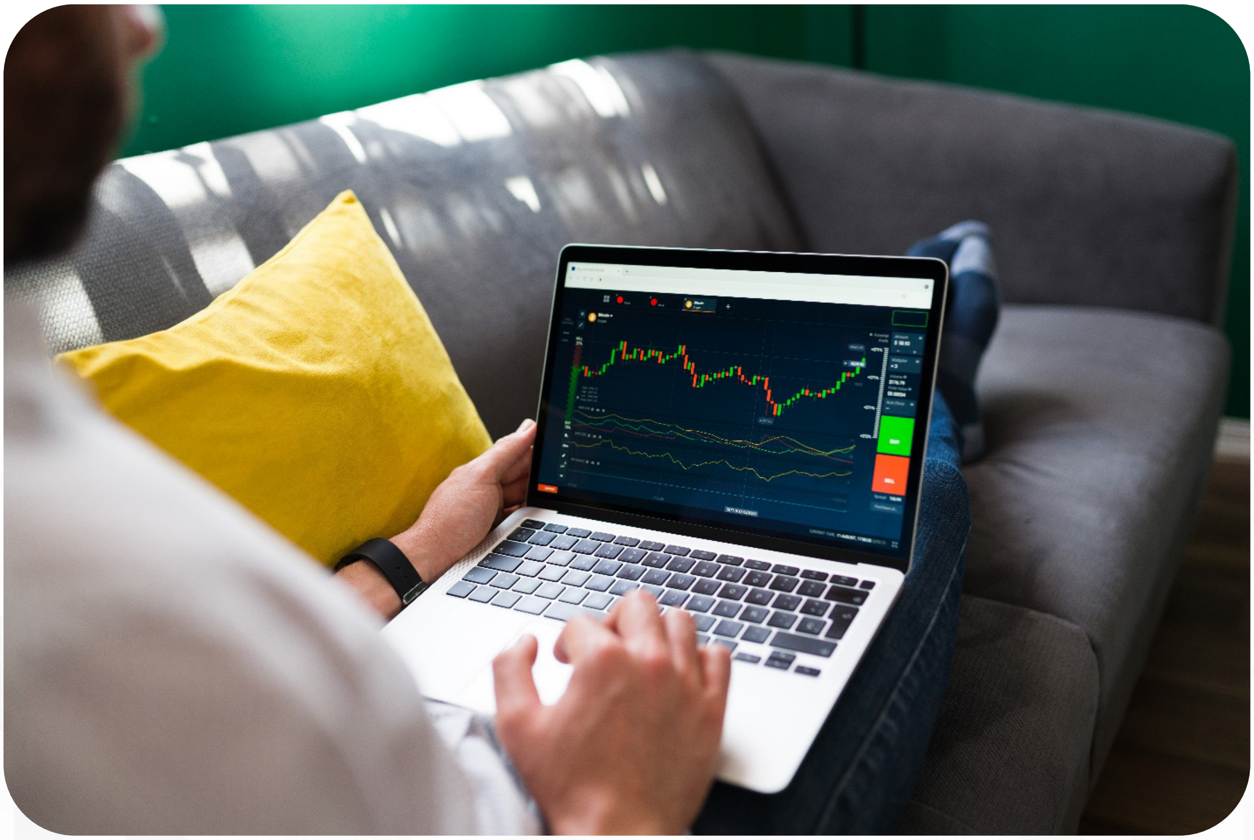
This is a 6-month period of time where the returns of the market are less robust (May 1 - October 31) than the other 6 months (November 1 – April 30).

PLEASE note that I don't consider this period of time in the market the time to liquidate my accounts and go hide away in the mountains until this period ends.

I am not here to say over this time frame the markets are going into a bear market or a bearish phase. The markets can end up higher at the end of this period, it just may not be up as high as the markets have the other 6 months of this pattern.

A strategy I love that I see having wonderful profit potential is Selling Puts (more on this later in the report) and can even perform this strategy during this period.

2 SEASONS OF TRADING: SUMMER AND WINTER



The Sell in May and Go Away months are deemed the summer months and the months from November to the end of April are considered the winter months.

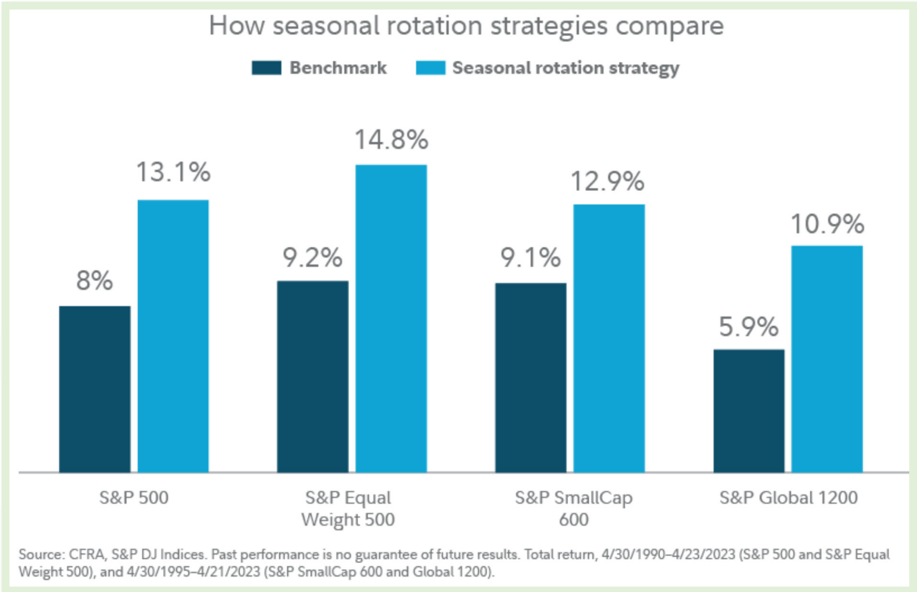
The term for this period of time (May 1 – October 31) is sometimes referred to as the 'summer doldrums'.

PERFORMANCE NUMBERS BETWEEN THE TWO PERIODS

The most powerful tool one has as an investor is Time. The longer one stays invested, the more the power compounding interest has to work and grow one's money.

As an options trader, the challenge is the underlying securities may not make as much of a price move in some time periods than other times of the year, which may not give as much ROI potential in the option. Some options strategies can take advantage of time decay and do not need as strong a price move to reap profits. These strategies may include Credit Spreads and or Time/Calendar Spreads. I mentioned I like the Selling Puts strategy, and I still plan on educating you on the basics later in the report. But before I get into the Selling Puts strategy let me point out the data.

The researched data shared is from various sources and we will reference where the data came from. According to Fidelity Investments since 1990 the S&P 500 has gained an average of about 2% from May through October, whereas the S&P 500 tends to gain a 7% average, thereabouts, from November through April.



The above image is also from Fidelity and the research shows how one can consider a rotational strategy, where one can rotate money from one asset class to another, and how the other classes shown in the image compare over this time period to the benchmark S&P 500.

This image and data further show me the Sell in May period is NOT one to bail on the market during its 6 months. The Fidelity data says to consider rotating money into different sectors. They see consumer discretionary; industrials, materials, and technology sectors have notably outperformed the rest of the market from November through April.

They then go on to say defensive sectors outpaced the market from May through October.

What I ascertained from them is this: since 1990 there has been a clear divergence in performance among sectors between the summer and winter periods.

‘SELL IN MAY’ MIGHT BE ‘STAY IN MAY’ THIS YEAR

The S&P 500 went on a decisively bullish tear from November of last year to present, (even though at the time of this writing the S&P 500 has rolled over a bit from its all-time, closing high established on March 28, 2024.

Before that, the S&P 500 gained about 5% from May 1, 2023, to October 31, 2023, (Summer months). To emphasize again how the winter months tend to outperform the S&P 500, it is up roughly 20% from November 1, 2023, through April 24, 2024.

We have the Fed backing away from the perceived existing plan to cut interest rates this year. For a while there, the expectation was we were to get 3 rate cuts this year. Now it seems some aren't expecting their first rate cut until January of 2025. Right now, their battle is against inflation and trying to control the rates at a level needed as they want to get or see inflation get down to 2%.

Another reason we might see an immediate stall or decline in price performance, at least starting in May; is earnings.

At this point earnings season for the first quarter is about halfway through.

Based on expectations earnings are coming in better than expected overall.

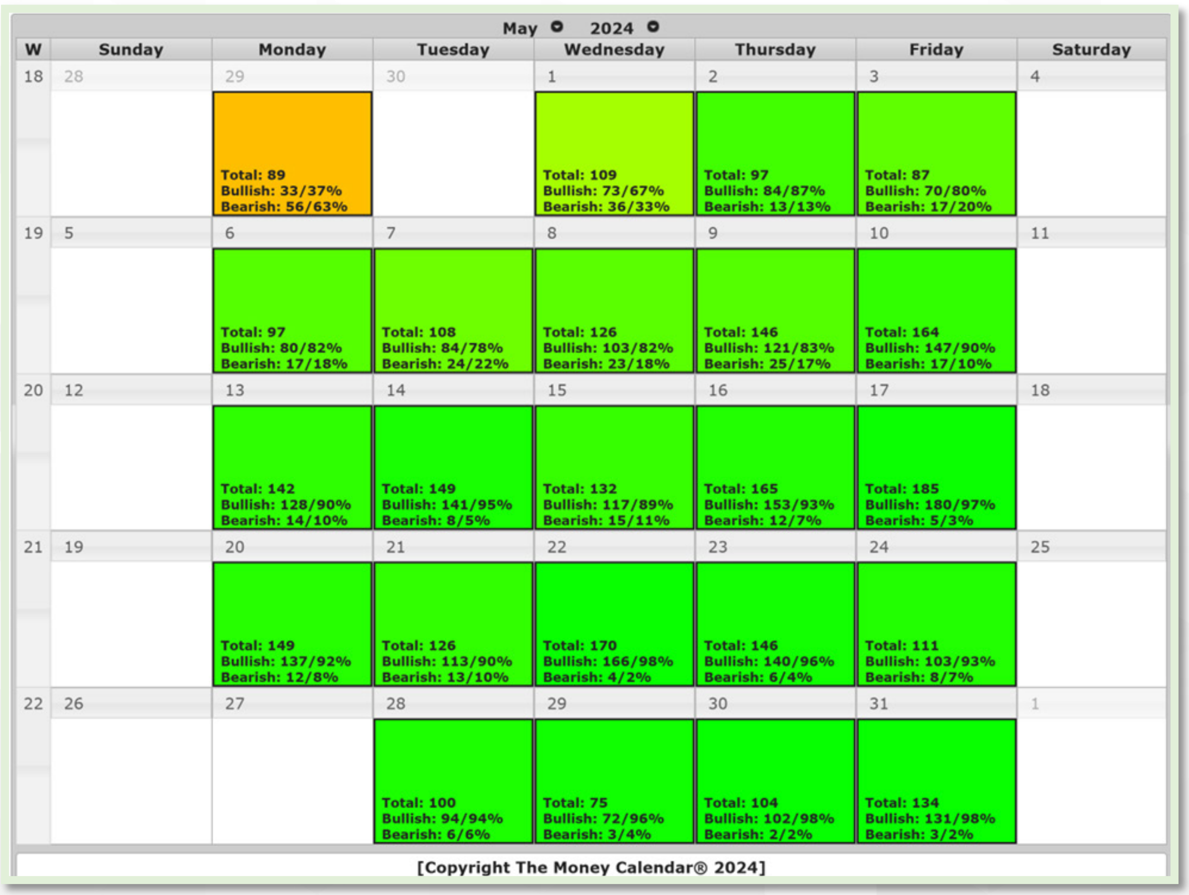
The latest info from FactSet reports, 46% of the companies in the S&P 500 have reported for Q1 2024 to date. 77% of these companies have reported actual EPS above estimates, which, per the report, is equal to the 5-year average of 77% but above the 10-year average of 74%.

MONEY CALENDAR IN MAY

Despite this, we are coming up on a seasonally bullish period of time for the markets based on my Money Calendar scanning tool. My curated list of 325+ securities show the majority of 10-yr. back-tested price moves happened in a bullish manner.

Each day I get a total number of securities that have moved either higher or lower 90 or 100% of the time, meaning they moved higher or lower 9 or 10 of the past 10 years.

This bullish data indicates that the first month of the Sell in May might not be as bearish as one might expect.



May 2024

W	Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
18	28	29 Total: 89 Bullish: 33/37% Bearish: 56/63%	30	1 Total: 109 Bullish: 73/67% Bearish: 36/33%	2 Total: 97 Bullish: 84/87% Bearish: 13/13%	3 Total: 87 Bullish: 70/80% Bearish: 17/20%	4
19	5	6 Total: 97 Bullish: 80/82% Bearish: 17/18%	7 Total: 108 Bullish: 84/78% Bearish: 24/22%	8 Total: 126 Bullish: 103/82% Bearish: 23/18%	9 Total: 146 Bullish: 121/83% Bearish: 25/17%	10 Total: 164 Bullish: 147/90% Bearish: 17/10%	11
20	12	13 Total: 142 Bullish: 128/90% Bearish: 14/10%	14 Total: 149 Bullish: 141/95% Bearish: 8/5%	15 Total: 132 Bullish: 117/89% Bearish: 15/11%	16 Total: 165 Bullish: 153/93% Bearish: 12/7%	17 Total: 185 Bullish: 180/97% Bearish: 5/3%	18
21	19	20 Total: 149 Bullish: 137/92% Bearish: 12/8%	21 Total: 126 Bullish: 113/90% Bearish: 13/10%	22 Total: 170 Bullish: 166/98% Bearish: 4/2%	23 Total: 146 Bullish: 140/96% Bearish: 6/4%	24 Total: 111 Bullish: 103/93% Bearish: 8/7%	25
22	26	27	28 Total: 100 Bullish: 94/94% Bearish: 6/6%	29 Total: 75 Bullish: 72/96% Bearish: 3/4%	30 Total: 104 Bullish: 102/98% Bearish: 2/2%	31 Total: 134 Bullish: 131/98% Bearish: 3/2%	1

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SECOND BEST 3-MONTH PERIOD BASED ON WINNING PERCENTAGE

Last year's report showed data from Merrill Lynch analysts saying that the month of May saw a stock market advance 57% of the time. Going back to 1928, the 3-month June-August period typically is the second-best of the year, realizing a gain 63% of the time, of which the average reported then was a gain of 2.9%. I haven't read anything over this past year that says anything has changed.

Merrill goes on to write that a weak May normally results in a "more robust" June-August period.

5 STYLES OF OPTIONS TRADING

The previous data written in this report speaks to my teams and my assessment that even if there is merit to the Sell in May approach pattern, in recent years we no longer view this as a call to action to bail on one's investments and go to cash.

Though the markets (SP500) may not be as robust in the summer months vs winter months there is still an opportunity to make money whether it be with one's investments or as an options trader.

I, as an options trader, have 5 ways or styles I use for my options trading.

(1) Seasonal – Sell in May is a seasonal approach.

(2) Statistical Based

(3) Volatility Based

(4) Momentum Based

(5) Trend Based

In some ways, a couple of these may be similar to others on the list, say Seasonal and Statistical.

Seasonal is where a security has a pattern or history of trading up during certain parts of the year, (like semiconductors tend to do week in the summer), and there are statistics that say how often the security trades in a particular way or direction during certain parts of the year or over specific time frames.

I deem 'Sell in May and Go Away' as a seasonal pattern.

MY OPTIONS TRADING MANTRA

1) Spot an Opportunity

2) Build an acceptable risk option trade, and

3) Manage that trade

First, I recognize a seasonal pattern or the overall markets with Sell in May. I then research to (1) Spot an Opportunity.

Since I mentioned findings from Fidelity that defensive sectors outpaced the market from May through October during this period, I want to look at Money Calendar to see if I can find a security in that sector that has a Money Calendar bullish pattern to consider and options trade on.

MY IDEAL OPTION STRATEGY: SELLING PUTS (FOR EDUCATION PURPOSES ONLY)

I am an options trader and educator of how to trade options. I do not offer recommendations and this option strategy scenario is not to be taken as such.

I can show you how I use my online option data/analysis tools to find trade setups, but it is up to you to discuss the suitability of any trades in your account with your broker/financial professional.

When I say selling puts it is where one is actually selling 'naked' puts. Naked means one does not own the underlying security.

A put option is the right to sell or 'put' the security to another. What is occurring here is selling the markets the right to sell you the stock at a specific price on or before a specific date.

There are a couple of things that can happen in a selling put scenario.

The first thing that could happen is the underlying security trades higher than the strike price put you sold and at expiration if the stock is higher than that strike price you are not likely to be forced to buy the security.

This should result in that option expiring and you keep the money made for the sale of that put option.

The second thing that could happen is the stock is less than the strike you sold and at expiration (or sooner) you get assigned or 'put' that stock.

You would have to have the money in the account (likely at the time you sold the put option – or what is called 'cash secured') to acquire 100 shares for every contract sold (as 1 contract is equal to 100 shares).

That reminds me to tell you all my first rule of selling naked puts: I only sell a put on a security I wouldn't mind owning in the first place. If you don't want to take ownership of the security do NOT sell a naked put on/against it.

Then if you end up taking the stock you have done so at a reduced cost to what the strike price is because the premium of the sold option reduces one's basis.

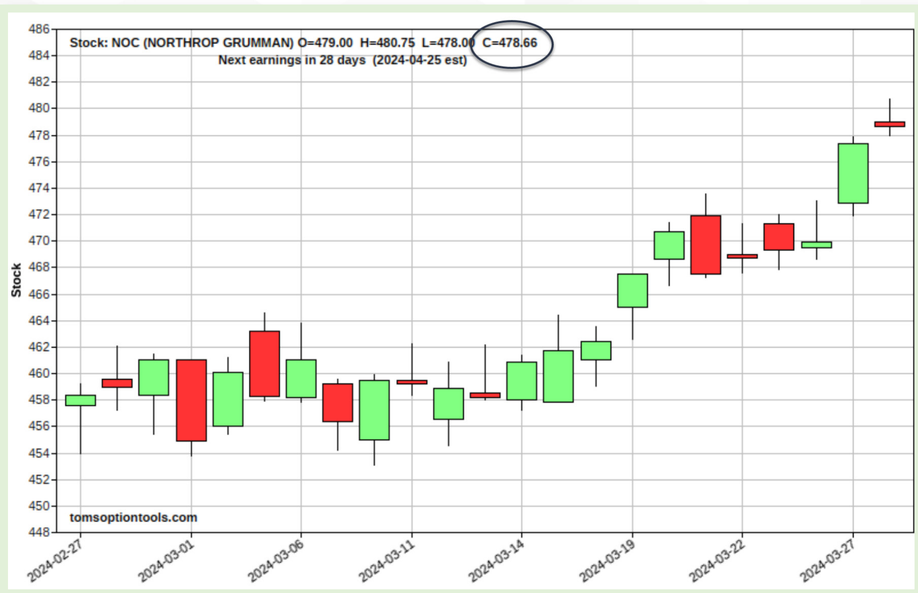
And you can now consider the Writing Covered Call strategy to potentially cash flow the markets by doing this as often as you can.

EXAMPLE OF THE SELLING (NAKED) PUT STRATEGY

LEN	27	$8.56	90.00%	$0.86	Jun 6, 2024	3	-34.4
LMT	26	$103.24	90.00%	$10.32	Jun 5, 2024	3	57.96
LRCX	25	$245.43	90.00%	$24.54	Jun 4, 2024	5	747.35
LUV	8	$21.15	90.00%	$2.12	May 10, 2024	10	30.88
LVS	8	$24.12	90.00%	$2.41	May 10, 2024	6	30.98
LYV	30	$25.75	90.00%	$2.58	Jun 11, 2024	1	6.36
MA	1	$9.57	90.00%	$0.96	May 1, 2024	4	22.38
MAR	4	$23.13	100.00%	$2.31	May 6, 2024	-	38.45
MCHP	19	$16.93	90.00%	$1.69	May 27, 2024	5	30.52
MCK	27	$138.96	90.00%	$13.90	Jun 6, 2024	6	8.48
MDY	25	$124.29	90.00%	$12.43	Jun 4, 2024	5	164.24
MSFT	1	$13.68	100.00%	$1.37	May 1, 2024	-	27.18
MSI	3	$19.83	90.00%	$1.98	May 3, 2024	10	100.94
MSTR	12	$366.22	90.00%	$36.62	May 16, 2024	10	1
NDAQ	26	$15.15	90.00%	$1.52	Jun 5, 2024	1	21.99
NOC	26	$154.94	100.00%	$15.49	Jun 5, 2024	-	153.33
NOW	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

The below Money Calendar data table shows two defense stocks with a bullish Money Calendar Pattern, Lockheed Martin Corporation (NYSE: LMT) and Northrup Grumman Corporation (NYSE: NOC). I will use NOC for this example (Not a recommendation).

NOC at the time of this writing was $478.66.



Money Calendar shows the average price move for NOC on this pattern over the range of days shown is 15.49 points or an average profitable move of $15.49.

Should NOC just move its average a target price could be assessed at $494.15.

One could Sell-to-Open an NOC May 17, 2024, $480 Put for $12.60.

This example is showing the numbers based on 1 contract (100 shares).

If you sell-to-open this option that would bring in $1,260 and one would have to have on hold $48,000 (if assigned, you would have to buy 1-00 share of NOC at $480).

Position	Num	Option Symbol	Expire	Type	Entry
Sold	1	NOC240517P480	2024 May 17	480 Put	12.60

For some that may be doable but for others, they may have to find 'selling put' opportunities on securities in their price range.

Scenario #1 is NOC trades higher than the $480 strike and therefore no one is likely to put you to stock at $480 since they could get a higher price on the open market.

You would get to keep the $1,260 and can consider looking out to future months to consider doing this again.

Scenario #2 is NOC stays below the strike and at expiration you get assigned or have to buy the 100 shares of NOC at $480.

The cost of that amount of shares at that strike is $48,000 however by taking in the $1,260 that reduces your cost basis. Instead of owning it at a basis of $480, its cost basis instead is $467.40.

Now you have the choice to look out for future months' expirations and the strikes and premiums possible to go after with writing covered calls.

Either way, I am happy. I either keep collecting premiums every time I do this, or I sometimes take ownership of a stock I would want to own anyway, and I get paid to acquire it.

If over the Sell in May Go Away period of time the markets are less robust I anticipate selling puts closer to the securities price as it may not move in price enough to get in the money on the strikes sold, but as implied volatility goes up over this period of time I could make money with the premiums being a little higher than normal.

DISCUSS WITH YOUR FINANCIAL PRO / BROKER ON WHAT YOU WANT TO DO

I realize for some they consider it best for them to simply go with the long-term investment goal; the buy-and-hold strategy, which means they only want to hang onto equities year-round, year after year, unless there's a change in the security's fundamentals.

Being more active than they currently are with their investments, just may not be in the cards for them.

They may feel intimidated as to what to do on their own and trusting their advisor may be deemed the safest thing for them to do – and they may see it as that approach is at least better than doing nothing at all.

I agree, putting some of your money to work in the markets over the long haul versus not, is better than nothing.

The thing to do now is discuss with your brokers / financial professionals what you collectively feel is the best approach for you. Do you take this info in and say thanks, but I will stick with what I have been doing or do you try sector rotation?

Do you add in some selling puts as a way to stay invested in securities and generate money through the sale of these option premiums with the possibility of taking ownership of stocks you would want to own anyway? This gives one the opportunity to stay invested and have shares to write covered calls on to generate more income.

I feel these scenarios are at least worth paper trading or tracking to see how they fare in this less volatile time period.

MY YOUTUBE EDUCATIONAL CHANNEL

I have a YouTube channel https://www.youtube.com/@TomGentileTrader where I educate and discuss my outlook on the markets at hand, my ideas on how to capitalize on pending market movements and how I use my software to spot opportunities, construct acceptable risk options and manage them. Go there and subscribe and continually learn from me.

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