

TRADERS' TRADERS

TRADERS'

The Secret of Success
Risk and Money Management
P. 48

Your Personal Trading Coach

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Trading the Scene of the Crime

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The ABC of Gap Trading

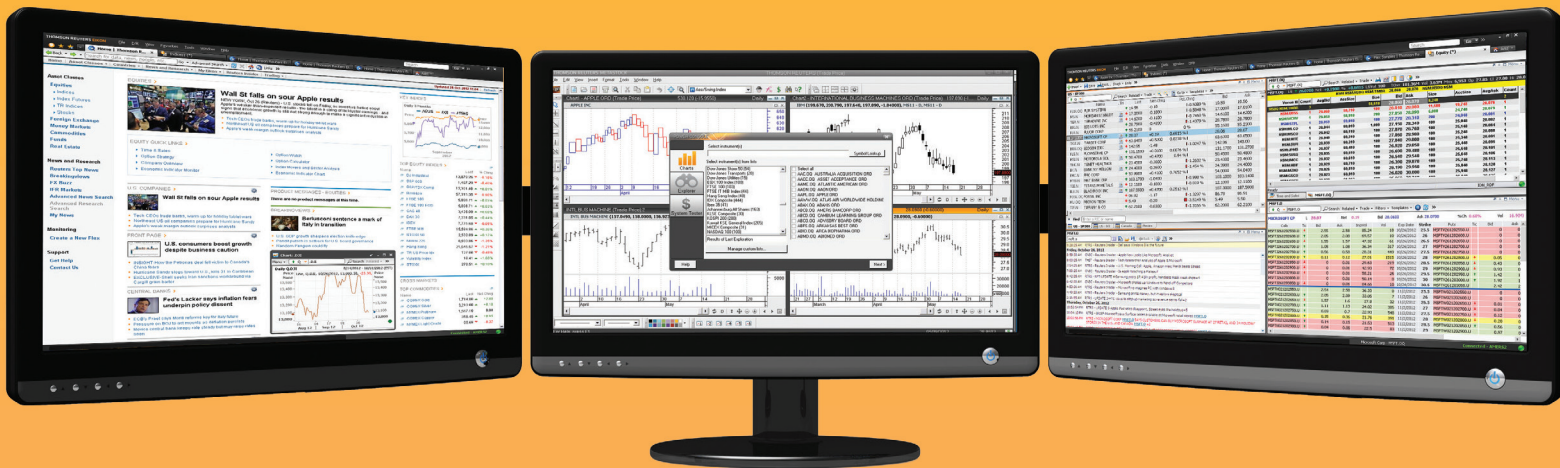
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Lothar Albert
Editor-in-chief and publisher

Eleven Years of a Sideways Trend

» Every trend is bound to come to an end sooner or later – and I don't just mean the long bull or bear market phases but also sideways phases, which have a much shorter life. Remember the year 2004 when stock markets were consolidating for around nine months? Or 2010 when things effectively were hardly moving for an equally long period? In both cases, the sideways phase was terminated by an upward breakout. Sideways phases, however, that continue for more than a year are very rare indeed.

What am I driving at? Well, it's all about a very special sideways trend that we have been observing for years. An absolutely straight sideways movement. No flinching in one direction or the other. Very rare indeed. I'm referring to the price of the printed edition of TRADERS' magazine in Germany.

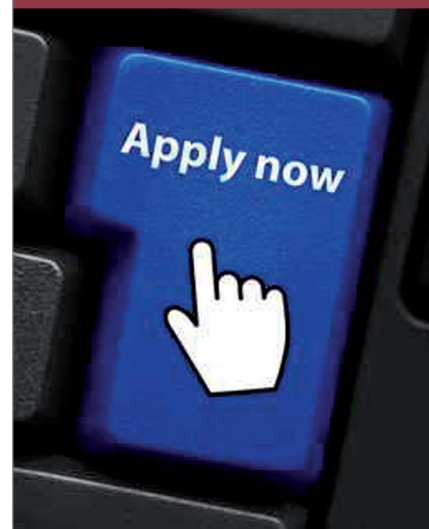
This "chart" has now been moving sideways for eleven years. Unchanged throughout all market phases whether they be a bull market or bear market or times of euphoria or panic. Our loyal readers in Germany have hung on to the "TRADERS' stock" – much to my delight. Of course, they've received rich dividends during that time – and on a monthly basis to boot – in the form of trading knowledge, strategy ideas, and great interviews with professional traders.

There is nothing new about the market invariably going up in the long term – history has taught us that. Similarly, there will be a long term increase in the level of prices. Everything is getting more expensive – with few exceptions, such as technology products. We have kept improving our magazine in the last few months and years, all of which has now led to an upward breakout of the magazine price from 5 euros to 5.80 euros for the German-language printed edition.

You as readers of the English-language online edition continue to enjoy an additional advantage: You can read the magazine for free! Besides diversification, that will give you the only free lunch there is on the stock market. I hope you can make a winning trade from this "market anomaly". «

Good Trading

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TRADERS'



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Mastering Fear in Trading

Stepping out of the Self-Limiting Patterns that Hold You Back

After a number of years of acquiring the knowledge of how to trade, most traders find their trading minds are still compromised by fear in the heat of the moment. Suddenly, all that knowledge is ambushed by fear just when they need that knowledge present in mind to make solid trading decisions. Inconsistent results follow regardless of how much their trading system is tweaked or changed to create external discipline. Finally the trader comes to the uncomfortable realisation that the problem is not with their methodology, their system, or the markets (despite these all working well in simulation) – the problem is in the six inches between their ears, and particularly with the way they deal, or don't deal, with their fears. In this month's cover story, Rande Howell (www.tradersstateofmind.com) describes how traders can overcome these issues.

» Does Fear Keep You Stuck in Trading Purgatory?

Traders read about expert traders who seem to be born with the right attributes for trading. These expert traders trade dispassionately with a powerful discipline that allows them to park their emotions at the door. And students of trading, who read about these characteristics of successful traders, often try to emulate the emotional control and state of mind they read about. They, like

Dorothy in the Wizard of Oz, click their heels and magically imagine themselves having the "right" emotional and mental traits. They may even watch a trader psychology DVD, listen to a guided meditation, mess around with their brain waves, or learn some Neuro-Linguistic Programming (NLP) tricks in hopes of an easy fix.

Try though as they may, the emotional roller coaster ride of their trading persists. The mistake students of

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trading make is that they compare themselves with these rare people who are born with a genetic predisposition and emotional temperament that is well suited for trading. Though they are rare, many aspiring traders set these off-the-shelf exceptional traders up as the psychological model for their trading. The problem is these rare traders come equipped with a very different emotional and mental predisposition than the vast majority of people who enter trading. In truth, most highly efficient traders have paid their dues and learned to work with their emotions, particularly fear, rather than suppress them (which does not work, but sounds like good advice).

Individuals may come equipped with a certain genetic inheritance that, under the right conditions, are expressed in such a way that it gives a person an advantage in certain

Components of an Emotion

What is emotion? It is simply the Body's/Brain's/Mind's triggering to any disruption to familiar status. Specifically, the components of an emotion (e.g. fear) are:

1. Arousal – the body cranking up
2. Feeling – subjective experience of the emotion. Thinking is compromised
3. Motivation – what the emotion is telling you to do (avoid, attack, approach)
4. Meaning (the assumption that becomes wired into your brain)
5. Temperament – genetics

domains. Taken to an extreme, you also see this genetic engineering in breeding dogs for certain traits. This kind of genetic engineering is simply not possible in humans. This does not mean that trait selection is not used to enhance performance though. Though humans are far more complex, the Russian and Chinese have used trait expression to steer young people with athletic promise to great advantage. And some traders win the genetic trait lottery for trading. The vast majority do not. They have to learn to develop a psychology built for trading. Otherwise, they continue to choke in the clutch – when the money counts.

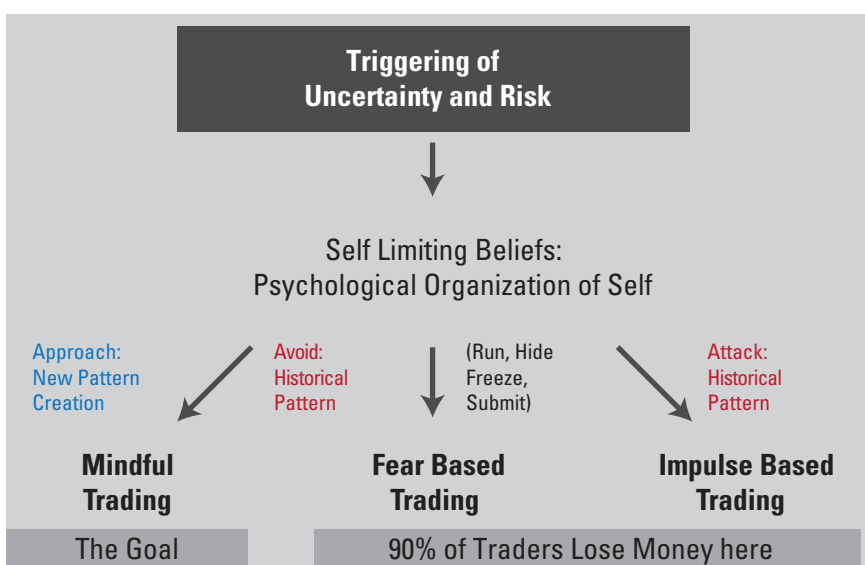
Nature vs. Nurture – If You Want to Conquer Fear, There Is Biology You Need to Understand

No matter how much they read about what the mind is supposed to look like to trade well, little is spoken about how the trader goes about building the very emotional and mental skills and attitudes necessary for successful trading. Just because nature did not equip you with the “right stuff” for your trading mind that does not mean that you cannot nurture your psychology so that you build the state of mind needed to successfully execute your methodology and become a consistently profitable trader. Just like other top performers in other domains, what separates them from the pack is not more talent (everybody has talent at the top), not better knowledge of their craft, but it is the emotional management (or emotional intelligence) to use that talent and knowledge in the clutch to produce peak performances. They have

to master their fears head on, rather than deny them. The same is true of traders, but even more so.

Nurture is of far more importance in developing a mind set than nature. Nature may give potential, but it is the individual that must develop that potential in order for it to become a talent. This means, even if you did not win the gene pool lottery, you can train your emotional and mental predisposition to your advantage in trading. Problematic emotional biases about money, worth, risk, and uncertainty are genetically handed down from one generation to the next. They are not deterministic traits. They are learned patterns that become wired into your brain/mind as habits. It's not genetics, but

F1) The Mind You Bring to Trading





Fearing fear is what locks the trader in repetitive self-limiting patterns. Learning to manage the fear, rather than fearing it, is the key to using trading knowledge effectively in the heat of the moment.



it is adaptation to circumstance. This is how the money narrative to which you adapted shows up in your trading. It is transmitted through the generations and your brain's adaptation to circumstance. And fear-based habits and beliefs can be de-constructed and re-organised into a much more trader-friendly perceptual map.

Deconstructing the Fusion of Uncertainty and Worry

Most of us grew up in environments that exerted pressure on our developing brain that organised us to “not make mistakes” and to focus on certainty rather than the management of ambiguity. It is from this constantly adapting brain that our “mind”, the way we interpret reality, emerges. For the vast majority of traders, by the time that a brain has approached maturity it is biased to seek certainty and avoid uncertainty. This is simply a biological bias of the human brain that has been amplified by what we are taught about risk and uncertainty.

This is an organisation of the mind that is not going to work well in trading. That particular adaptation can work well in other domains, but not in trading, where the emphasis is on embracing the management of uncertainty and risk. You brought a brain adapted to seek certainty and avoid certainty into the career of trading. The fear-based mind that emerges from these adaptive forces trades with a bias of not to lose because it fears loss. Now biology and psychology have conspired against the kind of mind that a trader needs to bring to trading – a mind that is comfortable with uncertainty.

Your brain fused uncertainty and the fear of death into a single construct (very appropriate for physical survival in a dangerous world), but was never prepared for trading markets. This particular

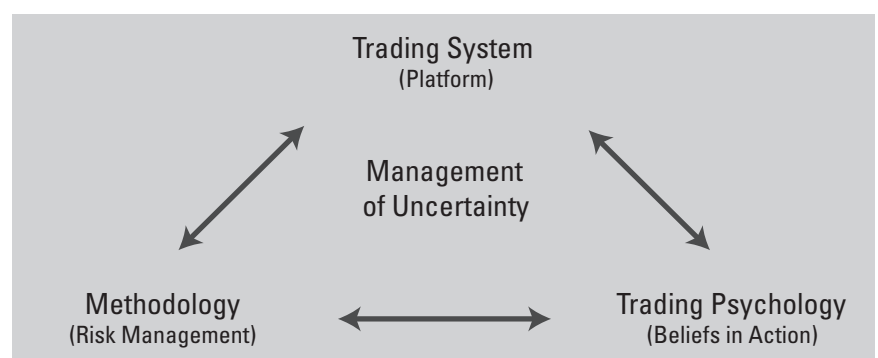
organisation of our perceptual map has to be de-constructed, de-fused, and re-organised from a fear-based interpretation of uncertainty to a probability and risk management based perception of uncertainty. This is the mind set that works in trading. The problem is that the uncertainty/fear construct has become the historical narrative that guides your perception of the markets. This is what you are projecting upon the markets. You are literally trading your beliefs about your capacity to manage uncertainty. It is at this point that the assumptions about fear and risk to which your brain adapted you become embedded as unexamined self-limiting beliefs. They sink into the background of your awareness and contaminate effective perception without your ever knowing it.

Out of Theory and into the Trading Room

What does all this theory look like in trading? Let's take a look.

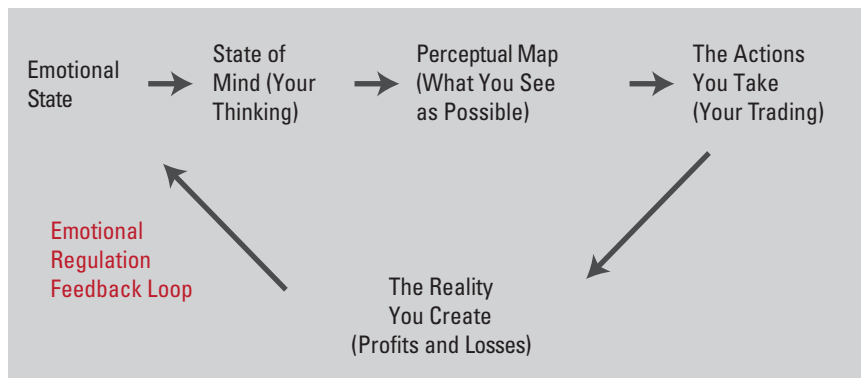
Jim is a trader who is literally a rocket scientist. He has a deep working knowledge of computer systems, aeronautics, and mechanical engineering – and now he is an attorney who practices intellectual property

F2) Successful Trading: Integration of Components



Without building the mind to harness the power of your system and methodology, your potential is blocked.

F3) The Cost of a Fear-Based Mind set



What happens if you don't address the fear? 90 per cent of traders lose money because they do not know how to conquer their fear. Leaving your emotions at the door is not an option. Instead, you can design which ones create your trading mind.

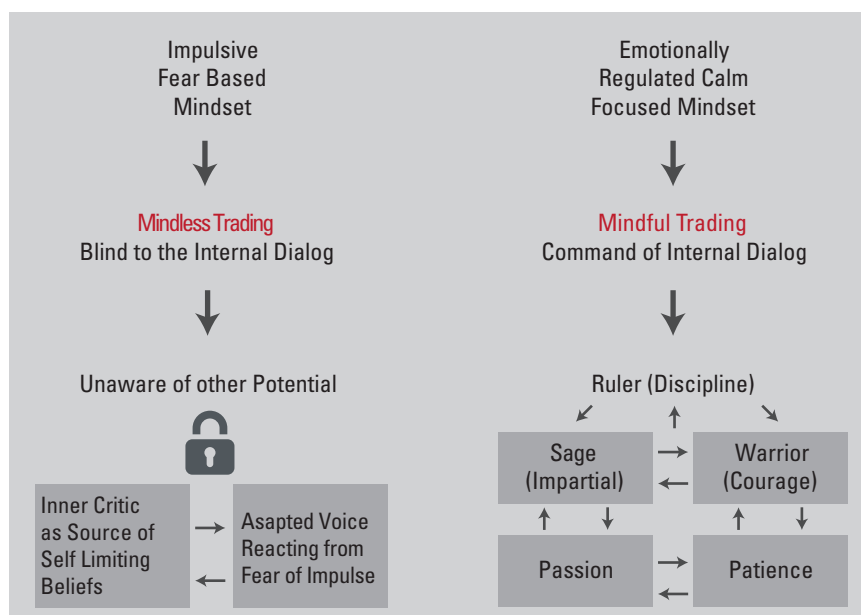
law. In simulation his trading reflects the clear thinking and impartial state of mind that you would expect out of a person with this kind of training and experience. However, when he trades and risk enters the picture he does not “see” all of the options and patterns that are reflected in his charts and indicators. His training is highly biased towards certainty (remember people’s lives and expensive equipment were at stake based on

his calculations) rather than the management of risk and uncertainty. He was trained that losing was not an option. Think about all that emphasis on “not making mistakes” and making good grades, rather than learning as we grow up. Then as an engineer, you are trained to “over engineer” so that the structure will not fail. You see the hidden bias here? This training became habitual and went into the background of his awareness. Now it is an unexamined bias that colours the perceptual world he sees. Uncertainty = Fear of being wrong. This assumption that uncertainty must be eliminated, now a belief embedded in the neuro-circuitry of his brain,

became the unexamined belief (or historical narrative) that he brought with him into trading. This belief was highly effective for him both as a rocket scientist and as a patent attorney where a high value was placed on certainty. However, this same thinking, so successful in one domain, was producing near panic for him while he was in a trade. As a result, he got out of trades too soon and he took his profits too quickly – long before he reached his target (he could be wrong and lose the profit he

had in his hands). Once in a trade, nothing was certain. Managing the trade was an exercise in the management of uncertainty in terms of probability rather than certainty. Uncertainty, still fused to fear, triggered and his rational and clear thinking mind was contaminated by fear. From this fear-based state of mind, options that would have appeared to him while in an impartial state of mind were swept away and replaced by the negative anticipation of worry. This is the impact of your historical narrative on your trading. And, of course, when the trading day is over and he reviews his trades, he cannot comprehend, why he missed so many signals and patterns. All he knows is that, yet again, he made bad trading decisions resulting in more draw-downs.

F4) Reconstructing the Trading Mind



The image describes the difference in the state of mind of a losing trader compared to a winning trader.

Changing the Historical Narrative of Uncertainty and Fear into Probability

Most traders (who come to recognise that the vast majority of trading is an inner game) come to realise that their historical narrative, now embedded in their neuro-circuitry of belief, is what has to be changed. There are no tricks or magic bullets. Most traders muddle through years of desensitisation (of their fears and self-limiting beliefs) before finding consistent success in trading. This process rewires beliefs about self and uncertainty that eventually open the possibility of trading on a new level. Fortunately, this re-organisation of the trader's mind can become more streamlined when we begin to understand how meaning is organised in the brain/mind.

There is no single organisation of the self. There is no final "me". "Me" is simply the current organisation of self beliefs that you hold as true. We do not see reality, we see shadows cast – and there is always an observer interpreting what it is experiencing. Traders come to hold certain assumptions about the market. Some of these assumptions have been worked out and have become an effective way of dancing with the market. Yet, the market does not care what assumptions you attempt to place on it, nor does it have awareness of the "truths" placed upon it by humans.

Before traders recognise that they are the problem (and the potential solution) to trading problems, they usually have traded for a number of years and are successful in simulated trading. They know how to trade a methodology that works in a classroom. It is when risk of capital is put in play that their "truths" about the market are challenged. It is at this point that the trader is not separating uncertainty from worry or fear. This situation is highly trainable. The assumptions of self that have become hardwired as self-limiting beliefs (their unexamined truths) are not failing because they don't know how to trade, but because they are not trained to operate in an environment of uncertainty. And the default adaptive program is to react from fear when confusion arises from moments of uncertainty (an everyday occurrence in the performance of trading).

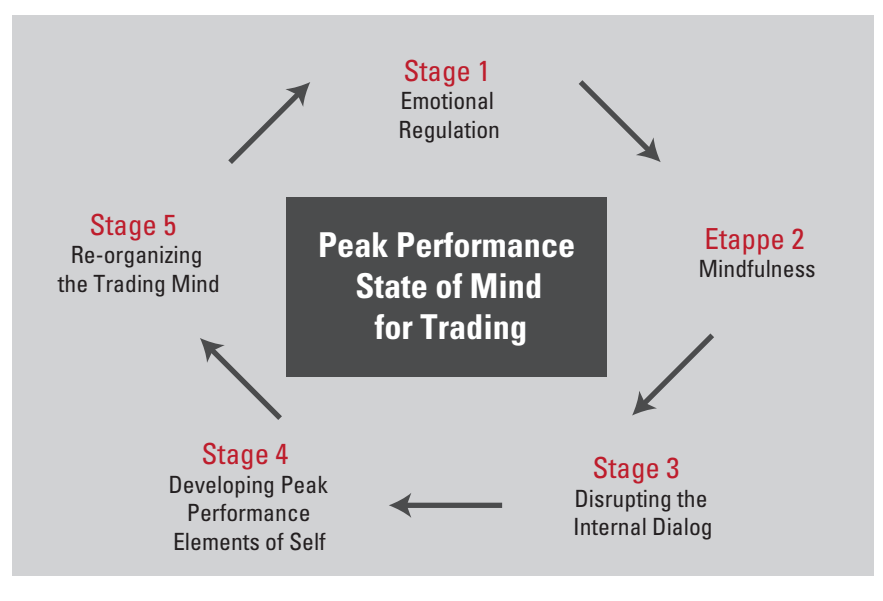
They will have to re-organise their beliefs about operating in an environment of uncertainty and their

skill to manage it, which can be accomplished, if the trader accepts full responsibility for the outcome. Otherwise, the trader will continue to fear fear. And of this program, wired into the neuro-circuitry, the trader begins to worry about a future that has not arrived, nor been created, yet. Fear now is contaminating the very critical thinking skills needed for peak performance trading. This is because the untrained emotional right brain is anticipating, with dread, possible negative consequences and then hijacks the rational left brain.

Fundamentally, traders need to learn a set of skills and tools by which they do brain surgery on their emotional belief system – this is far from applying logic to emotional reasoning. Trading becomes a great place to see "up front and close" the trader's beliefs about the self in action. There is no hiding from the "truth" as it has been organised within the self. Your trading account becomes the barometer of the effectiveness of the beliefs from which you trade. This is "walking the walk" rather "talking the talk". Yet most find that their "truths" are only unexamined assumptions about the world that drive their perception. It is at this moment that the assumptions behind the self-limiting beliefs can be observed and re-constructed. But the beliefs need to be seen in the context of emotion rooted in neuro-biology rather lumping beliefs into the thinking mind.

Building your beliefs into managing risk rather than avoiding risk is then possible. Anxiety at this point can be regulated and listened to, not from an avoidant observer, but from a disciplined and impartial observer – with very

F5) The Stages of Long Term Change



Roadblocks That Dominate a Trader's Mind – The 9 Trading Fears

1. Fear of uncertainty (hesitation)
2. Fear of loss (pulling the trigger)
3. Fear of missing out (impulse and exits)
4. Fear-based urgency to make up for prior losses (revenge trading)
5. Fear of not being right (making a mistake)
6. Fear of inadequacy (external validation)
7. Fear of self sabotage (blowing yourself up)
8. Fear of success or failure
8. Fear of growth and change (the box of your comfort zone)

Remember: The thinking you brought into trading IS NOT the thinking that will make you successful.

different outcomes. The “truth” they see allows them to be present in their trading very differently. The gap between simulated trading and live trading narrows as they train their state of mind to embrace uncertainty from a perspective of discipline, patience, courage, and impartiality. A far cry from the anxious state of mind that had them hesitating or trading impulsively as fear swept their thinking capacity away.

The major shift is that the trader is no longer trading to win or lose – which he cannot control with certainty. The trader is now managing the mind that produces the performance of his execution of the trade – which can be managed with a high degree of certainty. Outcome is still uncertainty in this way of trading, but the trader has now given his methodology and trading system the advantage of the probability of a successful trade. He is in control of the mind that manages uncertainty. This is trading in the zone or being in a trader’s state of mind.

Very few brain/minds have been shaped to trade well. Getting to the impartiality and discipline necessary

for trading is like trying to tell a horse in a burning barn to remain calm and simply walk out of the barn by carefully considering its options. Fortunately, belief can be changed. It begins with learning emotional regulation skills so that fear and greed do not sweep away your capacity to think from a disciplined and impartial state of mind. Then the trader must begin really examining themselves. This is done by developing the capacity to become mindful. Mindfulness, in essence, is the capacity to observe the coming and going of thought and to recognise that thought is not who you are. Thoughts, through the observation of mindfulness, become the voices of your beliefs that drive your trading. This is where the door to change opens.

The observer that we bring to uncertainty is what allows the trader to see what they see. A really good trader, as a trained observer of market phenomena, is seeing distinctions through his skill and an impartial mind set that a fear-based trader does not see, much like the rocket scientist turned trader was experiencing... very different observers of uncertainty with very different outcomes. There is a great Zen koan that goes like this: “Things are not always what they seem to be – nor are they any otherwise.”

Becoming Architect of the Self That Trades

Applying mindfulness as a tool to your trading allows you to bring the self-limiting beliefs that sabotage your trading into your awareness where they can be worked with. Instead of drifting on the currents of unseen self-limiting beliefs that limit the way you manage uncertainty and risk, you become the architect of the narrative you bring to trading. Uncertainty becomes decoupled from worry and fear. And you develop inner resources that allow you to bring forth into your awareness the discipline, patience, courage, and impartiality that live as possibilities in the totality of your being. In the face of uncertainty, you no longer have to be compelled by your fears to produce inconsistent results. Instead, you bring a state of mind to the uncertainty that creates the probability of successful trading. Trading is a journey into the possibility of who you can be. The “you” that you brought to trading is rarely the “you” that will bring you success in trading.

Emotional regulation and mindfulness are the cornerstones of re-organising the “self” that trades. It is your passion that gives you the motivation to learn and use these tools to become who you need to be for consistently successful trading. Trading becomes the journey into self mastery. «



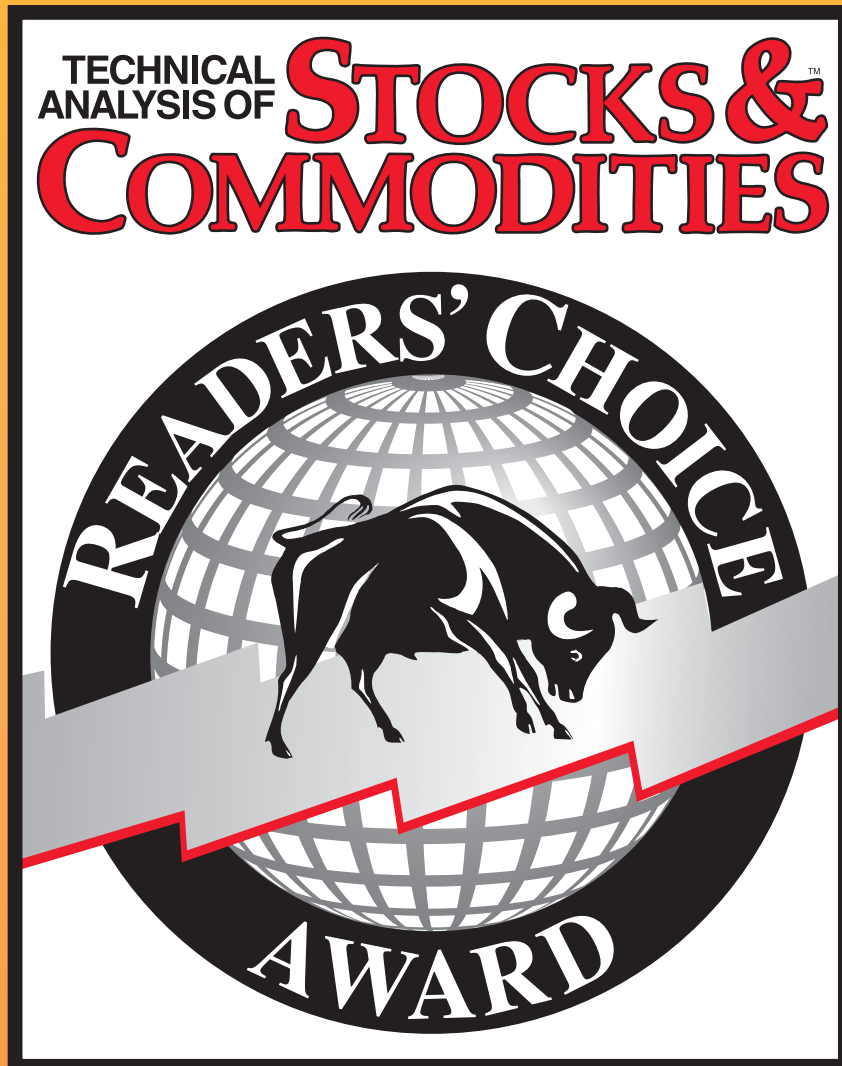
Rande Howell

Rande Howell (MEd, LPC) helps traders develop a peak performance state of mind. He is both a licensed therapist and performance coach whose work is grounded in emotional regulation, mindfulness, and Jungian archetypes applied to trading. He has a clinical background in training people to master their emotions and to transform self-limiting beliefs into productive mind sets. He is the author of four books including “Mindful Trading: Mastering Your Emotions and the Inner Game of Trading”. Rande also speaks internationally to traders, fund managers, and hedge fund managers.

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Alpesh Patel
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TRADERS' Talk

Knowledge Is Godly

This month we met up with one of the UK's most well known traders and market commentators, Alpesh Patel. After starting to invest at the age of just twelve years old at his local post office, Alpesh now manages his own London based hedge fund, has written eleven books on investing and entrepreneurship and is a frequent market commentator for BBC News and other financial channels.

» **TRADERS':** Hi Alpesh, thanks for taking the time to talk to us about your trading. To begin with, can you tell me what your preferred products and markets for trading are?

Patel: Nowadays it tends to be Forex. But it used to be stocks in the 80s when I was in my teens, moving on to penny shares (those under one GBP) because of the large rises, and then options trading because again of large potential gains and then onto futures, then spreadbetting for convenience. Today it is Forex and indices because of leverage (bang for buck) and also ease of trading and long trading hours and liquidity making my trading strategies easier to deploy.

TRADERS': Do you consider yourself a day trader, swing trader or position trader?

Patel: Definitely swing trader. I use the MACD a lot and it takes time to deploy those moves. Day trading is fine, where you hold positions for a few hours, but it is time consuming for me so I use my own algorithms to give me buy and sell signals and for swing trading. The secret to all success is automation – ever since the industrial revolution – actually ever since the invention of the wheel! Now we use computers for this automatism. My algos give me the buy and sell signals.

TRADERS': Information and reliable trading platforms are key to success for any trader. Can you reveal which platforms you use?

Patel: I like spreadbetting platforms from big players – after a bad experience using Worldspreads as a whitelable – I will never ever, ever use small firms ever again. You just can't risk it. I have recently completed a series of TV commercials with BWin and I like them of course and use MT4 for Forex trading on FXCM which is NYSE limited and a big hairy giant of a company. You can access accounts via www.alpeshpatel.com.

TRADERS': I have read many of your trading books over the years, and understand you started investing in shares as young as twelve years old – what, or who, originally inspired you to start investing at such a young age?

Patel: I lived opposite a Post Office and they had these free brochures which were for OAPs to understand so a twelve year old easily could learn about Government Gilts. So I borrowed £100 from my aunt because I wanted to pull my weight in my family who were working so hard.

TRADERS': Is this why you still devote your own time to teaching others to trade? A way of giving back, and helping others achieve success too?

Patel: I love education and communication. When I was at school and I eventually became a straight-A student, I would teach other students who would ask and their parents would be so grateful. Today, people ask why I do it, and I explain that I just love teaching and seeing the light bulb in others go on. But also because if you know something, and knowledge is godly, it is a sin to let others stumble and not teach them. So I subsidise my free education with some paid private education – a bit like in Britain we have state schools which are free, paid for by private taxes on the few who want privileged education! So for instance I charge people for my algos and that pays for all the free education I give in places like www.alpeshpatel.com.

TRADERS': In terms of trading strategies, can you describe your approach to trading?

Patel: Momentum and mean reversion are the two main strategies. With both I use triple filters to ensure all signals are confirmed before they are executed. The strategies work on basic principles of market insight about how prices move.

TRADERS': And what about stop-loss settings: this can often be the biggest challenge for new traders to get right – particularly when spread betting. How do you prevent getting 'stopped out' as it is known?

Patel: Most people don't realise that volatility based stops are what they need to avoid being too far or too close. I use either a two or three period low or a multiple of average true range. My position size is volatility based, so in more volatile markets where the stops would be wider because the market is swinging more wildly, my positions are smaller size and vice versa. That way there is no fear of being stopped too soon or too far.

TRADERS': How much is enough for you? When in a winning position how long will you go before taking profits? What are the main signals for you to out?

Patel: Exits are usually based on my algorithms. So with a MACD based exit it will be a two or three period low with a loss of MACD momentum. I then programme this into my algorithms so I don't have to keep looking for entry and exit conditions. I monitor this across various time frames so that I can have ample signals.

TRADERS': Do you add to winning long positions?

Patel: To winning positions yes, never to losing positions. But you have to make sure your holdings don't get too concentrated. I have created free education videos on adding to winning positions.

TRADERS': Do you favour any particular technical analysis systems to guide you – Bollinger Bands, Fibonacci, Elliot Wave or anything else? Or do you have your own rules?

Patel: I use MACD for momentum trading the most and also average true range (ATR) for mean reversion. But I use them in my own peculiar way, not the way you see in text books. I then put them in my algorithms for generating buy and sell signals.

TRADERS': When talking to early stage traders, what is the most important advice you give for becoming a successful trader?

Patel: Start small, read everything, understand trading psychology, be patient, practice load, find a strategy, understand money management and discipline.

TRADERS': The crisis in Syria and the anticipated response by the US has seen oil prices rise sharply recently – do you think this will continue, and what other global themes are you factoring in for your longer term trading strategies?

Patel: I tend to use just technical on indices and Forex so it actually doesn't get factored in, beyond that other than when it shows up in momentum as buy and sell signals on my algos. I don't try to work out why, only that I have a signal to enter or exit is all. That way life is simple and stress free.

TRADERS': And what about currencies? Do you foresee any big changes in Forex?

Patel: Well I'm going to India and the Rupee is at an all-time low against the Dollar. I think we will be surprised at Dollar strength because it is in fact a reserve currency and despite emerging market strength it will remain strong. Also the Euro will remain strong too, because we had overly been pessimistic about the Eurozone and as it starts recovering that will prove exactly how strong the monetary union is.

TRADERS': Thank you for your time. Your website www.alpeshpatel.com offers a wide variety of educational material, webinars, books and live training, but will you be making any live appearances later this year where people can meet you live?

Patel: I would love to do live appearances and I am due to speak at the London Investor Show (www.londoninvestorshow.com). I've just done a talk in Bangkok and so my live talks tend to be limited because through webinars I can reach a global audience.

TRADERS': Thank you Alpesh, good luck and we hope to talk to you again soon.

For further information about Alpesh Patel's books and training services visit www.alpeshpatel.com . «



Weekly Options – A New Field for Active Traders

Part 1: Plenty of Benefits and Few Drawbacks

Weekly Options – or simply “weeklies” – are a new category of options that have been available for just a few years. Unlike conventional standard options, they have a term of just one week. This means that active traders have totally new trading opportunities that come with a variety of advantages and few drawbacks. In this article, we will reveal some initial insights into the world of “weekly options”. Furthermore, specific strategies will be presented that can be implemented using these options.

» What Are Weekly Options?

Weekly options differ from conventional options in that they have a relatively short life. While the latter have terms of several weeks to several years, the term of the weeklies is only a few trading days. Weekly options are usually listed on any given Thursday and expire on the

Friday of the following week. The only time when weekly options are not offered are weeks during which “normal expiry dates” take place, in other words, weeks when standard options expire. During a trading month, there is now – instead of an option period – an expiry date of a series of options every Friday. Except for their short

period, weeklies have the same features as conventional Puts and Calls.

History of Weekly Options

Weekly options were first listed on the Chicago Board Options Exchange (CBOE), the largest US options market, in October 2005. Initially, there were only four basic underlyings for the new weekly options: SPX (S&P 500), XSP (Mini S&P 500), OEX (S&P 100), and the XEO (EUR S&P 100). All of these came with cash settlement. Again in 2010, weeklies on ETFs and on individual stocks were first introduced at the CBOE. The first shares serving as underlyings were Bank of America (BAC), Apple (AAPL), Citigroup (C), and British Petroleum (BP). Over time, more and more weeklies have been introduced by the CBOE on different underlyings – currently there are as many as several hundred. The volume of trade in these products has grown steadily. By now, weekly options constitute nearly 20 per cent of the trading volume generated by the CBOE.

Besides the CBOE, other futures exchanges have recognised the benefits of short-dated options in recent years and helped launch related products. For instance, the Chicago-based CME Group now offers weekly options on agricultural products (meat, cereals), interest-rate products (bonds, notes) and index options (S&P 500). In addition, Eurex has also included the trading of weekly options in its programme.

Why Weekly Options?

The motivation behind the listing of short-dated options may not be evident at first glance. On closer inspection, however, it is clear that there has to be more than a mere marketing drive behind the explosion in volumes, particularly in the US. So let's look at the motivation for trading short-dated options from the perspective of different market participants.

Weeklies for Writers

An integral part of all options is that the price of an option is composed of two components: intrinsic value and time value. Time value is of depreciating nature since an option with a shortening remaining term

has an ever-decreasing time value. It is especially this loss of time value that is either beneficial to many option traders (writers) or detrimental to a strategy (option buyers).

While it is known that the decline in time value begins as early as the first trading day of an option, this increases greatly in the final days and weeks. In percentage terms, for example, the decline in time value of options is significantly higher in the last 30 days of their period than, for instance, between the 90th and 60th day of their remaining term. From the writer's perspective, the advantage of weekly options is that, due to their very short term, the decline in time value is, in percentage terms, very high since the end of the option period is very near to the date of issue. That is why weeklies are quite interesting for option sellers.

Option Writing Strategy

A writer sells options in order to generate a profit from the premium received. He speculates on the price of the underlying asset (stock, ETF, future) not rising above the strike price of the option sold (for a call) until the expiry date of the option or falling below the strike price of the option sold (for a put). Option writers are, therefore, primarily interested in the decline of the time value of the options.

F1) AAPL on 15th Feb 2013

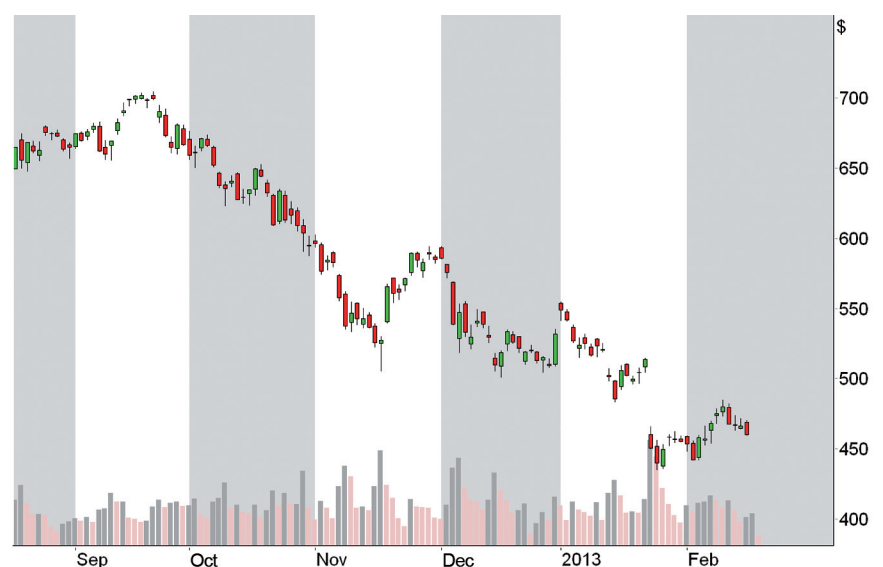


Figure 1 shows the chart of the first example described, in which a trader can decide, for example, on the sale of a weekly option or a standard option.

A Little Example Will Illustrate This

Date: 15th Feb 2013

Share: Apple (symbol: AAPL), current price 460.16 USD

Call Option Strike Price: 465 USD

Option A: Weekly option, period until 22nd Feb 2013, remaining term seven days – price 3.70 USD

Option B: Standard option, period until 16th Mar 2013, remaining term 29 days – price 11.23 USD

Both options have no intrinsic value as they are quoted “out of the money” (OTM, for short). So their price is only made up of the remaining time value.

What can a trader earn now, if he sells these calls and the value of the Apple share does not rise above \$465 until the corresponding expiry date?

Using option A, a trader can earn a total of \$3.70 over the next seven days. Since one option refers to 100 shares, this is the equivalent of \$370.

370 USD / 7 days = 52.85 USD per day

Using option B, a trader can earn a total of \$11.23 (equivalent to \$1123).

1123 USD / 29 days = 38.72 USD per day

This means that the weekly option offers traders a 36 per cent higher return a day! These are dimensions, the impact of which, is a dramatic increase in performance over the year.

This simple example demonstrates the opportunities that options sellers are offered by using weekly options.

Weeklies for Option Buyers

Buyers of options can also benefit from trading weeklies. For example, stock traders often use options to protect themselves against any risks during the release of quarterly figures. Regardless of whether a trader is long or short in the stock, the company’s figures can prompt a significant price jump upwards or downwards.

Many traders protect themselves against that by purchasing classic monthly call or put options. In doing so, though, these traders are always faced with the problem that in case of doubt they not only have to pay for the relevant time value of an option as well, but that in the lead-up to the release of quarterly figures many options are becoming particularly expensive as a result of an often incipient increase in implied volatility. The same is true of traders who hold positions in index derivatives (futures, ETFs) and want to protect themselves, for example, ahead of any central bank meetings or pronouncements by political figures.

Another example

Again, weekly options can be helpful here, as is illustrated once more with an example:

Date: 15th Feb 2013

Underlying: SPX (ETF on the S&P 500 Index) – price 1519.79 USD

Suppose a trader is long in the ETF and wants to protect himself

Exchange Ratio of Stock Options

One option always refers to 100 shares or ETFs. In the second example, a trader is assumed to have 100 ETFs, which means that the value of his position is 151,979 US dollars (1519.79 USD x 100).

F2) S&P 500 on 15th Feb 2013

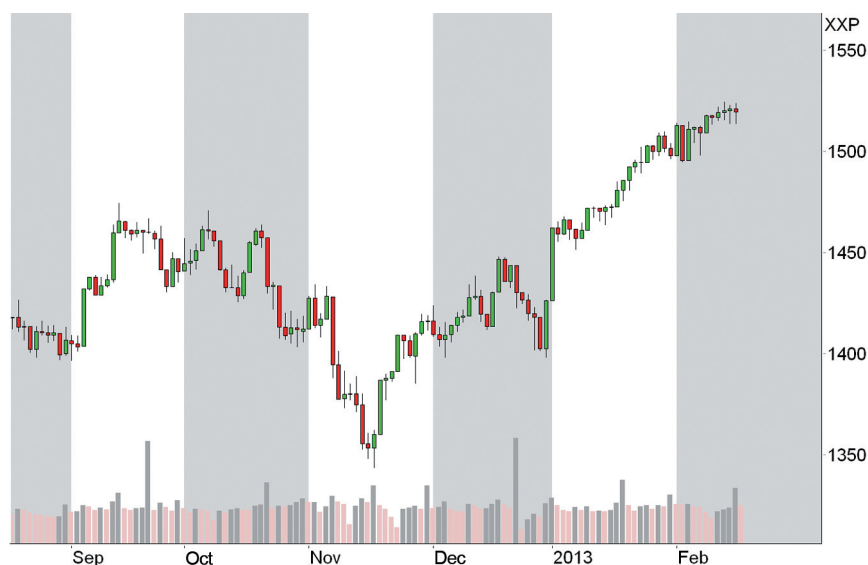


Figure 2 shows the chart of the second example described, in which a trader can decide on the purchase of a weekly option or a standard option.



By introducing weekly options, the US stock exchanges have succeeded in creating an entirely new and highly interesting opportunity to trade options.



over the long weekend – on 18th February the US celebrates Presidents' Day and US stock markets are closed. How can a trader secure short term protection against falling prices? In the example, the trader decides to buy a put option right at the money (ATM for short) at a strike price of \$1515. This means that he limits his risk to four points or 0.31 per cent in case of a price slump of the S&P 500.

Option A: Weekly option expiring on 22nd Feb 2013, remaining term seven days – price 5.60 USD

Option B: Standard option expiring on 16th Mar 2013, remaining term 29 days – price 15.40 USD

If the trader uses weekly options, he needs to pay \$5.60 or \$560 to protect his position. This represents 0.36 per cent of the overall position. However, if the trader uses the standard option, his hedging costs will amount to \$15.40 or \$1540, representing 1.01 per cent of the overall position.

Weekly options enable this trader to save more than 65 per cent of his hedging costs. This is a compelling argument for using weekly options in this particular case.

Weekly Options for Brokers and Stock Exchanges

Using weekly options usually leads to an increase in trading activity, generating more commissions (for brokers) and fees (for stock exchanges). Considering that, for example, at the CBOE sales generated by weekly options now account for nearly 20 per cent of total sales, it is clear what potential this offers to brokers and stock-exchange operators.

It is all too understandable, therefore, that by now many stock exchanges have commenced trading short-dated options. In an extreme case, this has, for example, even led to the Amsterdam-based options exchange NYSE Euronext offering daily options with a remaining term of only one day each.

Weekly Options in Europe

In the next few years, US traders will probably see weekly options developing into a well-established important trading instrument. Besides the advantages and trading opportunities arising from trading weekly options, this could also lead to a specific marketing campaign by brokers and banks as well as to a government tax regime that doesn't hurt trading.

As far as the latter item is concerned, that may pose a challenge to European traders: Should the EU governments decide to introduce a financial transaction tax, this could put a significant damper on trading short-dated options since any short term trading strategy would probably incur such a tax. However, it remains to be seen how things will be developing here since other products would also be affected by this as well.

Conclusion

By introducing weekly options, the US stock exchanges have succeeded in creating an entirely new and highly interesting opportunity to trade options. Despite the apparent drawbacks that such trading seems to carry at first glance in terms of the extra burden of fees, you should not lose sight of the many positive and profitable opportunities offered by trading these options. Active traders as well as long term investors occasionally seeking hedging opportunities by using options, will find that weekly options provide them with an exciting opportunity to get involved in the market in keeping with their respective requirements. «



Jens Rabe

Jens Rabe received his market training in Frankfurt and Chicago and had the opportunity to work, amongst other places, on the trading floor of the CBOT. He is the author of the (German-language) book, "Option Strategies for the Practical Trader – How to Secure a Steady Income on the Stock Market."

✉ www.optionsstrategien.com



Gold and the New Investing World

Game over for a Generation?

We are in a new era and the character of the market is changing as global events shaping the Dow, Nikkei and FTSE, but it is gold that investors really need to be aware of. Private investment guru Clem Chambers, CEO of ADVFN.com and author of "The Death of Wealth: The Economic Fall of the West", argues that "Interest rates are going up, bonds down, equities up, dollar up, yen down, but gold? Will it be the new era's 'Sell in May' candidate?"

» They say that no one ever criticises madness when it is working in their favour. This is why few people working in banks made a fuss before the crisis set in between 2007 and 2008.



Clem Chambers

Clem Chambers is CEO of ADVFN (www.advfn.com) and author of several books such as "101 Ways to Pick Stock Market Winners" and "A Beginner's Guide to Value Investing".

Likewise, if you criticise a stock that is flying to the moon for being too expensive, you will not be thanked. When it falls, you will be blamed too, as if pointing out a lunatic is the same as making them mad. So it is with mixed feelings that I'm watching the Dow and, to a lesser extent the FTSE, going ballistic.

It is understandable for the Nikkei to collapse and zoom, as I have previously written that there is a revolution under way in Japan. However, the post 'taper panic' rally is so strong that, even while I'm long and prospering, it leaves me a bit breathless.

Of course we are in a new era, and I've been writing as much all year, but to see the market change character is quite amazing, even if you are expecting it.



You can buy gold cheaper in a store
than they can dig it out of the ground now.



There is always a chance this is a mirage and that at any second the roof will cave in, but as I write, the Dow looks like it is going to explode. If it explodes, the implications will prove to be significant.

For one thing interest rates are going to go back to pre-2008 levels and perhaps a lot faster than expected. To keep base rates at affordable levels is going to take a lot of QE (Quantitative Easing). We will then be talking about naked monetisation rather than the tight money laundering that is currently going on between governments and their dependant banks. Currently QE is a kind of accounting trick, where banks make fortunes on free money but cover them up by vaporising their massive, but unaccounted for, bad debts. Furthermore, if interest rates rise, then governments will have to buy their bonds for cash to fund themselves and keep base rates in check. That would create another round of historic financial insanity and chaos.

The Real Cost of Gold?

The Present Situation

Meanwhile, back to the present: It appears there isn't a significant gold mine that doesn't produce enough significantly above the current price. How did that happen?

You can buy gold cheaper in a store than they can dig it out of the ground now. The rough cash price on average amongst the major gold miners is about \$1600 an ounce. For some of the big names it's over \$2000. So in practice I, Clemgold Mining Inc, can buy gold for \$1300 an ounce and sell it again and you, my shareholders, could pay me \$100 an ounce to do it and I would be a more profitable company than half of the biggest, smartest gold miners in the world. I am left wondering, if some of them haven't been doing exactly that. It would certainly explain a lot of mysteries I can't fathom. Perhaps Clemgold mining could just say, it had an aggressive hedging strategy...

Anyway, you would have thought that gold selling below the cost of production might suggest the price will rally. I think that's probably right, but in a business when miners can be credible, the value of their product go up by more than 500 per cent and they can still lose money, you have to wonder why you would play in that sandbox at all. There is a lot of gold above ground and if people get disillusioned with it, then it is game over for

a generation. Interest rates are going up, bonds down, equities up, dollar up, yen down, but gold? I was tempted to buy in August for a Santa-style rally. Gold was this year's May dump, perhaps it will be the new era's 'Sell in May' candidate?

Is There Anything New Happening in the Market?

History Repeating

On the island of Yap, limestone disks with holes in the middle were money. Yap had no limestone, but an island called Palau 300 miles away did. Getting rock back 300 miles across the Pacific in a canoe made the rock exotic and precious, just like gold is to us. Originally the rock was carved into fish shapes, but in the end the rock was carved into disks with a hole in the middle for easier carrying.

Like our modern capital, it wasn't where the money was located that was important or defined if the owner was rich or poor, it was the agreed ownership of the rock that held the key. After a transaction, say a wedding dowry or a purchase of land, the rock could be left where it sat and the owner could safely be assured that the wealth it represented was safe. Apparently this was such a strongly agreed principle that when a "Rai stone," as this money was called, fell off a canoe into deep water, it was agreed that the value was still there and could be used for future transactions. Because money was after all money and everyone knew the rock was down there somewhere in the world's ultimate vault and the value remained intact. It remained collateral in Davy Jones' safe deposit box.

In due course, a sailing ship showed up and being from a more sophisticated economy its occupants were soon helping the Yapese get more and bigger denominations of rock money. Consequently the "Rai" currency hit the inflationary skids and it is said the ship's crew did well in trade from the process.

Conclusion

Today's monetary sacred cow is gold, but just like Yap rock money inflation has also hit gold in the past. When the conquistadors started shipping the gold of the Americas back to their European motherland the impact on prices was sharp. They flooded Europe with gold and like the "Rai" its value fell like a stone. Limestone and gold are only immutable until they aren't. «



Trading Seasonalities

Part 3: Long Idea for Johnson & Johnson and Sherwin-Williams

October is known for being the month during which there will be a low in the stock market. In this issue, however, two US stocks are presented which have always averaged between five and ten per cent price rises in October. Both candidates come from the universe of the so-called "Dividend Aristocrats".

F1) Trading Idea Johnson & Johnson



The stock of Johnson & Johnson should be held in the portfolio from October 10 to November 25. In the past, the stock increased five per cent on average in that time. Also, the quarter dividend is due on November 23.

» As defined by Standard & Poor's, the title "Dividend Aristocrat" is only given to any US company that has raised its dividend 25 years in a row. This list, which on average includes just over 50 stocks, will be adjusted each year. The Dividend Aristocrats are considered to be the "kings of the stocks"; the more uncertain the economic situation is, the more important are stable yields like the dividends paid.

Trading Idea for Johnson & Johnson

The first buy candidate is Johnson & Johnson, known for its skin-care products Penaten and Bebe that have literally been everybody's companion throughout their early years; in addition, the stock is included in the Dow Jones index. The stock consolidated at a high level and

had lost ten per cent of its historical high when this article was written. An examination of the last 25 years shows a 92 per cent chance of an increase if the stock is included in one's portfolio on 10th October. The average profit in the past was five per cent, but may peak significantly higher, i.e. at up to ten per cent. The maximum increase was 10.26 dollars while the largest loss amounted to 2.84 dollars. It is recommended that the position be held until at least 25th November. In 2011, for example, there was even an increase of over 25 per cent after this date.

Figure 1 shows the formation of a downward trend as well as the time period of seasonal strength (green). The dividend yield is currently 3.04 per cent and is supported by the fact that Johnson & Johnson by now achieve more than 70 per cent of their profits in the medical field. The fact that people in industrialised countries live ever longer lives causing demand for Johnson & Johnson products to be high, has raised hopes of the dividend continuing to rise. With a direct purchase, you can probably count on collecting the quarterly dividend on 23rd November; most recently, the amount paid was \$0.66. For option traders it is recommendable to buy calls at the CBOE (Chicago Board Options Exchange). As an entry signal, you should wait for the downward trend to be broken.

Trading Idea for Sherwin-Williams

The dividend yield is not quite as high in the case of our second buy candidate. The Sherwin-Williams Company is a chemical company headquartered in Cleveland, Ohio and operating primarily in North and South America. The company, which is listed in the Fortune 500 with sales of nearly eight billion dollars and about 32,000 employees, manufactures dyestuffs, paints, and building materials that are sold in their own shops called Sherwin-Williams Paints. In 1866, the company was founded in Cleveland by Henry Sherwin and Edward Williams.

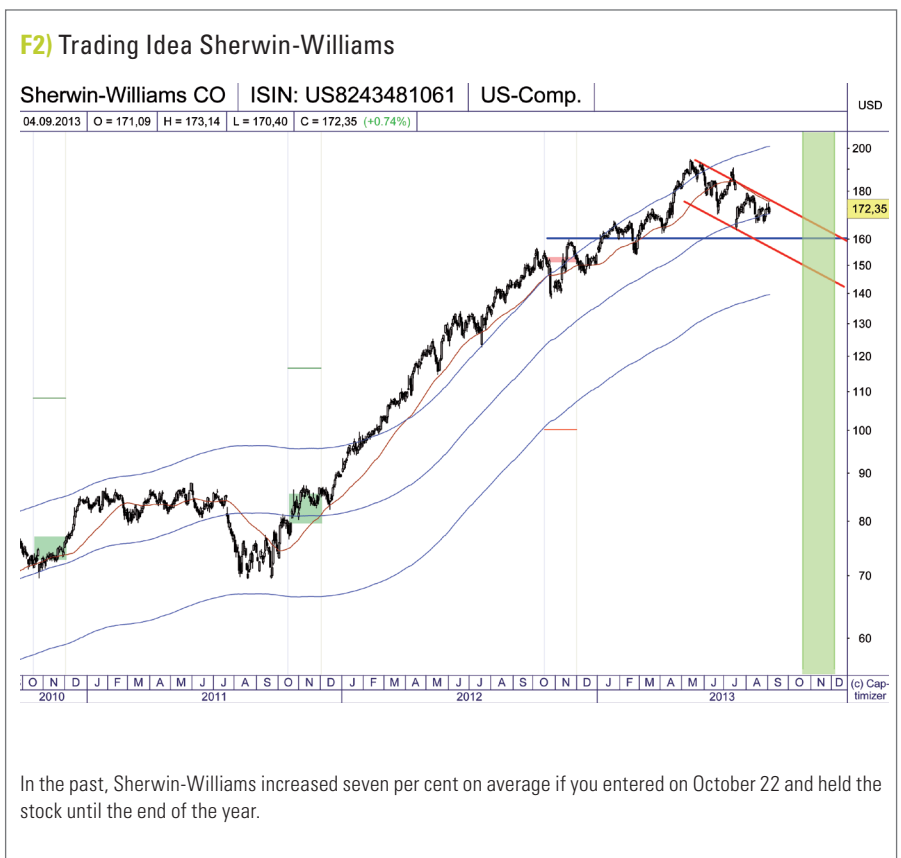
A dividend yield of 1.17 per cent means that so far there has been paid significantly less than initially announced. Nevertheless, the stock should be bought on 22nd October and held for 45 calendar days. Up

Video Update

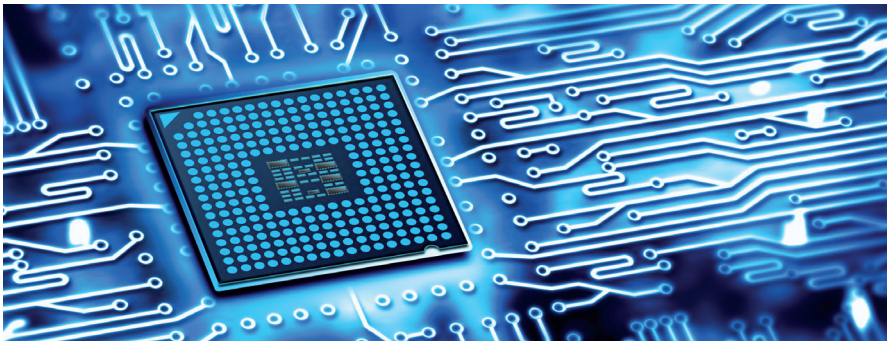
On 11th and 23rd October, you will find a video analysis of the stocks presented above in each forum of the TRADERS' website (www.tradersonline-mag.com/index.php/forum).

to 5th December, this resulted in an average profit of seven per cent, the maximum profit being eleven per cent which equals a maximum of 8.61 dollars. The average loss amounted to 2.18 dollars. The year 2012 was a special case: there was a maximum decline of eleven points before the turnaround occurred enabling the position to be closed at a small profit in early December.

Figure 2 shows the price development. The stock has lost ten per cent and is in an intact downward trend. To enter, you will again be waiting first for strength to develop. The downward trend needs to be broken first. During the holding period, a quarterly dividend of \$0.50 will be collected. Again, option traders may find what they are looking for on the US futures exchanges. In both cases, it is recommendable to purchase in-the-money options with a maturity of three months. «



ACCIDENT AT GOLDMAN CAUSES MASSIVE OPTIONS TRADES



A technical accident obviously caused a flood of unwanted options trades at the investment bank Goldman Sachs. The 17 minutes after the open at the US options exchange on 20th of August 2013 could become very expensive for Goldman Sachs: during this time the US investment bank mistakenly submitted a considerable number of options trades because of a technical defect.

Stock exchanges were informed that options on stocks with trading symbols beginning with H to L were concerned. It is completely unclear how these orders could have been executed accidentally and what the size of the damage will be. The Financial Times speculated that the damage could be more than one hundred million dollars. Goldman only stated that they did not expect a major losses and made no comment further. The bank

could absorb even a larger loss: Goldman Sachs published fabulous profits this year.

An insider attributes the false orders to a computer error. The error caused inquiries to the bank for price information to mistakenly be sent as orders to the exchanges. Experts said that it concerned options on large-cap companies like Johnson

& Johnson, JPMorgan Chase and Kellogg. The major exchanges were informed that they should check these orders. The exchanges could cancel orders retroactively or adjust prices if they were executed by mistake. But this would lead to a domino-effect because other traders who closed these errant Goldman deals down the road would also be affected. These traders often hedge trades with further trades.

A year ago a similar case stirred a furore. At the beginning of August 2012 a software-error at the US financial service provider Knight Capital Group massively disrupted NYSE when errant orders were placed for 45 minutes. Losses for Knight Capital amounted to 440 million dollars and threatened the existence of the company.

Source: www.spiegel.de

CHARLES H. DOW AWARD

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Charles H Dow Award

Since 1994, the MTA has presented the Charles H. Dow Award for excellence and creativity in technical analysis. The papers honored with the Award have represented the richness and depth of technical analysis.

The Charles H. Dow Award currently carries a prize of \$5,000.00 and is the most significant competition for recognition in the field of technical analysis. The paper or a summary may be published in the MTA's *Journal of Technical Analysis*, *Technically Speaking* e-newsletter, and posted to the MTA website.

For information on the Charles H Dow Award, please contact Ajay Jani, CMT, DowAward@mta.org.

CHARLES H DOW AWARD WINNERS	
2013	GEORGE SCHADE
2011	RICHARD BAUER
2011	JULIE DANLUBIST
2009	KEVIN LAFHAM
2010	WAYNE WHALEY
2008	STANLEY EAKINS
2009	BUFF FELZ DORMEIER
2009	WILLIAM DESHURKO
2003	GARY ANDERSON
2004	JASON GOEFFERT
2001	PETER ELIADES
2002	PAUL DESMOND
1999	ERIC BJORKSEN
2001	CHARLES KIRKPATRICK
1998	CHRIS CAROLAN
1999	STEVE LEVTHOLD

George Schade, Jr., CMT Honored as 2013 Dow Award Winner

Since 1994, the MTA has presented the Charles H. Dow Award for excellence and creativity in technical analysis. The papers honored with the Award have represented the richness and depth of technical analysis. The Charles H. Dow Award is the most significant competition for recognition in the field of technical analysis.

At the 40th Anniversary Gala Dinner, the MTA recognized George Schade, Jr., CMT as the recipient for the 2013 Dow Award.

[View a video of the award ceremony](#)

[See the 2013 Guidelines for Submissions](#)

The Market Technicians Association (MTA), a professional organisation for technical analysis practitioners and the governing body for the Chartered Market Technician (CMT) designation, announced its selection of this year's Charles H. Dow Award recipient. Selected was George A. Schade Jr., CMT, for his paper "The Repeating Story Of On-Balance Volume," on the importance of history to the technical analysis field.

The MTA has presented the Award for excellence and creativity in technical analysis since 1994. Technical analysts are invited to send submissions for next year's award, for which the submission deadline is February 1, 2014. The winning author will receive a cash prize and will be invited to present the paper at an MTA seminar or chapter meeting, and may also be published in the MTA's *Journal Of Technical Analysis*, e-newsletter, and website.

Source: <http://MTA.org>

RECORD REVENUES FOR FXCM



FXCM Inc. announced for the quarter ended June 30, 2013, revenues of \$140.1 million, compared to \$91.7 million for the quarter ended June 30, 2012 – an increase of 53 per cent. U.S. GAAP net income attributable to FXCM Inc. was \$10.1 million

for the Second Quarter 2013 or \$0.32 per fully diluted FXCM Inc. Class A share, compared to a loss of \$1.4 million or \$0.06 per FXCM Inc. Class A share for the Second Quarter 2012.

Source: www.fxcm.com

JOE GRANVILLE, WHOSE BEARISH CALLS MOVED STOCKS, DIES AT 90



Joseph Granville, a newsletter writer and technical analyst who moved stock markets with bearish calls in the 1970s and '80s, has died. He was 90.

The publisher of the Granville Market Letter since 1963, Granville predicted the Dow Jones Industrial Average's slide in 1977 to 1978 and the end to the surge in computer-related shares in 2000. He was wrong in 1982 and 1995 when he called for losses before stocks rallied.

Granville used criteria such as trading and price patterns rather than more commonly analysed data. He started developing his own stock-market theories at what was

then E. F. Hutton & Co., a New York-based brokerage, from 1957 to 1963. By 1981, Granville was influential enough to spur a market slump. That January, he sparked a 2.4 per cent one-day decline in the Dow average by advising his subscribers, "Sell Everything!"

Granville's main stock indicator was On Balance Volume (OBV), which he developed. He also followed charts that tracked investor sentiment, the number of stocks reaching 52-week highs and lows, and the daily number of advancing and declining stocks. He compiled the measures into what he called his "Net Field Trend Indicator," used to predict the market's direction. "Everyone is following the economy. I'm following the market," Granville said in an October 2006 interview. "I'm the exact opposite of Wall Street."

Source: www.bloomberg.com, written by Nikolaj Gammeltoft

GOLDMAN SACHS, VISA & NIKE SET TO JOIN THE DOW JONES INDUSTRIAL AVERAGE

Recently, we've seen a major change in the Dow Jones Industrial Average (DJIA) index composition. The Goldman Sachs Group Inc. (NYSE:GS) has replaced Bank of America Corp. (NYSE:BAC), Visa Inc. (NYSE:V) has replaced Hewlett-Packard Co. (NYSE:HPQ), and Nike Inc. (NYSE:NKE) has replaced Alcoa Inc. (NYSE:AA) in the DJIA effective Monday, September 23. The index changes were prompted by the low stock price of the three companies slated for removal and the Index Committee's desire to diversify the sector and industry group representation of the Index.

Such changes don't cause any disruption in the level of the Index. The divisor used to calculate the DJIA from its components' prices on their respective home exchanges will be changed prior to the opening on the date of the change. This procedure prevents any distortion in the DJIA's reflection of the U.S. stock market.

Source text: www.djindexes.com; Source table: Wikipedia

New Composition of the Dow

3M1	Intel
American Express	Johnson & Johnson
AT&T3	JPMorgan Chase & Co.5
Boeing	McDonald's
Caterpillar	Merck & Co., Inc.
Chevron	Microsoft
Cisco	Nike
Coca-Cola	Pfizer
Disney	Procter & Gamble
DuPont	Travelers
ExxonMobil4	United Technologies6
General Electric	UnitedHealth
Goldman Sachs	Verizon Communications
Home Depot	Visa
IBM	Wal-Mart



INDIA ATTEMPTS TO **STABILISE THE CURRENCY**

The Indian rupee slumped to a record low of less than 69 to the dollar, its worst performance since 1995, on growing worries that foreign investors will continue to sell out of a country facing stiff economic challenges. An assault on the psychologically significant 70 level appears imminent, as intervention from the central bank seen recently

gave the rupee only a brief respite. Policy makers have consistently struggled in recent weeks to come up with steps that can convince markets they can stabilise the rupee and attract funds into the country despite extraordinary measures last month by the central bank to drain liquidity and action to curb gold imports, while attempting to cut India’s huge oil import bill. If steps are not taken to implement the reforms necessary to tackle the structural issues, the government will be left with the so-called “3D options”: debt default, devaluation, deflation.

Source: www.theguardian.com/business

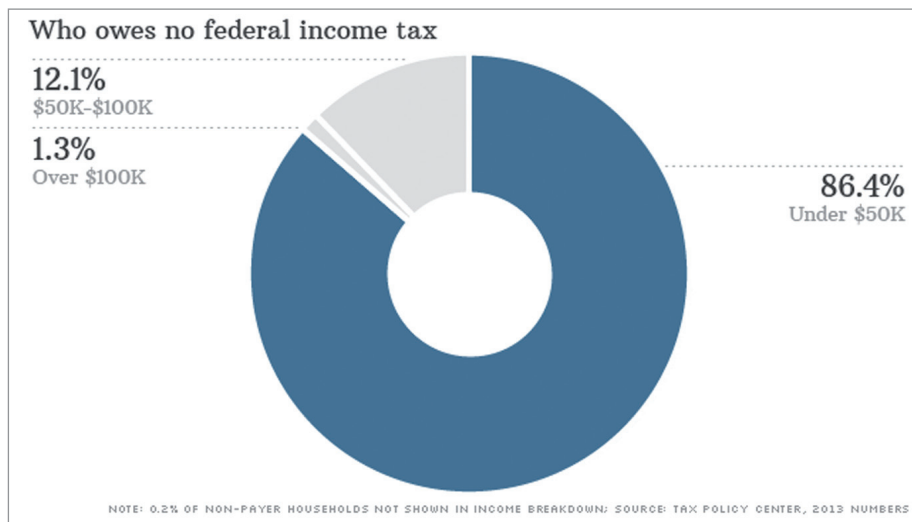
CHINA TRADING ERROR REDUCES INVESTOR CONFIDENCE IN STOCKS

The biggest swing in China’s benchmark equity index since 2009 threatens to further erode confidence in the nation’s stock market after it lost more money for investors than any in the world during the past four years. China’s shares were roiled August 16 by a trading error at Everbright Securities Co that spurred a 53 per cent surge in volumes and a swing of more than six per cent in the Shanghai Composite Index. The MTM loss

was about 194 million yuan (\$32 million). The company blamed a flawed arbitrage trading system and it used its own funds and liquidated some securities holdings to ensure clearing. The China Securities Regulatory Commission has decided to investigate the brokerage. No human operational errors were detected in Everbright Securities’ trading on August 16.

Source: www.bloomberg.com

IMPROVING US ECONOMY DOES NOT **NEED MORE TAXES**



A little more than 43 per cent or 70 million US households will end up owing no federal income taxes for 2013. That’s down from recent years because of an improving economy and the expiration of various tax cuts that were passed after the 2008 financial crisis. The households with zero income tax liability are not evenly distributed across income groups. The majority this year – nearly 67 per cent – have incomes below \$30,000. Specifically, an estimated 798,000 households in the nonpayer group

make between \$100,000 and \$200,000 a year; 48,000 have incomes between \$200,000 and \$500,000; 3000 make between \$500,000 and \$1 million; and 1000 households bring in more than \$1 million.

By Jeanne Sahadi; Source: www.money.cnn.com

worldoftrading²⁰¹³

WORLD OF TRADING 2013

In November 2013 the World of Trading – the greatest expo for trading and finance in Germany – will take place again in Frankfurt. With over 50 speakers and nearly 60 exhibitors the World of Trading has never been bigger. The expo starts with the Pre-Conference on the 14th of November, where well-known traders show their market-skills during live trading and seminars. On the 15th and 16th of November the expo offers many opportunities for traders to expand their knowledge in trading and meet national and international experts, like Abe Cofnas, Ronnie Chopra and John Person. Brokers, banks, publishers as well as software and hardware providers offer new products and services. On Friday, every attendee can visit the Great Live Trading Event with many pro traders.

English speaking visitors shouldn't miss these dates:

Thursday, 14th November – “Live Trading” with David Furcajg and Birger Schäfermeier.

Friday, 15th November – 9:30am-11:30am, 2pm-3pm, 5pm-6pm, “Great Live Trading Event” with Abe Cofnas, Orkan Kuyas, David Furcajg and many more.

Friday, 15th November – 4pm-5:40pm, Seminar with John Person.

Saturday, 16th November – 12am-1:40pm, “Trading Binary Options: Strategies and Tactics” with Abe Cofnas.

Saturday, 16th November – 2pm–2:40pm, “Learning High Probability Trading and Execution Tactics” with Rob Hoffman.

Saturday, 16th November – 4pm–4:40pm, “What Economic Data/Fundamentals are important to Forex markets and where are the current trading opportunities?” with Ronnie Chopra.

Save the date and visit the World of Trading on 15th and 16th November 2013!

More info: www.wot-messe.de

MF GLOBAL – WHERE IS THE MONEY?

The CFTC (Commodity Futures Trading Commission) intervenes in the case of the bankruptcy of MF Global and files a lawsuit against the company, the company's manager Jon Corzine and the deputy chief financial officer Edith O'Brien.

According to the prosecution clients' money amounting to 1,2 billion Dollars were used for financial transactions concerning purchases of European government bonds. Based on recorded telephone calls and emails a mess of transactions of clients' and companies accounts was exposed. For example large amounts of money were transferred to the Bank of New York Mellon (BONY) based on O'Briens orders. There are separately defined clients' accounts at the BONY in addition to the company's own accounts. O'Brien reportedly answered the inquiries of the BONY, if the transfers satisfy the regulations of the CFTC, with the statement, that supervision is not necessary. The prosecution states furthermore, that the MF Global violated the company policy by spending more money than available on the company's accounts. According to the records Corzine had this information but nevertheless gave the orders of the transactions. Therefore money of the separated clients accounts were used to keep up the liquidity of the company.

He simply does not know where the money is, said Corzine in his witness statement in front of the committee. He was stunned that the MF Global could not pay the hundreds of millions of dollars of their clients. The chief financial officer O'Brien on the other hand stayed silent. The bankruptcy of the MF Global is the eight largest of the US history. Corzine wanted to turn the company into an investment bank with a proprietary trading department. But the company gambled with European government bonds and had to file bankruptcy in 2011. About 1000 employees lost their jobs. During the investigation it showed that 1,2 billion dollar of clients money was missing. Therefore the CFTC intervened. The CFTC regulates the futures and options markets as an independent authority in the USA. The regulations of the CFTC indicate that clients' accounts and the company's accounts have to be kept separately. The access to the separate accounts is forbidden. Therefore the CFTC filed a lawsuit against MF Global.

Now the employees are questioned if the statement of Corzine is true. But still nobody knows where the money is.

Source: Futures Magazine



NEW PRODUCTS



WEBREVIEW



SOFTWAREREVIEW



BOOKREVIEW



APPVIEW

Letters to my Broker

**P.S. What do you think of the Market
by Clem Chambers**

» Living and trading in the 21st Century can make you feel like you are living in a new age. Trading via our phones, live streams, Level 2 and the world's markets dominated by bots – we've come a long way since the world before the Wall Street Crash.

Or have we? A famous stock market book "Letters to My Broker", written in 1920 by A. Kustomer recently republished by ADVFN Books with new material from Clem Chambers, is packed with market insight, not just for prohibition-era New York but also for today.

A Modern Satire

The amazing thing about this pre-crash book is that it is so fresh and so relevant. It could almost be a modern satire. It would seem impossible that a 90-year-old book could be relevant today and contemporary that it feels like it should be a modern hoax. But human flaws and characteristics don't really change. Technology may have advanced, but it's debatable whether we have!

Can so very little have changed since 1920 that you can appreciate Joe's, the lead character, letters to his broker as, if they were emails sent from a smartphone?

About the Author

Clem Chambers is CEO of ADVFN (www.advfn.com) and author of several books such as "101 Ways to Pick Stock Market Winners" and "A Beginner's Guide to Value Investing".

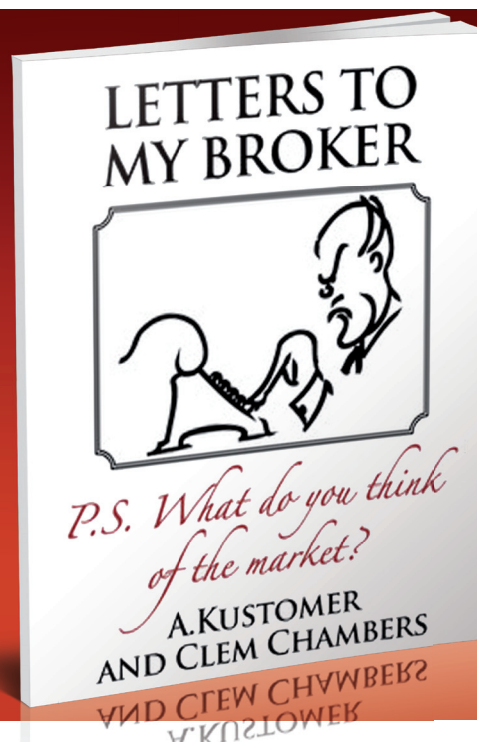
But "Letters to My Broker" is no hoax. This book, which catalogues the out of control behaviours of a trader, is a record not of today's market gamblers but of a speculator from just after World War I ended. It's a different world from today's high tech one, but not, it seems for the trader.

For all the online trading technology, the overarching regulation, the thousands of educational books on investing, traders behave now exactly as they did 94 years ago. What is more, the results, losses and how they occur seem unchanged. It is like some steam-punk fantasy, without the fantasy.

The Muppets

It is perhaps the wicked way the author sends up himself (or perhaps his customers) with pinpoint accuracy that drew me in, or perhaps, like all great satire, it was the way it strips away pomposity and humbug to reveal the sorry truth, which hits my funny bone. Yet it is not the humour wherein the value of this book lies. It lays out the behaviours that cost so many novice investors and would-be traders so much of their hard earned capital. These losses were real then and are real now. They are as significant as they are unnecessary.

Goldman Sachs employees have been known to call their clients "muppets," which translated in trader speak means clueless participants. In the markets, clueless participants are lambs to the slaughter. Trading is a game of winners and losers and muppets don't stand a chance.



Letters illuminates this and Clem Chambers' modern additions and commentary give an insight into the mistakes of the novice.

It's hard to start in the market and not be such a lamb to the slaughter, but this book gives you a master class in how muppets behave and what can happen to them. Novice and experienced investors can all benefit from this master class.

The Same Traps Now and Then

In the City of London, I recently saw a banner outside a poker room. It read, "Beginners welcome." That was also surely the case in 1919. It doesn't need to be like this, but as this book shows, for the last 100 years at least, private investors have been falling into the same traps.

Joe, the book's protagonist, is a wealthy man, but his Wall Street dealings aren't going the way he planned. Driven by the excitement of trading and the lure of easy money he is prepared to constantly come off on the wrong end of the deal, chasing the illusory market killing.

He also isn't a tragic figure, not at all. He is a man who will never starve. He has skill, determination and smarts. He has built a small fortune in the rag trade. If he loses his shirt he can sew another. Yet somehow he can't get to beat the street and instead takes a thumping from the market time and again. He is not a quitter, he is not sorry for himself, not for a New York minute.

This is New York in 1919. There is no safety net. There is no regulator. There are no insider trading rules. Wall

Bibliography

Title:	Letters to my Broker
Subtitle:	P.S. What do you think of the Market
Authors:	Clem Chambers
Pages:	132, Paperback
Price:	£ 8.74
ISBN:	978-1908756190
Release:	June 2013
Publisher:	ADVFN Books

Street is the Wild West, and meanwhile the Wild West is also still the Wild West. There is no one to go crying to if you lose; there is no social safety net. If you get ruined, you get ruined.

The Short Life Trader

Yet for all the difference in times and safeguards, Joe behaves like any iPhone wielding day trader punting today on Pink Sheet stocks in New York, AIM in London or Mothers in Tokyo. While generations have come and gone and the world has changed dramatically, the psychology, behaviour and fate of the "short life trader" has been left untouched. This is a book to laugh with and to learn from. «

Robbie Burns, author of "The Naked Trader"
(www.nakedtrader.co.uk)



The Rebound-Strategy

How to Find Favourable Entries

Simple strategies can be as successful as complex ones – often they are even more successful. This rebound strategy is ideal for traders who do not want to work with indicators or complex trading strategies.

» If a stock is in a clear trend chances that the trend continues is greater than chances of a reversal. In these trends exaggerations and/or understatements of the fair fundamental value of a stock develop. If a stock would always be traded at the fair intrinsic value, there would be much less volatility because the real worth of a company does not fluctuate very much in the short term.

Take the example of Volkswagen (Figure 1): The stock dropped 40 per cent from July to October 2011 and then nearly doubled within a year. If it was a rational price development, there would have been a steady increase as Volkswagen published increasing profits and therefore the value of the company should have increased accordingly.

If you search for rebound-candidates you should be aware that sell-offs often develop based on the exaggerated emotions of market players.

The Strategy

Now let's take a closer look at the details of the rebound strategy:

1. Flop-Screening

If you want to profit from exaggerations on the stock market, search for "stock-flops" with the help of a top/flop-screener. You can find such a screener if you enter "top/flop-stock-screener" in a search engine. For example, you can do flop-screening with the components of all major indices. If you screen foreign indices, you should always look at the chart of the stock exchange where the particular stock is listed.

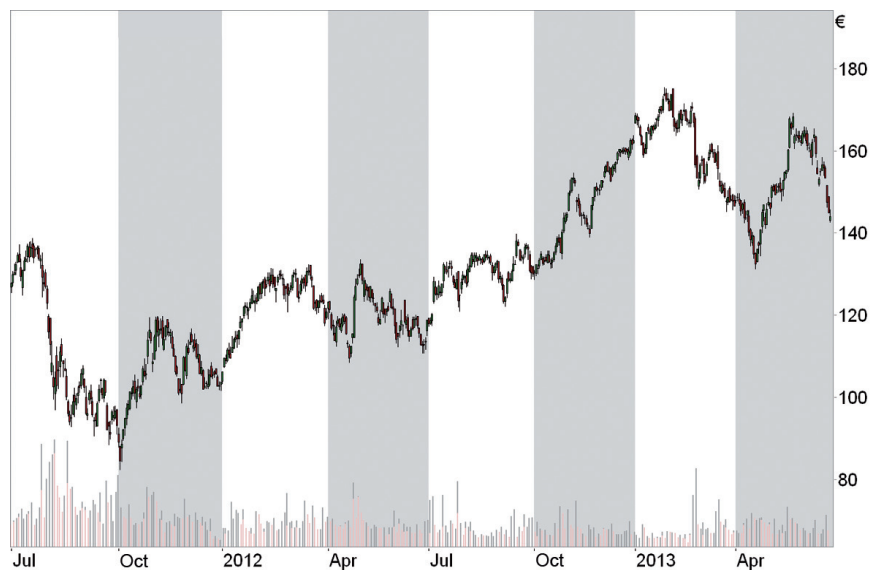
You should also take the daily volume of the underlying stock into consideration. Some stocks will have a trading volume of less than 100,000 Dollar. In this case you are at a disadvantage – the bid/ask-spread may be high and in the worst case you can sell your stocks with high slippage only due to low trading volume. Therefore you should only trade stocks with high volume in order to improve your results.

We recommend three months as a screening-period, but of course you can also use smaller or larger time frames. In general you should mainly look at the ten per cent that have dropped the most. The next step – technical analysis – is the analysis of stocks that have decreased during this period of time.

2. Setup

The individual flop-stocks have to fulfil at least two criteria to be acceptable for a buy (we use candlestick charts):

F1) Volkswagen 2-Year Chart



The chart shows the meaning of primary trends that develop based on emotional trading. If market participants would only trade based on fundamental data (Key word: homo economicus) there would not be such drastic selling and buying.

- The stock developed at least two daily candles in a sideways movement after a downtrend (bottom).
- A horizontal support-line in the daily chart.

F2) Top/Flop-Screener

comdirect

Home > Informer > Aktien > Top-/Flop Listen

Index und Zeitraum wählen
 Index: MDAX Zeitraum: 3 Monate Anzeigen

Treffer [50 Treffer] Seite: 1 2

Name	Aktuell	3 Monate	Datum Zeit	Volumen	Branchen
KLOECKNER & CO SE NAMENS-AKT...	8,595	-24,37%	21.06.13 01:00		k.A. Sonstige Handel
SALZGITTER AG INHABER-AKTIE...	25,99	-23,57%	21.06.13 01:00		k.A. Eisen / Stahlindus..
SUEDZUCKER AG INHABER-AKTIE...	25,50	-21,66%	21.06.13 01:00		k.A. Nahrungsmittel
SGL CARBON SE INHABER-AKTIE...	25,685	-18,19%	21.06.13 01:00		k.A. Spezialchemie
BILFINGER SE INHABER-AKTIE...	70,38	-13,13%	21.06.13 01:00		k.A. Dienstleistungen
HOCHTIEF AG INHABER-AKTIE O...	47,35	-12,80%	21.06.13 01:00		k.A. Bauhauptgewerbe
DEUTSCHE WOHNEN AG INHABER-A...	12,76	-12,36%	21.06.13 01:00		k.A. Immobilien
AURUBIS AG INHABER-AKTIE O.N.	45,185	-12,25%	21.06.13 01:00		k.A. Metallverarbeitung
PUMA SE INHABER-AKTIE O.N.	215,60	-11,06%	21.06.13 01:00		k.A. Sportartikel
GERRY WEBER INTERNATIONAL AG...	31,475	-9,99%	21.06.13 01:00		k.A. Bekleidungsartikel
HANNOVER RUECK SE NAMENS-AKT...	55,83	-9,95%	21.06.13 01:00		k.A. Versicherungen
TAG IMMOBILIEN AG INHABER-AK...	8,275	-7,13%	21.06.13 01:00		k.A. Immobilien
GSW IMMOBILIEN AG INHABER-AK...	29,02	-7,06%	21.06.13 01:00		k.A. Immobilien

The top/flop-screener shows the weakest stocks of the German DAX, sorted in descending order of losses for the past three months.

Strategy Snapshot	
Strategy name:	Rebound Trading
Strategy type:	Countertrend, long only
Time frame:	Daily chart
Setup:	long: At least two consolidation-candles after a sell-off and bottom building at an important technical support level
Entry:	At open of the following day, if open > close
Stop-loss:	0.1 % below support line resp. below low of the past two candles
Take profit:	first profit-target: twice the initial risk; second profit-target: four times the initial risk
Trailing stop:	After the first profit target was reached the stop for the remaining position is placed at break even
Risk- and money management:	0.5 % per trade
Average number of signals:	Depending on the number of underlyings

If you wait for the bottom to build, you increase the hit rate for rebound trades. But if you buy when the stock is still in a clear downtrend, the risk that the stock will continue to fall is high. You should always think of the well-known saying “never catch a falling knife” and act accordingly.

Large institutional investors often use phases of bottom-building to buy and further accumulate stocks at every drop in price. Institutions have to enter large position sizes over several days and weeks and therefore the potential downtrend can reach enormous momentum.

3. Entry

If the downtrend of a stock was slowed down by a consolidation of two consecutive days at a support level, you can buy the stock on the third day as long as the open is higher than the close of the last two days. You should wait for the actual open of the market to place your order as there are considerably higher ask/bid-spreads pre-market.

4. Exit in Case of Loss

A basic part of a trading strategy is to define the stop-loss before entering a trade. The stop-loss should be placed 0.1 per cent below the support area that is characterised by the support line and the past two daily candles in a sideways movement. If the low of the past two days is at or slightly below the support-line you place the stop at 0.1 per cent below this daily candle. But if the support line is below the low of the past two daily candles, you place the stop 0.1 per cent below the support.

The risk per trade is 0.5 per cent of trading capital. Therefore an initial stop of two per cent below the entry means you have a position size that equals 25 per cent of the entire trading account. You can calculate the position size as follows:

$$\text{Position size} = 1 / (\text{initial stop in \%} / 0.5) * \text{total trading capital}$$

5. Exit in Case of Profit

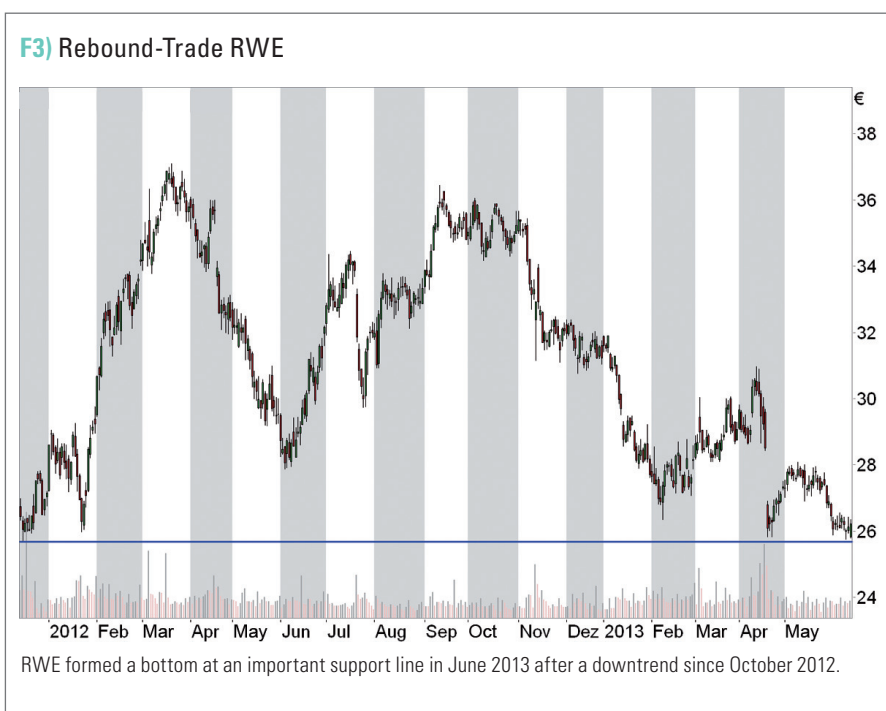
We take half of the profit as soon as we earned twice the initial risk. We let the second half run until it earned four times the risk. This way you avoid getting upset about closing the whole trade too early and at the same time you maintain a very good risk/reward ratio (RRR). As soon as the position reaches the first profit target, the initial stop for the remaining position is placed at break-even.

Examples

Two examples illustrate the rebound-strategy:

Example 1: RWE (Figure 3)

Following a period of strong losses RWE has consolidated by the beginning of July 2013 at a major support line. The entry criteria (bottom-building of at least two days) has been fulfilled. A



higher open on the following day triggered the long-entry. We assume that the last candle closed at 26 EUR. The entry is executed the following day, provided the open is above 26 EUR. The support line is below the lows of the last two candles, therefore the stop is placed 0.1 per cent below the support line. In our case the stop is placed at 25.62 EUR – that is, 0.38 EUR or 1.5 per cent below the entry. The first profit target for half of the position is at double the initial risk ($2 \times 0.38 \text{ EUR} = 0.76 \text{ EUR}$) at 26.76 EUR. After this profit target is reached, the stop is placed at break-even. The second profit target is at four times initial risk ($4 \times 0.38 \text{ EUR} = 1.52 \text{ EUR}$) at 27.52 EUR. We still assume that the entry is executed at 26 EUR; if the entry is higher, the profit targets have to be calculated accordingly.

The next step is calculating the position size. We assume that total trading capital is 100,000 EUR:

Position Size = $1 / (\text{initial stop in \%} / 0.5) * \text{total capital} = 1 / (1.5 / 0.5) * 100,000 = 33,333 \text{ EUR}$

We will risk about 0.5 per cent of the trading capital or 500 EUR for this trade.

Notice: On the 20th June RWE would have been stopped out after the DAX dropped heavily following the announcement of the results of the Fed meeting on 19th June. This shows that an initial stop is very important. You should not use mental stops, but you should enter the stops as soon as you place a trade. Nobody can watch the markets at all times and sudden price drops can be painful and expensive if you only use mental stops.

Example 2: Suedzucker (Figure 4)

In September 2009 the stock screener filtered Suedzucker, a Bavarian sugar refiner. We see that a bottom formed at a support line with two horizontal daily candles at the end of September. But there was no higher open the next day. Only on the following day (fourth day) was the entry executed because the open was above day 2's close. If Suedzucker had dropped below the support line on the third day, the entry on day 4 would have been obsolete. The stop was placed 0.1 per cent below the support at 13.30 EUR at 13.29 EUR. After the entry at the open at 13.50 EUR on the third day the price target at 13.92 EUR and the second profit target at 14.34 EUR was reached.



Sebastian Ritsert

20 year old Sebastian Ritsert, is a bank clerk and has been studying stock markets since he was 16. He has already developed several investment strategies using different time frames. He plans to become a funds manager or trader after he completes his business degree.

✉ Sebastian.ritsert@web.de

Opportunities for Improvement

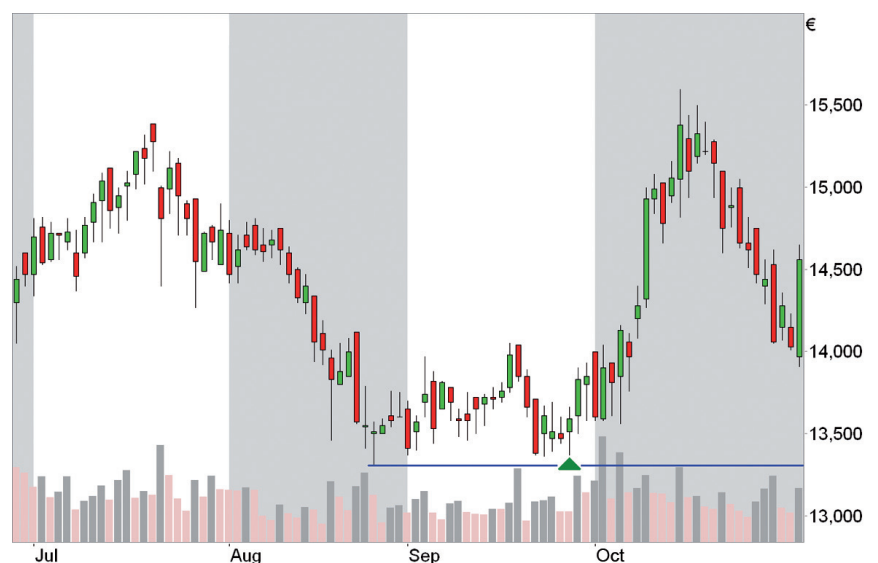
You can improve your hit rate with the following entry criteria:

- Entry only at bottom-building at important price levels, for example whole numbers like 50 or 100 EUR.
- Entry only if the stock opens on the third day with an up-gap (after two days of consolidation).
- Buying power exceeds selling power considerably in the order book.

Conclusion

Simple strategies can be successful. Even beginners can recognise a bottom-building at a support line. Beginners especially, can use this rebound strategy to start developing their own trading methods. «

F4) Rebound-Trade Suedzucker



Bottom-building at support at the end of September 2009. Two days later there was an entry signal (see green arrow).



Make Use of the Symmetry of the Market

Trading the Scene of the Crime

F1) Breakout



Locate a stock or commodity that has broken out of a consolidation pattern for the first time.

One of the simplest techniques revealed by reading the charts which many traders overlook, is the “institutional accumulation” and “distribution area,” better known as the “scene of the crime.” In this article, Nick Santiago will show you how to trade that setup.

» Technical analysis based trading is primarily focused on putting the odds in favour of the trader through use of reading charts. As a short term trader or an investor, you must make sound decisions which when implemented properly, will reveal the best chance of making money. In other words, become the house not the gambler. You need to position yourself like Steve Wynn of Wynn Resorts, not the guy sitting on the other side of the blackjack or roulette table. Steve Wynn knows the longer someone gambles at his

casino, the more money someone will lose. As a trader, you need to be confident that the more trades you take, the greater the odds are in your favour, not the other way around. You do not want to gamble or take unnecessary risks, that is the opposite of what successful traders do. Trading is all about putting the odds in your favour; this simple technique I am about to discuss will help guide you to the path of being the house and not the gambler.

One of the simplest techniques revealed by reading the charts which many traders overlook, is the “institutional accumulation” and “distribution area,” better known as the “scene of the crime.” When analysing the chart of a stock, you will notice this pattern play out often. Here is what you need to look for to find the scene of the crime:

F2) Pullback



When the stock returns to the area where it broke out, that will now be a good support level for a bounce.

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» Technical trading is all about putting the odds in your favour. «

Strategy Snapshot	
Strategy name:	Scene of the Crime
Strategy type:	Pullback trade
Time horizon:	Daily chart
Setup:	First breakout from a consolidation pattern, stocks holds higher (lower for short trades) for at least 7 days, pullback to the breakout level
Entry:	At the initial breakout level
Stop-loss:	Below last lower Pivot (higher Pivot for short trades)
Take profit:	Measured Move from breakout level, distance to be added = breakout - lowest low in between (highest high for short trades)
Trailing stop:	None
Risk and money management:	1-3% risk per trade

1. Locate a stock or commodity that has broken out of a consolidation pattern for the first time, (a breakout is when the stock has moved either higher or lower from the consolidation point or period, as noted in Figure 1).
2. After breaking out of the consolidation area, the stock then trades higher (or lower in the case of shorting) then moves back to the breakout area where the stock was consolidating. When the stock returns to the area where it broke out, that will now be a good support level for a bounce.
3. The key is to make sure that the breakout from the consolidation area lasted for at least seven bars in the particular time frame you may be using. If the breakout was less than seven bars and price reverts

back to the consolidation area, the odds of the "scene of the crime" holding as high probability support will decrease significantly. In the JPM example, take note of the +7 bar move above the scene of the crime level, and the large bounce that occurred after it returned to that level in the chart here.

Remember, technical trading is all about putting the odds in your favour; entering this trade only when the breakout lasted for at least seven bars will help increase your odds.

Trade Strategy Example

In this chart example, traders can look to buy JPM at the scene of the crime level which is around the \$51.00 area. As you know, all trades can fail. Therefore, keeping a stop-loss at a close below the daily chart \$50.00 level would be prudent. This stop area was the last Pivot or pause in early May before the breakout



» Start to learn how to read the charts and profit from the markets. «

above the scene of the crime resistance level at \$51.00. The upside target would be around \$56.00, so the target would be near the \$56.00 level.

Here is how you would calculate the profit target; simply take the last major low Pivot, which in this example is mid-April around \$46.00, and calculate the distance (or difference) to the scene of the crime resistance level at \$51.00. This gives you roughly five points of upside for the target. It is always important to note that stocks, commodities, and most equities are all very symmetrical. Therefore, you can apply this same rule to different trades, all things considered.

Conclusion

The “scene of the crime” technique can be used on all time frames. The same rules of this technique can be applied for finding resistance levels and potential short-trade setups as well. When looking for a short-entry point based on this technique, follow the same principles, just in reverse. Take careful note of where price consolidated then broke down. The point where the stock broke down will be good short term resistance.

It is always beneficial to have extensive knowledge in technical charting to enhance the odds of any trade. Remember, technical trading is all about putting the odds in your favour when entering a position. Start to learn how to read the charts and profit from the markets. «

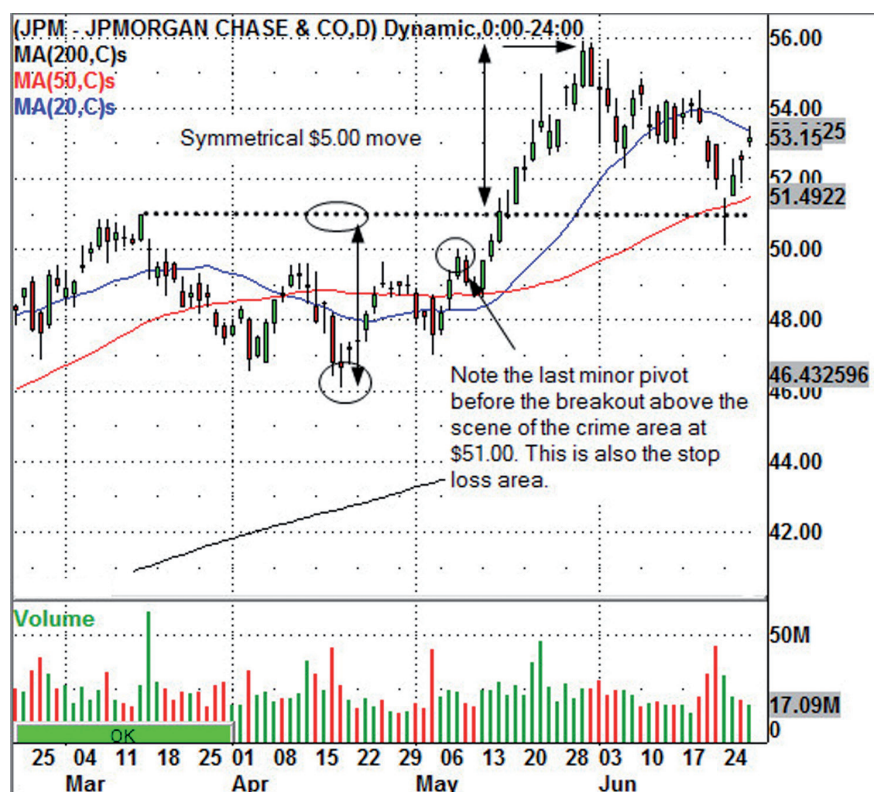


Nicholas Santiago

Nicholas Santiago is President & CEO and Chief Market Strategist at www.InTheMoneyStocks.com. He started trading in 1991. He successfully managed money for a large, affluent private client group. In 2007, he partnered with Gareth Soloway to realise his dream of educating others about the truth of the markets.

✉ www.InTheMoneyStocks.com

F4) Trade Management



A good initial stop would be at the last lower Pivot. As for a profit target, you can use the distance from the Scene of the Crime level to the lowest point in between, and add that to the breakout level.



The ABC of Gap Trading

How to Trade Gaps Profitably

Gaps are events that keep giving traders food for thought and encourage them to speculate. If gaps are considered in terms of their importance within the current trend, they will provide valuable insights that are of benefit to chart analysis and, if necessary, to trading setups that can be used immediately.

» Definition of Gaps

A gap on a daily basis in the classical sense is characterised by the current day's trading range being outside the previous day's trading range. In an upward gap, therefore, the current day's lowest price is above the previous day's highest price, whereas in a downward gap the current day's highest price is below the previous day's lowest price. In candlestick charts,

gaps are known as so-called "windows". A downward gap is a "falling window", an upward gap a "rising window".

Psychologically speaking, gaps are based on the changed perception of market participants which leads to a reassessment of the current price level. This is immediately reflected in the opening price of the new trading day. If this is within the trading range of

the previous day but differs from the closing price, this is called a partial (opening) gap. However, if the opening price is outside the trading range of the previous day, we speak of a real or full (opening) gap. If this opening gap is not or not completely filled by the end of the trading day, a gap will be left on the daily chart.

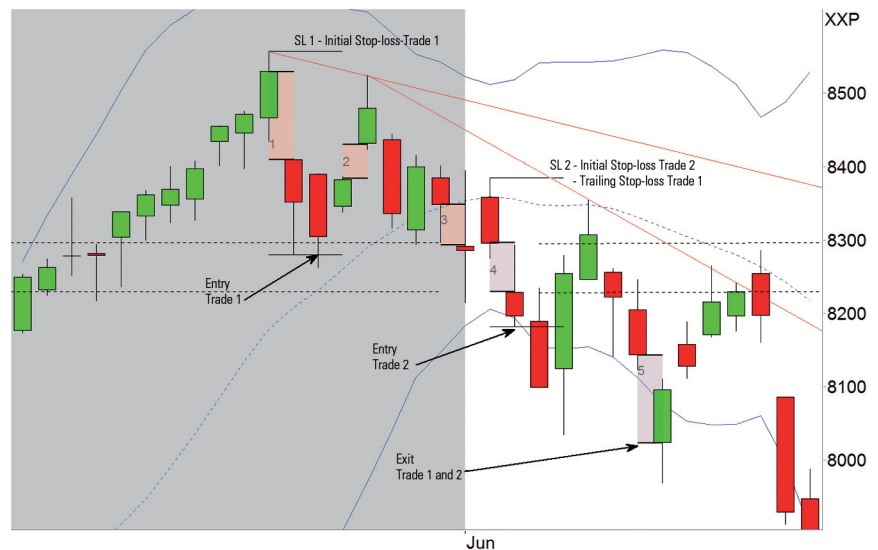
Preliminary Considerations

Based on an analysis of past price performance, the correct interpretation of the resulting gap is to be used to trade a newly emerging trend. Ideally, this movement begins with a breakaway gap, is followed by a continuation gap and concludes with an exhaustion gap (see info box).

Each gap begins with an opening gap at the start of trading. But at this point in time it is still impossible to determine whether the opening gap will continue to exist until the end of the trading day and what type of gap will be formed. A meaningful assessment of the constellation of the chart will not be possible until the end of the trading day since the volume data will also be available by then.

Because of the sudden change in the sentiment of market participants, gaps represent important support or resistance zones. Technically, the latter cannot be considered to be broken until they are overcome by the closing price. Thus, a pullback into a gap that cannot be held by the closing price is a confirmation of the significance of this gap. However, such a pullback may occasionally overshoot the gap. In that case a stop-loss at the "inner" boundaries of the gap is in danger of being triggered by an intraday pullback. Consequently, only the highest or lowest prices of the candles surrounding the gap are suitable levels for entry and stop-loss points.

F1) DAX Daily Chart with Gaps

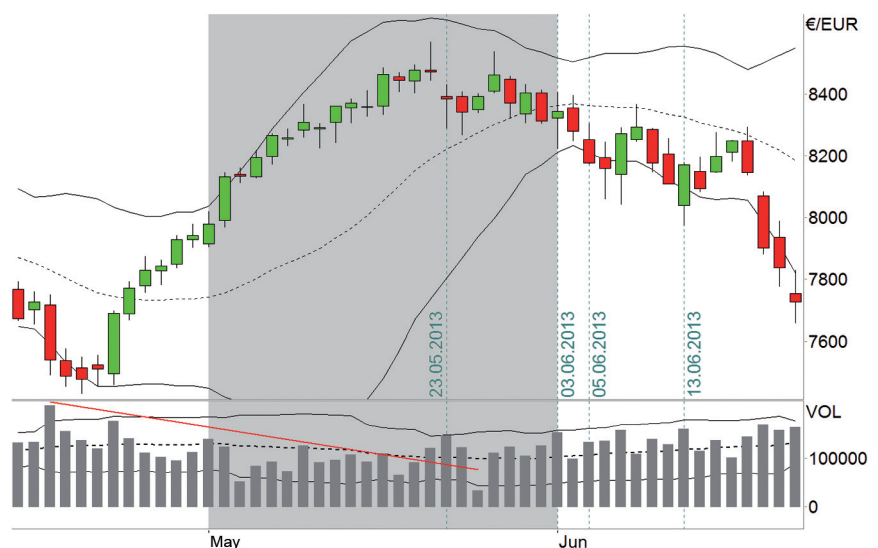


The gaps described in the text are shaded grey and are numbered. The range of the continuation gap (Gap 4) has been moved to the past and the future. Here you can easily follow the way a resistance zone evolves from a support zone. There was a "polarity change" at this level.

The Strategy in Practice

We will be using the DAX (Figure 1) as an example. Since analysing gaps also requires volume to be included, volume data from the DAX future (Figure 2) will be drawn on. Starting from the low on 19th April 2013, the DAX reached a new all-time high on 22nd

F2) FDAX Daily Chart with Volume



Guide lines are used to mark the gap days since the FDAX gaps are not as pronounced because of the longer trading hours. Volume is shown in the subchart. Price and volume are given a 20-day Bollinger Band. Volume peaks are clearly visible on the days of the breakaway and exhaustion gaps.



Because of the sudden change in the sentiment of market participants, gaps represent important support or resistance zones.



Overview of Types of Gaps

Breakaway Gap

Breakaway gaps appear after a completed price pattern and signal the start of a strong movement. They are often associated with high volumes.

Continuation Gap (Runaway Gap)

Continuation gaps occur in an on going trend movement. In an upward trend, this is a sign of strength, whereas in a downward trend it is a sign of weakness. This gap may also be referred to as a measuring gap, which is based on the assumption that it occurs at about the halfway point of the movement. So if the distance covered so far is added, the approximate target area can be determined. Volumes at this gap are rather moderate.

Exhaustion Gap

Exhaustion gaps occur towards the end of a movement. If the previous two gap types have already occurred, an exhaustion gap can be expected. Volumes should be high here.

Occasionally, "common gaps" are also mentioned in literature. These are gaps in sideways phases that are closed rather quickly and therefore not considered to be particularly significant. Gaps resulting from the dividend discount may also be included in this type. A particular constellation is the island gap. In theory, it is a pattern rather than a gap. This is a price range that is separated from the rest of the price action by two gaps (exhaustion and breakaway gaps). This pattern usually marks a change in trend (island reversal).

May 2013. This movement was very dynamic and had no significant pullbacks. Only the DAX future volume failed to confirm the rise. The corrective movement from 15th March 2013 to 19th March 2013 made it possible for price targets to be identified via the Fibonacci extensions. The 161.80 per cent extension was at around 8479. This target was reached on 22nd May 2013 and was also exceeded by the closing price of the day.

On 23rd May 2013, the DAX opened with a real gap down of around 120 points (calculated from the closing price to the opening price). The opening price was not exceeded during the entire trading day. By the end of the day there remained a real gap down (Gap 1). Until then, the FDAX volume was the highest this month (Figure 2). So a breakaway gap may be assumed that presages a newly emerging trend. In keeping with the strategy parameters, a stop-sell order is placed below the low on 23rd May 2013, with a stop-loss above the high on 22nd May 2013 (Trade 1).

The order was triggered on 24th May 2013. The price subsequently tended to move sideways and with a gap up (Gap 2) made a new attempt at an all-time high – but to no avail. The last high was not exceeded and the price tended to move downwards.

On 3rd June 2013 (Gap 3) and 5th June 2013 (Gap 4), the DAX opened with real gaps down that were temporarily filled during the trading day. Ultimately, however, the daily closing price remained below the opening price. As can be seen in Figure 1, uncertainty candles already formed in this zone during the upward movement in May. Comparing the two gaps reveals that the opening gap 4 is larger than the opening gap 3. The body of the candle is also larger in Gap 4. Now if the price falls below this level, the downward pressure could intensify.

In summary, all the signs point to a continuation gap even if it's not a gap according to the classical definition. A second short position was placed by sell-stop below the low on 5th June 2013 (Trade 2) and triggered on 6th



Marco Baeger

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June 2013. The stop-loss for both open positions was now above the high on 4th June 2013.

The price subsequently trended downwards at first, but then reverted to the area of the continuation gaps. This clearly shows how dangerous it can be to place the stop-loss directly at the boundaries of the gap. On 11th June 2013, the DAX opened with a partial gap down and continued the downward movement.

On 13th June 2013, the DAX opened with a large gap down (Gap 5, 120 points again, as was the case with the breakaway gap). The opening price marked a new low in the current downward movement. At the same time, this price was below the lower Bollinger Band of the daily chart. During the first hour of trading, the 50 per cent retracement of the movement from 19th April 2013 to 22nd May 2013 was also touched at around 7988. Since there was an already existing breakaway gap and a continuation gap, it was safe to assume an exhaustion gap. Likewise, the other technical constellations described suggested an extreme price. The stop-loss for the two short positions was adjusted to the high of the first hour of trading and triggered in the course of the trading day. The day's closing price was well above the opening price. The opening gap was largely closed. The following day, the DAX opened with a gap up and subsequently rose right up to the resistance zone of the continuation gaps.

Price Targets

In gap trading, price targets can only be calculated if continuation gaps occur. In our example, there is a surprising result when using the measuring gap method described in the info box.

The calculation is made at Gap 4. The latter results from the closing price on 4th June 2013 at 8296 points and the opening price on 5th June 2013 at 8229 points. The high on 22nd May 2013 was at 8558. This results in a movement of 262 points completed by 4th June 2013. Now if we subtract these 262 points from the opening price on 5th June 2013, this results in a price target of 7967 points in the DAX. The day's low on 13th June 2013 stood at 7968 points. Now here is an ideal way of achieving the price target.

Waiting for the Stop-Loss or Realising a Partial Profit?

In keeping with the strategy parameters, the exit is made above the high or below the low of the candle following the exhaustion gap. However, it is possible for considerable profit potential to result from the last thrust of the movement following the exhaustion

gap, which would be lost again with this type of stop-loss. Hence it is advisable to realise a partial profit if the price target derived from the continuation gap has been reached.

The Added Value of Gaps

A correct interpretation of gaps allows conclusions to be drawn for further price action. In doing so, try to integrate the gaps into the ongoing movement and to consider other aspects of technical analysis. Not every trend movement includes all three types of gaps. Thus, you can trade only a breakaway gap or a continuation gap (see Strategy Snapshot). «

Strategy Snapshot	
Strategy name:	Gap Trend
Strategy type:	Trend Trading
Time horizon:	Daily Chart
Portfolio/markets:	Indices, Stocks
Part 1	
Setup:	Long or short, speculating on a newly emerging trend after appearance of a breakaway gap
Entry:	Stop-buy order (long) above the high or stop-sell order (short) below the low of the candle following the breakaway gap
Stop-loss:	Below (long) the low or above (short) the high of the candle formed before the breakaway gap
Trailing stop:	(Initial) stop-loss
Exit:	Ideally, after the occurrence of an exhaustion gap – otherwise, after the identifiable end of the trend that had started with the breakaway gap
Locking in of partial profits:	Possible if the initial risk has been reached
Risk and money management:	1% risk per trade
Average number of signals:	Depending on the market
Part 2	
Setup:	Long or short; speculating on a continuation of the previous trend after the occurrence of a continuation gap
Entry:	Stop-buy order (long) above or stop-sell order (short) below the candle following the continuation gap
Stop-loss:	Below (long) or above (short) the candle formed before the continuation gap
Trailing stop:	None
Exit:	Ideally, after the occurrence of an exhaustion gap – otherwise, after the identifiable end of the trend confirmed by the continuation gap
Locking in of partial profits:	Possible if the price target resulting from the continuation gap has been reached
Risk and money management:	1% risk per trade



The Range Strategy

How to Filter Profitable Breakout Stocks

Trading strategies can be very complex and complicated to implement. The concept we are introducing in this article shows that only a few lines of screening code are enough to find interesting breakout candidates. The idea is simple: Search for stocks that trade in a sideways range prior to the breakout.



David Pieper

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» A successful trading strategy need not be very complicated nor very revolutionary – the fact, that the trading signals are clearly determined, appear in high regularity, can be embedded in a complete system, and offer little room for emotions and subjective estimations, is much more important. One of the most popular approaches is the breakout of consolidation



The goal of this trading strategy is the timely recognition of consolidation zones that may be broken shortly and therefore generate a long or short signal.



zones, which can be determined with technical analysis tools. But the time effort is significant depending on the number of underlying's. If you look at a large pool of stocks the use of indicators within a screening-tool offers a better solution. We would like to show you how to create a simple screening-filter with the use of Moving Averages using an example of the Stockfetcher.com platform.

Step 1: Filter Interesting Candidates

The goal of this trading strategy is the timely recognition of consolidation zones that may be broken shortly and therefore generate a long or short signal. We will use S&P 500 stocks. We use Moving Averages to filter stocks that trade in a range and we will use the 13-day average and the 34-day average – of course you can use any other combination that you prefer. The following command line is programmed in the screening filter:

```
set{maratio,ma(13)/ma(34)}
maratio between 0.99 and 1.01
```

The limitation of the ratio between 0.99 and 1.01 assures that only those stocks are filtered where the 13-day line is one per cent above or below the 34-day line at maximum (sideways range).

An additional condition is that the 20-day line – in comparison to ten days prior to screening – has to be flat. The result is a Moving Average ratio that shows the relation of both smoothed lines to each other. The definition is that if the averages show a horizontal development, it is a sideways trend. The following command lines manage this step:

```
set{maslope,ma(20)/ma(20) 10 days ago}
maslope between 0.995 and 1.005
```

These four command lines complete the screening tool and now we can use it on stocks. We already mentioned that we are using the stocks of the S&P 500. Of course additional restrictions are possible and would be wise, especially the minimum volume – for example only stocks with a trading volume of more than one million shares per day – or a certain minimum share price, for example, we exclude stocks under ten dollars.

We would like to show you the inner life of the screening tool and therefore we have displayed some of the stocks that were identified as trading candidates with the above mentioned filter on 27th June 2013 in Figure 1.

F1) Result of the Screening Filter “Range”



Screening tools like Stockfetcher.com are excellent for filtering a large pool of stocks for individual criteria. We displayed stocks that fulfil the described consolidation setup and are ready for a – often dynamic – move.

Just a quick glance at the charts shows that the filter did a good job. Instead of evaluating 500 stocks manually, the trader can leave this work to the computer. Moreover: The trader receives the daily results by e-mail, if desired – it cannot be more convenient.

Step 2: Deducing Trading Scenarios

After identifying some stocks that fulfil all criteria, the trader should search the charts for some specialities – this is the final touch.

The following questions could be of help:

- Is there a large gap in the chart (take-over, quarterly figures, et cetera)?
- Are quarterly figures due shortly?
- Are there any abnormalities that speak for the exclusion of the stock?

After this step we can plan the trade. In our example we chose the Visa share. Figure 2 shows that the stock traded in a narrow range between 176 and 184 dollars in May 2013 after increasing dynamically the week prior. The trader could place a long and a short order as an if-done order to profit from a breakout.

The stop on the long position should be placed closely below the lower border of the range. If the short order is executed, the stop should be placed above the upper range. The advantage of the trading of this pattern is clear: The trader has a setup that determines a clear stop.

Strategy Snapshot	
Strategy name:	Range Breakout
Strategy type:	Swing trading
Timeframe:	Daily chart
Setup:	Long/short: breakout of the consolidation zone
Entry:	Upper border of range (long), lower border of range (short)
Stop-loss:	Other side of the range
Take profit:	Sell first part after reaching one times the range, second part after reaching two times the range
Trailing stop:	For the rest of the position after reaching the profit targets
Risk management:	1% risk per trade
Average number of signals:	Depending on the number of underlying's, that are used with the screener

The Exit

The exit is the most important part of the trade – because only then it is decided whether the trade is profitable or not. Every trader should decide for himself, if he wants to use a trailing stop and therefore act as a trend follower or if he places a clear profit target. A simple exit strategy that can be used systematically could be:

1. Measuring the sideways range (blue mark in Figure 2).
2. Closing of 25 per cent of the position after a book profit of one times the original range. At the same time placing the stop for the rest of the position at break-even.
3. Closing of 50 per cent of the position after a book profit of two times the range.
4. Securing the rest of the position with a trailing stop. Therefore the trader can profit of a potential trend continuation.

Conclusion

This screening approach, with which we developed a simple range breakout strategy, can be implemented on a broad stock pool. The chance of finding stocks that are ready for a breakout trade increase independently of the development of the broader market.

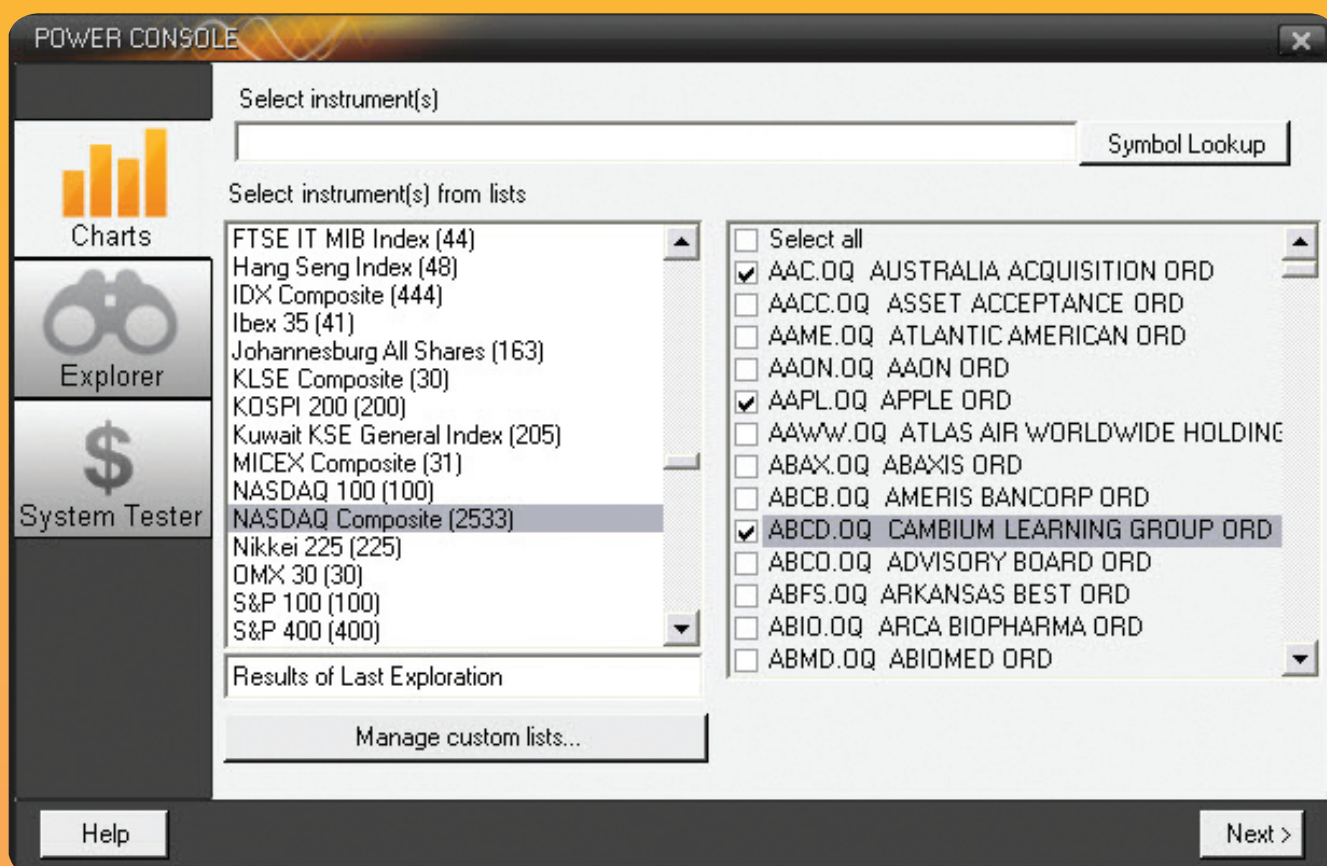
We will show further ways to use screening filters like stockfetcher in future issues. «

F2) Visa Daily Chart



Visa shares trade in a clear uptrend and were identified as a breakout candidate by the range filter. The projection of the blue range to the upside and the downside shows potential profit targets.

“Does a powerful analysis tool need to be complicated?”



The MetaStock Power Console takes everything that is great about MetaStock and puts it in one convenient spot, waiting for you when you open the application. You can open a chart, start a scan, run a test, review reports, make custom lists, and more... from one convenient dashboard. Want to open a multiple charts with your favorite template all with the click of a mouse? No problem. Want to run a scan on your preferred list of stocks? It's a snap. The MetaStock Power Console answers the question, "How can we take a great analysis tool and make it easier to use?"

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Trading Journal: Faik Giese

4th to 31st July 2013 – Long Trade NUS

In our Trading Journal series, traders – from beginners to professionals – present one of their trades that taught them a special lesson. This time it is Faik Giese.

» The following trade shows the potential of dynamic single stocks, if I follow a strategy that includes a flexible exit strategy that adjusts to the market environment. I use a combination of fundamental analysis, sector analysis and technical analysis to identify potential candidates. If the analysis of these factors results in an entry, I then add another criterion – the broad stock market. If it favours a long entry – which I try to evaluate with a complex risk model – I will buy. For the entry itself (the timing) I define certain entry-levels before the open in the daily chart and then execute them with buy-stop orders.

Thursday, 4th July, 2013: Analysis and Selection

Holiday in the USA. Scanning the stocks as well as the following analysis filters the stock of Nu Skin Enterprises, symbol NUS. The company has increased profit and sales by more than 20 per cent in the past four quarters. Therefore it is the fastest growing company of the peer group of “personal & household products”. From a technical point of view NUS is interesting for two

reasons: First, the stock formed an important sideways movement with a narrow consolidation over the past five trading days; second, the stock did not follow the correction of the S&P 500 of the past weeks and therefore NUS outperformed 92 per cent of all stocks as shown in the relative-strength ranking in Figure 1. My evaluation model of the broad stock market has not turn green yet and therefore I decide to enter only if the broader stock market – represented by the S&P 500 – turns up.

Friday, 5th July, 2013: Trading Plan and Entry

Prior to the open it shows that the S&P 500 will open positively. I define two entry levels in the daily chart where I want to enter the market with buy-stop orders to build a position step by step:

1. Entry 0.1 per cent above the high of the 1st July, 2013 at 62.76 USD.
2. Entry 0.05 per cent below the high of the consolidation of the 27th June, 2013 at 63.16 USD.

» The next day brings the all-clear: NUS increases further and closes at the daily high. Volume is above average but not too high to expect a temporary top. Now letting profits run is the name of the game. «

My initial stop-loss will be placed at 61.08 USD, which means 0.1 per cent above the low of the five-day consolidation. It is a very tight stop, but I have had very good experience with it – despite a hit rate of 45 to 50 per cent. The entry happens on a Friday – 6th and 7th July is weekend – and therefore the volume will be below average. Therefore I do not consider intraday-volume requirements. At 10.49 am and 1.32 pm New York time the entry takes place in NUS. My average entry price is $(62.79 + 63.17) / 2 = 62.98$. My initial stop-loss is placed at 61.08 USD. Therefore the actual risk per stock is 1.9 USD (without commissions).

Monday/Tuesday 8th and 9th July, 2013:

First Wariness, then All-Clear

During the course of the first trading day the profit climbs to 2.40 USD temporarily. Not bad, if it wasn't for the low volume of a stock at a new all-time high. The next day brings the all-clear: NUS increases further and closes at the daily high. Volume is above average but not too high to expect a temporary top. Now letting profits run is the name of the game.

Wednesday, 10th July, 2013:

Unexpected Support

After the prior days' close NUS unexpectedly announced that the prognosis of profit and sales – despite losses in currency – will be corrected to the upside. My plan is to let profits run. Therefore I only trail the stop for the whole position to 69.79 USD after the open. This equals 50 per cent of the gap size (open minus prior days' close). NUS closes at 79.36 USD. The profit of the position is 16.38 USD. This is a risk-reward ratio (RRR) of 8.6.

I expect a consolidation after this strong trading day. My exit level for the whole position is at $4 * ATR(12)$ below the high of the day at 74.54 USD.

Thursday, 18th July, 2013: Adding to the Position

After the consolidation I add to my position. I use a buy-stop limit order at 78.10/78.12. Execution price: 78.12 USD; stop-loss for the whole position: 76.48 USD; risk per stock for the second position: $78.12 - 76.48 = 1.64$.

Wednesday, 31st July, 2013: Exit

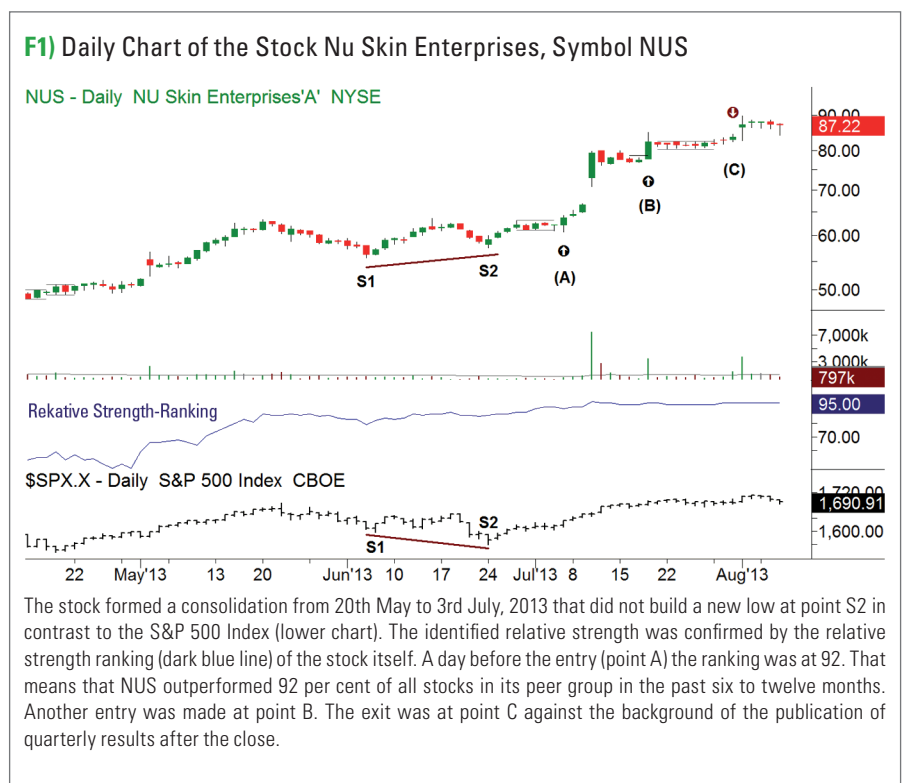
In view of the fact that the company will publish quarterly figures the next trading day, I close my position five minutes before the close at 83.58 USD.

Conclusion of the Trade

Trades 5th July: Total profit per stock 20.60 USD, risk of 1.90 USD per stock, which means a risk-reward ratio (RRR) of 10.8.

Trade 18th July: 5.46 USD profit per stock, risk 1.64 USD, results in a RRR of 3.3.

Conclusion: Such high profits compared to risk are only possible if you let profits run and limit the risk using tight stops at the same time. «





Risk- and Money Management

Part 1: The Three Stages of Truth

In this series we introduce a multilevel process of developing a risk- and money-management plan. The first part deals with the cognitive process that you have to pass through to understand the meaning of money management.

» Trading is a classic sport for individuals. You are a lone fighter and you are forced to deal with all the prominent aspects that lead to successful trading. Every trader will eventually realise that he needs a solid money-management plan in addition to good analysis. The history of trading is full of traders who thought that this

truth was not valid for themselves and that they were the exception.

A famous saying by Arthur Schopenhauer (1788-1860) gets to the heart of the necessity of good money management and how traders feel about this truth at the beginning and then finally accept it:

» Especially trading beginners think that «
success in trading is one big profit.

All truth passes through three stages. First, it is ridiculed. Second, it is violently opposed. Third, it is accepted as being self-evident.

Please take this saying in and take stock of yourself. It is the same with trading, isn't it? And it is especially true when it comes to risk and money management, right? We will now pass through the three stages of this truth from a trader's point of view.

Stage 1: Money Management Is Ridiculed

We often hear that the worst thing that can happen to a beginner trading is a series of profits at the beginning of his career: then the new trader thinks that trading is the easiest game in the world and therefore he will think of money management, position sizing and topics like scale outs as ridiculous. His ego grows, as he lets his position size grow – and then his luck turns. The market reverses and goes against him. Now the trader thinks that the market "is down on him". Active risk and money management could have made sure that he stayed calm, because a possible loss would not have bothered him since the position size would have been in the appropriate relationship to his account size.

Conclusion: Beginners especially, think that success in trading is one big profit. But a trading career consists of many small trades – and risk and money management are essential.

Stage 2: The Rules Are Violently Opposed

This is the point where most trading careers end. Only a few traders succeed beyond this stage unscathed. This is the point where the wheat is separated from the chaff, because even the best traders experienced this "struggle" at the beginning of their careers.

A very popular book, which should be a part of every trader's library, is Jack Schwager's "Market Wizards – Interviews with Top Traders". One topic runs like a thread through this book: Not one of the traders paid much attention to the topic of risk and money management at the beginning of their careers. The traders interviewed even increased their positions after a few losing trades in order to make up the losses. This is called "doubling down" which means the doubling of a losing position to reach break-even faster – one of the major mistakes in

trading. By this point the death of the trading account is only a question of time. But the market wizards succeeded in turning the corner. But not every novice trader is able to do so. Some have to end their trading career before it really started.

Stage 3: Acceptance of Risk and Money Management

Trading takes on a new meaning as soon as a structured risk- and money-management plan is accepted as the natural and obvious way to succeed in trading in the long run, because there are always new trading opportunities. But your risk is now limited and therefore your trading cannot get out of hand. If you follow a strict risk- and money-management plan you can use your time to search for entries that offer a good risk-reward relation (RRR). Components such as fear of being stopped out because the position size is too large and your account is endangered will play only a secondary role. Perhaps the trade will not be successful, but that is all right, because you have a clearly structured and well-thought plan. As soon as you understand that good risk and money management is essential and that it should fit your personality, you will have some kind of insurance against the loss of a substantial amount of your trading account. The relief that follows will have an enormous impact on your trading results.

Conclusion and Outlook

The importance of a good risk- and money-management plan was explained explicitly. But what do the details of good risk and money management look like? What are the pitfalls and how can you avoid them? The second part of our series will deal with these "ABC's of risk management". «



Jens Klatt

Jens Klatt is a market analyst at DailyFX.de and moderates the German DailyFX-forum. He has been in the financial sector for over seven years. Besides technical and fundamental observation of the markets, he focuses on sentiment analysis in the forex markets and develops his trading decisions based on this analysis.

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The Trader's Technical Arsenal

Common Indicators in MetaTrader – Part 3

Following part 2 of the series titled “Common Indicators in Meta Trader,” you are presented with part 3. This piece discusses the Bears Power, the Bollinger Bands (BB), and the Commodity Channel Index (CCI); as they function in MetaTrader, which continues to increase in popularity (especially version 4.0). In most cases, the indicators’ default parameters are used.

» The Bears Power

It is already known that there are two kinds of speculators in any type of market: bulls and bears. The bull speculates on the possibility of an instrument moving northwards; the bear speculates on the possibility of an instrument moving southwards. When an instrument goes north, it

means the bull reigns. When an instrument goes south, it means the bear reigns. Though the bull-bear relationship is interrelated, there are times when one kind of speculator dominates. Should you be able to determine which one is dominant at a particular period you might be able to anticipate what the market might do next.

Developed by Dr. Alexander Elder and introduced in his book titled "Trading for a Living", the Bears' Power measures the sellers' stamina.

Computation:

The Bears' Power (BEARS) indicator is the low price for the day (LOW) minus the 13-day Exponential Moving Average (EMA) price.

$$\text{BEARS} = \text{Low} - \text{EMA}(13)$$

In Figure 1, you can see how the Bears' Power indicator looks like on the chart. Here, the indicator is shown in bold blue. In order to use this indicator successfully, you would do well to combine it with another indicator. Which other indicator comes to your mind? If you are thinking of an MA, you are correct. A bullish signal is thus generated when the trend indicator points to a bullish market, and the Bears' Power is negative yet rising. This kind of signal is even more reliable if it is in the form of a bullish divergence.

The Bollinger Bands (BB)

This famous indicator was developed by John Bollinger and is used to measure the significance of volatility in a market. It is a charting tool plotted two standard deviations away from a Simple Moving Average. Because standard deviation is a measure of volatility, the BB can tell us when the market is rangebound and when it is trending significantly. The bands are narrow in a rangebound market, whereas they are wide in a significantly trending market.

$$\text{Middle Band} = \text{SMA}(20)$$

$$\text{Upper Band} = \text{SMA}(20) + (20\text{-day standard deviation of price} \times 2)$$

$$\text{Lower Band} = \text{SMA}(20) - (20\text{-day standard deviation of price} \times 2)$$

The computation could be modified a little to blend with the intrinsic nature of some trading instruments or approaches. The creator of

F1) Bears' Power on the Chart



The Bears' Power indicator is seen here on the daily chart. The indicator is shown in bold blue. Observe how the indicator behaves during an uptrend and a downtrend. It may be combined with other indicators.

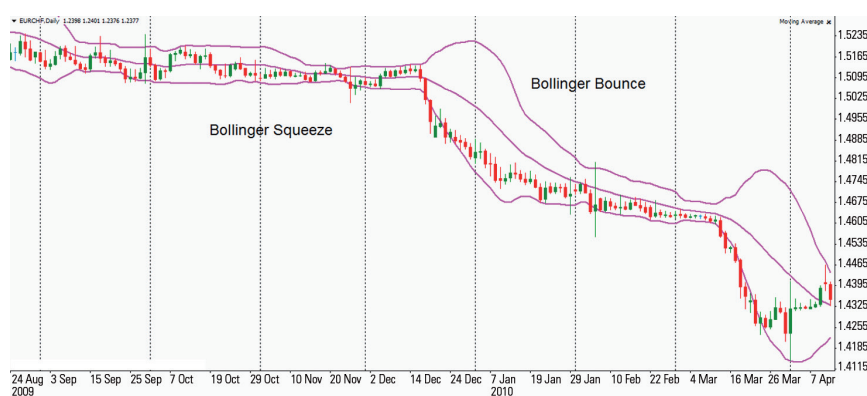
the BB, John Bollinger, advises some tweaking to the standard deviation calculation. When the SMA period is also modified, it would reflect on the amount of candles or bars considered when computing the standard deviation.

Lack of space don't enable us to go into more detail here. For more information on that go to www.bollingerbands.com.

The BB Bounce and the BB Squeeze

Please check Figure 2. Since the BB has the Upper Band, the Middle Band, and the Lower Band, it is no surprise that the price is prone to returning to the Middle Band. When price is pushing the Upper Band upwards, it may pull back. When it is pushing the Lower Band downwards,

F2) When the BB Bounces and Squeezes



This is a daily chart of the EUR/CHF. The Bollinger Bands period 20 are shown in magenta. You can see how it behaves during a sideways market and during a trending market (the BB Bounce and the BB Squeeze).

F3) The Traditional Use of the CCI



On this GBP/JPY chart, you can see how the CCI generates buy signals in oversold conditions and sell signals in overbought conditions. Some inaccuracy can be noted, as well as some accuracy.

it may experience some rally. Thus, the more the price pushes against the Upper Band, the more overextended the bull market; the more the price pushes against the Lower Band, the more overextended the bear market. It can be said that the price is going up when it is above the Middle Band and that the price is going down when it is below the Middle Band. The higher the time frame on which the BB is used, the more important are these points, including supply and demand zones in the market (for the indicator also acts like a kind of supply and demand zones).

The BB Bounce occurs when the market is trending up strongly. You would see the price pushing against the Upper Band, which means it would soon go back towards the Middle Bands. The reverse is the case when price is

trending down strongly and pushing against the Lower Band.

The BB Squeeze occurs during quiet phases in the market. The Bands would become tightened – a condition which chartist like to take as an early signal that the market would soon become highly volatile. As the market consolidates, the BB becomes narrow – hence the Squeeze. It is known that a breakout will eventually follow a consolidation phase, no matter how long it may hold out. When the price breaks upwards from the BB Squeeze, it is probable that it will continue trending upwards.

This pushes the price further northwards as it shrugs off any bearish threats: the marsh would stay aloof, if it had no relationship with the river. When the price breaks downwards from the BB Squeeze, it is probable that it will continue trending downwards.

We should bear in mind that the BB can also be used in conjunction with other indicators, and it can be used for many types of strategies and in many ways in addition to those mentioned here.

Commodity Channel Index (CCI)

The Commodity Channel Index (CCI) indicator was created by Donald Lambert and was discussed in a trading magazine that was released in 1980. It has become famous among chartists and speculators. This

tool calculates the relationship between a price, a Moving Average, and a common normal deviation from that average.

Computation:

The instance here is based on the CCI period 20 (as used in this article). It means that the number of the CCI periods (which is 20 in this case) is used for both the Moving Average and the normal deviation.

Typical Price (TP) = (High + Low + Close) / 3

CCI = (TP – SMA(20) of TP) / (.015 x Mean Deviation)

F4) Using the CCI and the EMA for Trend Trading



On this EUR/CAD daily chart, the CCI is used as a trend-confirming indicator rather than a tool that merely gives overbought and oversold situations. Using this in conjunction with an EMA period 20, long trades are sought only as long as levels are above both 0 of the CCI period 20 and the EMA period 20 – and vice versa. With this combination the hit rate of the signals is improved.

The CCI is computed in such a way that the location of the price is more than 70 per cent of the time in the region between +100 (overextended bull market) and -100 (overextended bear market). Traditionally, the CCI identifies proportionally high prices when they are above their average. The reverse is also true of a bear market. Traditionally, the CCI is used to pinpoint overextended bear or bull markets. When this decision-making tool is used in conjunction with other technical indicators and price actions, it can produce fine results in many types of financial markets.

In Figure 3, we see the traditional use of the indicator, which generates buy signals in oversold conditions and sell signals in overbought conditions. The CCI is based on a period of 14 days. On the chart, some inaccuracy can be noted, as well as some accuracy.

In Figure 4, you can see how the CCI is used as a trend-confirming indicator rather than a tool that merely shows overbought and oversold situations. The problem is that when a market is in a strong trending mode it can remain in the overbought or oversold condition for a long time, while contrarians



Azeez Mustapha

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get thrashed. Here, only the level 0.00 is given (the levels +100 and -100 are done away with). Therefore using this in conjunction with an EMA period 20, long trades are sought only when the price is above both level 0.00 of the CCI period 20 and the EMA period 20 – the logic is reversed for the period when the price is below both level 0.00 of the CCI period 20 and the EMA. With this combination, the hit rate of the signals is improved.

Conclusion

In part 4 of this series we'll discuss these indicators: DeMarker, Envelopes, and Force Index. «

Preview of the next Issue

COVERSTORY



Trading vs. Triathlon – What Great Athletes Can Teach You

Obviously, trading and triathlon are different sports. However, you might be surprised to hear that the process to become successful is very similar to both, indeed. Marko Graenitz, who did many interviews with professional traders and is a triathlete himself, will delve into what triathlon can teach you about trading.

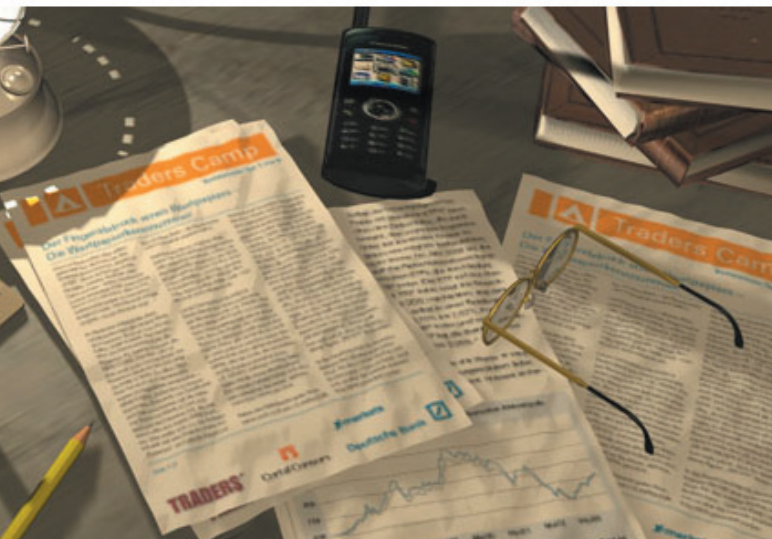
PEOPLE



Markus Heitkoetter

As founder and CEO of Rockwell Trading, Markus Heitkoetter has shared his trading ideas with more than 300,000 traders in over 190 countries. In 1996, he began developing a number of trading systems and in 2002, decided to leave his job as a director at IBM to become a professional trader.

The November issue of TRADERS' appears on **31th October 2013**.



Economic Data as Market Mover

Part 2: ISM-Manufacturing Index

First, the market is quiet and uneventful and there are no extreme movements. And only moments later the markets seem to go crazy. Often the reason is economic data – mainly from the US. Today we want to introduce the ISM-Manufacturing Index which depicts the current state of the manufacturing industry and therefore ranks among the most important economic indicators of the financial markets.

» In contrast to other surveys where the sentiment of the respondents is examined, the ISM-index shows the actual development of the particular companies and therefore it is not as volatile. «

» Analysts and investors use several different indicators for the analysis of the economy. The so-called “manufacturing indices” play an important role: They offer information about the beginning of the production process. Prior to the production of an actual product you need to order the necessary commodities – that is the task of the manufacturing managers of the different companies. They are interviewed month after month and based on this data the index is calculated. In the US there are three kinds of indices that are calculated and published – including the ISM-indices of the non-manufacturing and the manufacturing sector.

What is the ISM-Index

The ISM-index of the manufacturing sector is published every first workday of the month by the Institute of Supply Management (ISM). It is based on a nationwide survey with a sample size of about 400 companies interviewed from 20 different sectors – therefore the index is a reliable and current picture of the cyclical American industrial sector. The index consists of the following sub-components that are weighed differently and aggregated to an overall index:

- new orders (30 per cent)
- production (25 per cent)
- employment (20 per cent)
- supplier deliveries (15 per cent)
- inventories (ten per cent)

In contrast to other surveys, where the sentiment of the

respondents is examined, the ISM-index shows the actual development of the particular companies and therefore it is not as volatile. The index is seasonally adjusted to avoid seasonal fluctuations and contortions. Figure 1 shows the monthly overview of results.

Meaning for the Financial Market

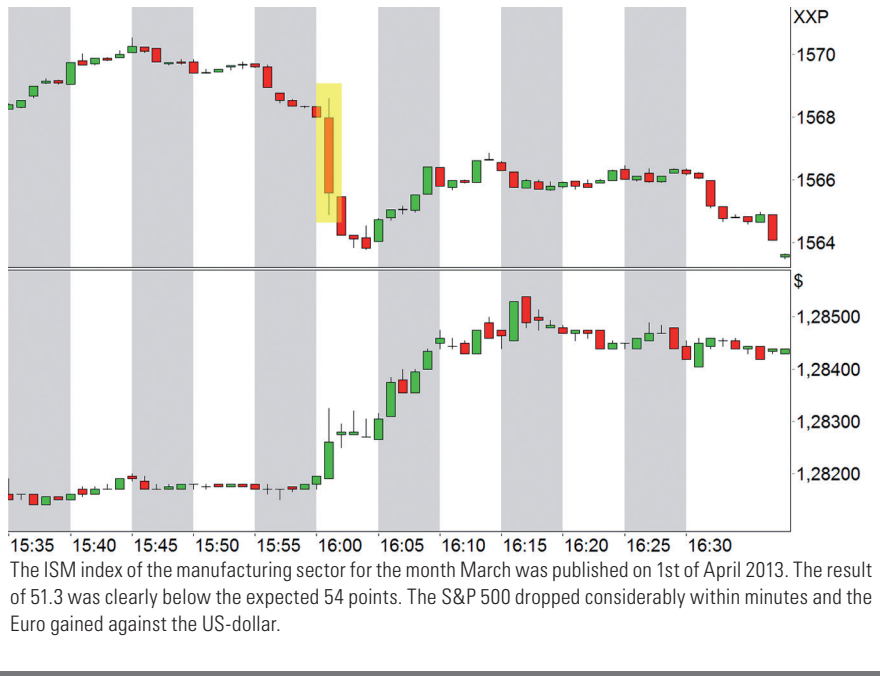
Interpretation of the ISM index is guided by the changes from the prior month as well as the distance

F1) ISM Index of the Manufacturing Sector, March 2013

MANUFACTURING AT A GLANCE MARCH 2013							
Index	Series Index Mar	Series Index Feb	Percentage Point Change	Direction	Rate of Change	Trend* (Months)	
PMI™	51.3	54.2	-2.9	Growing	Slower	4	
New Orders	51.4	57.8	-6.4	Growing	Slower	3	
Production	52.2	57.6	-5.4	Growing	Slower	7	
Employment	54.2	52.6	+1.6	Growing	Faster	42	
Supplier Deliveries	49.4	51.4	-2.0	Faster	From Slowing	1	
Inventories	49.5	51.5	-2.0	Contracting	From Growing	1	
Customers' Inventories	47.5	46.5	+1.0	Too Low	Slower	16	
Prices	54.5	61.5	-7.0	Increasing	Slower	8	
Backlog of Orders	51.0	55.0	-4.0	Growing	Slower	2	
Exports	56.0	53.5	+2.5	Growing	Faster	4	
Imports	54.0	54.0	0.0	Growing	Same	2	
OVERALL ECONOMY				Growing	Slower	46	
Manufacturing Sector				Growing	Slower	4	

The ISM report of the manufacturing sector gives indication of the development of several components like new orders, production, price development and employment. The 50-point level is the cutting line between contraction and expansion of the economy.

F2) S&P 500 and EUR/USD on 1st of April 2013



portfolio managers often use the ISM index for analysis of the bond and the stock markets because of its high significance.

Example

Figure 2 shows the 1-minute candlestick chart of the S&P 500 in the upper part and of the EUR/USD currency pair in the lower part. The March 2013 ISM index for the manufacturing sector was published on Easter Monday. According to Bloomberg, consensus expected 54 points. The actual result was clearly lower at 51.3 points. If we look at the sub-components (Figure 1) we see that this disappointment was due to the decrease of incoming orders by 6.4 per cent.

to the 50-point level that is the threshold between economic expansion and contraction. If the ISM index is above this threshold it means expansion on the overall level – if the ISM index is below this threshold it is an early warning signal of an economic slowdown. The meaning of this level shows primarily in the behaviour of the US-central bank – it won't increase interest rates if the ISM index quotes below 50. Empirical studies show that the real threshold between contraction and expansion of the US economy is at an ISM level of 43 points. Analysts and

The US markets' first reaction showed that a new high on the prior day was extremely negative: The S&P 500 dropped four points within minutes whereas the Euro gained dramatically against the US-dollar. It is interesting to watch the narrowing of the trading range prior to publication of the report – a clear sign that market participants slowed down their activities and therefore the order book was thinning. After the publication of the news we see that discharge and volatility increase considerably. The example shows that trading shortly before or after publication of important economic data is always high risk. The prediction of price direction is not possible because of uncertainty and the unknown positioning of market participants. Short term traders should plan to close open positions prior to publication – and they should never enter new positions shortly before or after the publication of data.

Conclusion

The ISM index is an important economic indicator although the number of companies surveyed is relatively small; there is still a close connection to the development of the economic cycle. The markets still react strongly to changes in the index because of its high reliability in the last decades. «

Information

Indicator:	ISM index (manufacturing sector)
Organisation:	Institute for Supply Management
Period:	Monthly, first working day for the prior month
Time:	16:00 CET
Important key figures:	Overall index
Market relevance:	High
Publication dates:	2nd January, 1st February, 1st March, 1st April, 1st May, 3rd June, 1st July, 1st August, 3rd September, 1st October, 1st November, 2nd December
Website:	www.ism.ws/ISMReport

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The Pro's Process

Part 13: Michael Bigger

In this series we are asking Pro Traders about their psychological processes. Delving a little into how it feels to them when trading. The good and the bad. How this has changed over time and what preparation they do mentally for performing as a trader. One of the key features for us was that we wanted traders with experience who have been through the mill over the years and of course, we appreciate those who were kind enough to talk to us so candidly. We hope this gives developing traders more to learn from. Each interview in this series was conducted by Richard Chignell who is himself a trader. Please visit his blog at <http://embrace-thetrend.com>.

» **Richard Chignell:** How long have you been trading?

Bigger: I started on Wall Street in 1992. I was trading the equity derivatives book for Citibank Canada. I stayed in Canada for two years and then I moved to New York. Before that I was trading my own account for five or six years.

Richard Chignell: That's 20 to 25 plus years' experience. What style of trading or investing would you say you practice?

Bigger: Everything.

Richard Chignell: I notice on your website that you are not just a trader but you are also active in investing.

Bigger: We trade, we invest – trading is about making money. Opportunities are fleeting and they present themselves in different shapes and at different times. We do not have blinders on that say, oh you know, that we have to just trade value or something like that. We don't look at the world in that fashion. Our model is that, and maybe we draw it from physics, that we are basically trading potential energy. That is basically what Buffett does. Buffett calculates the value of a company, comes up with an intrinsic value, and, if it is below and if he likes the model of the company and stuff like that he goes ahead and buys it. So basically what he does is that he exploits a level of energy between its intrinsic value

and the stock price. We do that in terms of value or in terms of statistical arbitrage, etc. We are always thinking about exploiting pockets of valuation. If we buy something, if it is statistical, what else can we sell against it. If we buy a stock, we ask ourselves: What is its intrinsic value? Can we hedge it with the S&P? We try to rotate our inventory and do things of that nature.

Richard Chignell: Are you also market agnostic? Do you trade futures and stocks or are you stock market focused?

Bigger: Yeah, I used to run big equity books so we basically do everything, but we don't touch commodities that much except for trading them with ETF's.

Richard Chignell: So getting into the reality of when you are actually trading; how do you feel when a trade goes against you?

Bigger: That's a very good question. You know, it doesn't affect me like it would affect a lot of other traders. I'm not right or wrong because in the next five minutes something goes against me. We try to get ourselves in situations where, if it goes against us, we still feel good about the situation.

To give you an example: let's say we have a stop, we would never have a stop that is so close to where

the market is so that we would get pushed out of the situation. Usually we are in a situation where we are very confident of our facts and we let our positions run and it's fine. We run big portfolios, they are diversified so we are not neurotic about a position in particular. We bought a lot American Apparel which is in a distressed situation, it went to 1.70, came back down to 90 cents, This reversal doesn't affect me one bit. The thesis is still intact. If you are driven by the stock price you are going to go crazy.

Richard Chignell: Does this alter at all when you have your trading or your investing mind set in place? Obviously one has a longer term time frame and different parameters that you are thinking about. Does that effect your emotional feelings?

Bigger: Aren't they the same? We are looking at potential energy in situations. Whether it be a short term position or a long term position we don't look at the world that way. We look at the world in terms of potential energy and where can we extract the energy out of the system. We don't categorise in terms of 'are we doing value investing here or there', in a sense a little bit, but overall that is not what we are trying to do.

Richard Chignell: I think that makes a lot of sense.

Bigger: We have backgrounds in physics. We have mathematicians working with us and PhD's and so we look at the world from a physics kind of standpoint and where the energy is in the system and how we can exploit it. And you know what, I don't care what category other people put on how things are trading. They can have their own stuff, we do it our own way and we are very happy with that. So if we are valuing situations, we get those values, we look at the facts and act accordingly. And if we have to get out of a position because we are wrong we just do it but it's never so related because the price went down or it goes up or goes against us or stuff like that.

Richard Chignell: I think that offers a very interesting perspective – especially the physics and the energy direction side of things. There is the flip side to the question about how you feel when trades or investments goes for you? Because obviously emotions are at play to some degree. How does that differ?

Bigger: We try not to get influenced by it, but you know mentally you are always influenced a little bit by your position especially when you have a big position on. If it goes in our favour you know we can be, maybe, a little overconfident but we know we have to manage that.

I'll give you an example: When we traded CROC's, we bought the stock at about 90 cents, it went up to 32 dollars and then we sold a little bit, but it was just a tiny bit on the way up, and then it came down to twelve dollars. We have a very long term thesis on that company, so we wish we would have sold more, but we are happy with the thesis. So it all really depends on your time horizon, it depends on what you own and sometimes you wish you had sold more. But that is easy to say, when the stock price is down.

I could have done the same thing with Amazon, when it went from 100 bucks to 34 bucks in 2008. We had that big gap down but man you look at the stock price now. On American Apparel we have a huge position in that name and we think the company is going to earn its stock price in basically five to seven years from now. So that puts the stock at ten to 15 dollars, if it doesn't go bankrupt and bankruptcy is a potential. We have our own odds on that. Does it matter if the stock goes to zero? It doesn't. I mean, we are going to lose money but in terms of how you look at it right now and the probabilities and stuff like that you know what your bet is and zero is part of the scenario.

Michael Bigger

Michael Bigger is an investor and trader who has been involved with trading technologies for more than 20 years. In 1992, he joined Citibank as head trader of U.S. single-stock derivatives, where he managed a five billion dollar portfolio of equity derivatives. In 1998, he joined D.E. Shaw & Co., L.P. to trade the U.S. equity derivatives portfolio. In 2000, he started the listed equity options business by establishing KBC Financial Products as one of three initial market-makers of the International Securities Exchange. He built that business into the primary market-maker for listed equity options on over 120 companies, with 15 traders executing thousands of trades per day. In December 2001, he left KBC to start the trading firm Bigger Capital. The company just completed a software application to extract investment information from liquid networks and has incorporated this information in its trading algorithm.

He received a BS in Physics from the University of Quebec in Montréal in 1986 and an MBA from York University in Toronto in 1991.

As a private investor in start-up companies, he was among a group of investors who sold Innovative Fibers to Alcatel for 175 million dollars in July 2000.

He is the author of "In Praise of Speculation!" and "How Traders Achieve Creative Flow".

Richard Chignell: So, Michael, your very scientific based approach and viewpoint means that you never let your emotions override a thesis that you have?

Bigger: Oh... I don't know. We are very emotional. I am a very emotional guy, but I know what I'm dealing with. Like in the case of American Apparel: The reality is that it could go to zero and it has potential of ten to 15 dollars, so we know that probability. So of course I will be emotional, if we lose all that money, but that doesn't change the nature of the bet that we made. I guess we are a slave to that bet unless the facts change for some crazy reason, which can happen too, and then we would unwind.

Richard Chignell: Michael, I noticed reading your bio you come from a very scientific background and obviously you have been speaking about science and physics with regards to your company's way of trading. Have your feelings changed over the course of your trading career or have you always had this sort of background, where the emotions aren't going to effect your models?

Bigger: Well, I think one of the best lessons I have learned was, when I was in New York trading the single stock derivatives book. You have no choice. You have a market to make, you have a market for size to make, and, then you make your market. If you get hit, because the companies sell puts now you own like a few million puts on Microsoft, just as example, or Dell, or whatever the companies were in those days, so you have a huge position. And most of the time you don't like what you have, because it is big and it is very hard to get out of it. So you get very very good when you have a big position like that, you get very very good at working your butt off and going to the market and trying to find other things you can sell against it or buy. You need to do this to reduce the overall exposure and reduce the risk. That's basically how we approach our trading. We have a lot of positions and we are trying to move value from one to the other. So for us it is more about that process, exploiting value and sometimes not having the stuff you want to have, but working very hard to exploit that potential of energy. It is very hard to explain in words, but if you get dropped a massive position and you have to deal with it, I tell you, you learn very quickly. The charts don't matter and sometimes the volatility doesn't matter, if you have a huge position – what matters is: how the heck can I trade out of this? How can I find other opportunities to trade against it? If you buy something that is quite cheap or fair value, what can you sell? This is a very different discussion to what many talk about like 'the chart looks good' – come on, guys!

Richard Chignell: With a lot of that stuff, particularly having very large positions, obviously your emotional system gets bombarded. Do you have any practices that you do away from the office or the trading screen to help handle things mentally or emotionally?

Bigger: Well, I play hockey and I do a lot of kite boarding.

Richard Chignell: Do you find that this actually gives you a balance to your market operation? A mental or emotional balance?

Bigger: Yes, kind of. Well, hockey is more like hustling. You have to hustle when you play hockey so it's a little bit like trading as you have to make things happen. So that doesn't get me too much away from the trading mental framework. The kite boarding is definitely more meditative: more of a meditation or relaxation as it is just such a totally different atmosphere.

Richard Chignell: Have you always had some sort of approach to balance yourself personally away from the markets? What about when you were back on Wall Street?

Bigger: Yes and no. I guess, not really. You know we are thriving in that commotion of trading the market and just going around and finding opportunities. So that is almost like a mediation, too. Although it doesn't sound like it. If you like it so much, and are passionate about what you do, for me it is like playing a hockey game, you know?

Richard Chignell: Do you feel you are naturally attuned to the market game and the involvement in it? Is it something that just came naturally to you?

Bigger: Absolutely. When I came to Wall Street, when they moved me from Montreal to New York, I asked the big boss of the trading floor "What the heck, why did you guys hire me? There are so many people in the US?" There were pretty big books back then and 500 traders on the floor and I was just always puzzled, why I was given that book in New York. Junaid Rubani told me, how to play the game: "Look you are a street fighter. You know we go into a fight and you go in there and you make things happen. You hustle, you make plays happen. That is what it is." It is never the same. There are different fights that you have to fight. You have to create things. You have to make things happen on your own without resources. It's like entrepreneurs – that's trading! I think, what he said captures the essence of trading, which is a little confusing for me as people approach trading saying it's stop losses, and, set-ups and all that stuff. For me it's not all that stuff. It's more like, you know, walking down the street and getting attacked and you have to defend yourself.



We trade, we invest –
trading is about making money.



It's a totally different thing. The last few weeks with the fiscal cliff made it a totally different ball game. You have to readjust how you see the market and do it very quickly.

Richard Chignell: I find it very interesting with your comments about a street fight and having to defend yourself as well as the context of the recent fiscal cliff. Do you find trading is more about having a good defence rather than an offence?

Bigger: I think, it is having a killer offence, when people are panicking. That is where the street fighting comes from. During the fiscal cliff episode, when people start shaking, you have to go into the market and if they need liquidity, you have to provide it. That's basically how I trade. What the charts look like and all that stuff is irrelevant. The money you take is the money you get from other peoples mistakes in one way or another; because they are mis-pricing securities. So when you sense that the market is nervous and is mis-pricing you have to go in there. You can't wait for the sun to show up because it doesn't work that way. You have to go in there and provide liquidity and extract money out of the system. That's how we look at things.

Richard Chignell: This is brilliant stuff, Michael. I am conscious though not to take too much of your time so let's wrap up with: If you could give one piece of advice, with all of your years in the game street fighting in the markets, to aspiring traders about emotionally handling the market – what would it be?

Bigger: Maybe it's going to surprise you, but if you can have a little bit of the emotion that the market has and be able to step out of it and look at yourself and how you are emotional in that situation, it gives you a good read for how the market participants are acting. So it's almost like you need to be emotional to get the vibe of the market and how fearful people are and then you are in a much better situation to exploit that. It's almost like getting the good read on the emotional state of the market and then overriding your own emotion to take the proper position which is never easy. During that fiscal cliff period, when it goes down against you, you get emotional and others are emotional, but no one wants to get in there, just a few people want to go in there and buy the market. So it is a case of, how do you go in there and override that emotion? It is important to have that emotion, because

it gives you a good read on the market, but you need to be able to override it and then just go and be confident in yourself. For me that is how I approach it. I think this notion that you have to be a rational agent is rubbish.

Richard Chignell: The idea, that you are some kind of Mister Spock or Data from Star Trek with no emotions and very passive is true?

Bigger: Yes, it doesn't work that way! It is impossible. We are people on that mission, so we shouldn't be too emotional.

Richard Chignell: So despite the fact that you are a scientist, and most of those that work for you are scientists, you can't take out the human emotion side of the market?

Bigger: No you can't take out the human factor. We have a little model that is called the 'Levy Flight'. You can search for it on my blog as we have written about it. It's basically a mathematical model that represents how animals go and search for food and their random processes that they use to gather food depending on the conditions of the environment. The model accounts for that and when we think about this we think about the news and journalists and the media. The media and those people are always looking for food as they have businesses to feed, so they create a lot of anxiety. The Levy Flight is just a great model to use to visualise how things evolve in the media. Then you can look at that and then you can spot when the media moves, when the media goes totally all in, like with the fiscal cliff. That's when you want to look to get involved as that's when there are tremendous opportunities. You see that is one way we use science to understand emotion. We are all animals with that kind of instinct, but we just try to use mathematics to model some of those things.

We'd like to thank Michael Bigger for sharing the way he tackles the market from an emotional/mental side of things and for his willingness to allow us to post this as a free resource in the hope that traders who have been in the market for less time or are thinking of entering can perhaps pick up some A-HA's. If you are interested in finding more out about Michael, you can find him at his website:

» www.biggercapital.com «



Orkan Kuyas

The Facebook Trader

He trades (almost) everything and loves to add his two cents to anything. What's more, he does so successfully. Not for nothing is Orkan Kuyas called the "Simon Cowell of trading". Seriously, though, he has built himself a small empire as a "Facebook trader" within a short period of time. By now, his trading group on Facebook has more than 5500 members. Marko Graenitz met Orkan Kuyas in Duesseldorf, talking to him about his stock-market career, his trading approach, and his trading group.

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» TRADERS': Due to your trading group on Facebook, you have been well-known in the German trading scene for about two years. How

long have you actually been active in the stock market?

Kuyas: I first heard of the stock market when I saw the film "Wall Street". I forget exactly when that was but certainly sometime in the late 1980s. Later, I went on to study business and started to trade stocks on the side.

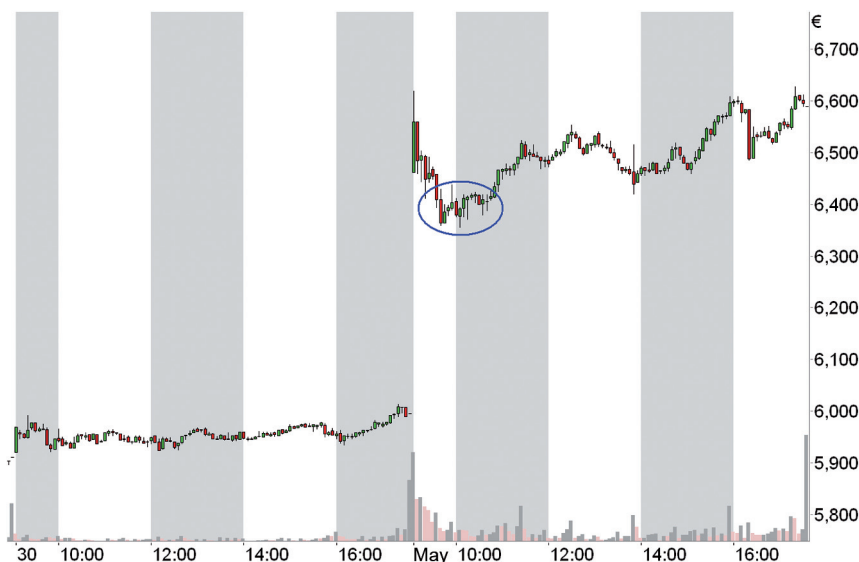
TRADERS': But you didn't learn in college how to trade, did you?

Kuyas: No, that had nothing to do with my studies, everything was much too theoretical there. At that time, I started trading stocks because those were the years of the New Economy and just about everybody joined in the gambling.

TRADERS': But "gambling" is a dirty word in trading.

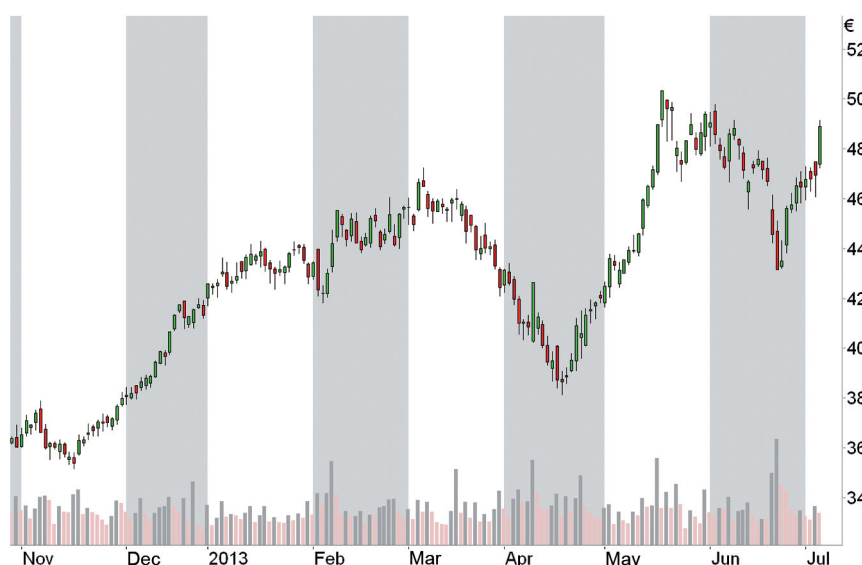
Kuyas: Yes, all that had nothing to do with good trading and risk management. But as a neophyte in such a market, you don't worry about it. Like almost everybody else, I initially did very well with that naive approach just as long as the markets were doing well.

F1) Day Trading Example



To Orkan Kuyas, trend-following intraday trading especially suits stocks that are currently strong or weak against the benchmark index. At the same time, there must be no excessive exaggeration present yet. The figure shows a 5-minute chart of Infineon from 30th April to 3rd May 2013. After the stock consolidated as a result of the upward gap (see marking), intraday trades in long direction seemed to be a natural choice, as was the case on the following days, as well (not shown).

F2) Swing Trading Example



In swing trading, too, strong stocks are interesting for long positions (and vice versa, weak ones for short positions). Daimler was going strong in November and Orkan Kuyas stated a target price of 45 euros. Once the target price had been achieved and the stock had corrected violently in April and May 2013, the share even soared to around 50 euros.

TRADERS': How did you pick your trades in those days?

Kuyas: Well, I did what you would never do as a professional trader: I read magazines and newspapers to replicate the hottest stock picks that were in there. But as I said, that worked great in 1999 when I started, simply because all stocks were going through the roof back then.

TRADERS': Where did you get the starting capital for your trading?

Kuyas: I used to work a lot in the music business on the side, both as a DJ and as a producer. Afterwards I would sit down at home, log on to the ultra-slow internet via my modem, look at the prices and buy and sell shares over the phone. My



It's comparable to what a hunter does, watching out for such special situations and then pulling the trigger at the right moment.



positions were mainly swing trades. I didn't start doing intraday trading until a few years later.

TRADERS': How did you survive the crash, when the New Economy bubble burst?

Kuyas: When prices were going south, things obviously weren't going very well any more. In the end, I exclusively made long trades at that time. You could not just bet on falling prices as easily as you can today. Luckily, I happened not to have any open positions when the terrorist attacks occurred in New York in September 2001. After the attacks, I was able to open new long trades at favourable prices and recoup some of the losses sustained during the previous months. In 2002, things were still going badly, so I decided to take an extended break starting with the middle of the year.

TRADERS': So after making all those profits during the New Economy, there was a reality check. What motivated you to return to trading?

Kuyas: A film that opened my eyes was "Rogue Trader", telling the story of Nick Leeson, the trader who after a meteoric rise drove the venerable Barings Bank into bankruptcy by engaging in extremely risky manoeuvres and building up huge positions. His big mistake was that he believed so firmly in his market assessment that he simply could not let go. He built up an extremely large long position in index futures and continued to buy when the markets were falling. One day there was a crash which was enough to wipe out the entire bank. This resembled the slump after the New Economy when traders continued to expand their losing positions in stocks that had fallen steeply, hoping that they would

recover. That was how many traders came a cropper back then. During the break I took from trading, I thought about a new trading concept of my own. I had done A-level maths at school, and I now wanted to use that knowledge for my trading as much as possible. I read a lot about technical analysis, including its "Bible", that is, John Murphy's book "Technical Analysis of the Financial Markets". I completely blocked out fundamental data, since they would not be relevant to my short term trading horizon. I never attended seminars though, but instead always taught myself everything. The only outside support I had was a little chat with a few trader friends two of whom to this day are Giovanni Cicivelli and "NoggerT".

TRADERS': What happened next?

Kuyas: As of 2003, things went really well. During this time there were also some rather obvious trends, for

F3) Drillisch's Crash Trade



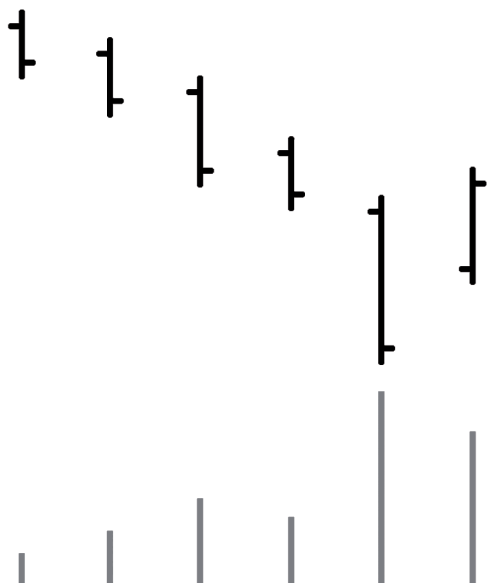
In November 2011 there was a sudden newsflash that Deutsche Telekom was terminating its cooperation with Drillisch, a German mobile-phone operator, and demanding the return of millions of euros in commissions. This caused the price of the Drillisch stock to suffer a massive decline. At 3.40 euros, Orkan Kuyas bought a small position by market order without any stops. The price drop of approximately 60 per cent seemed excessive to him. A little later the whole news story was denied and by the same evening, the stock went up to more than five euros.

example in solar and biotechnology stocks. Generally, things kept going well during the entire bull market until the year 2007. When Lehman Brothers collapsed, I lost a lot of money trying to bet on the stock's rally during the crash. However, since I had also been trading derivatives intraday and on the short side since 2003, I was able to survive the year of the crash reasonably well. Many other traders went bankrupt during that time as a result of the extreme volatility. I then managed to catch the trend reversal in March 2009 very well when suddenly one of the major banks issued a positive statement whereupon the entire market was swept upwards.

TRADERS': This was all before the emergence of your Facebook group. When did you start with that and how has that changed your trading?

Kuyas: I founded the group in May 2011. But not until August 2011 did I really start to actively post my trades and assessments there. My trading style though has not been influenced by that, since I continue to trade just the way I have traded before. By the same token, I cannot post every trade in the group since I also make short term fast scalping trades.

F4) How to Catch a Falling Knife



In stock-market parlance, buying into falling prices is like trying to catch a "falling knife", meaning that you may get badly hurt in the process. But it may also work. When prices decline sharply, Orkan Kuyas will wait for an extremely high bar to form in trading volume. This will be an indication of the stock being extremely sold and of the existence of an exaggeration that may be reversed again in the short term. However, traders should remember that even with a successful entry upon the upward momentum this is often only a short-term upward correction, and should therefore look for a quick partial exit.

TRADERS': Speaking of "strategy", could you please describe to us in more detail what your trading approach is like?

Kuyas: Sure. First of all, I have several trading styles: short term scalping, countertrend trades and longer-term swing trades. The swing trades basically go with the trend. I open such positions when there is an orderly market and it goes in a certain direction without any hint of an exaggeration. So it's a simple trend-following approach where I like to buy strong stocks and short weak ones. Or more precisely, when it comes to positions I hold overnight, I would much rather trade derivatives than stocks. This reduces my risk and leaves me with more liquidity. If there are strong exaggerations, however, I will position myself more countercyclically and trade in expectation of a short term trend reversal or hiatus. Regarding scalp trades, I quickly enter and exit a position just to take a few cents' worth of movement. This requires a special situation in the chart that I recognise on the basis of experience, a high degree of concentration as well as swift execution. To clearly separate swing and day trading, I have different accounts for each.

TRADERS': Can you name a few indicators that you use, or patterns that will help you make trading decisions?

Kuyas: I like using indicators as a supporting element, but never as the sole decision criterion. As a rule, I look at Simple Moving Averages, the MACD (Moving Average Convergence/Divergence), and RSI (Relative Strength Index). Either I use the indicator directly to derive my interpretations from it – for example, an "overbought" or "oversold" situation. Or I use the indicator in comparison to the price development in order to identify good trading opportunities based on divergences. I also like to use Fibonacci ratios and the Elliott Wave Count.

TRADERS': Elliott Waves – to exaggerate a little – are counted differently by each trader. Do you have an example to illustrate how exactly you apply this technique?

Kuyas: A good example was Gold on 28th June 2013 (Figure 5). After a five-wave downward movement in the days before, the A and B counter movements had already formed upwards. I went long and waited for a final upward push for the three-wave ABC pattern of a typical correction to be completed. A bit of patience was needed here, but in the evening the upward movement

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actually did materialise and I smoothed the trade late in the evening, making a good profit.

TRADERS': How do you set stops?

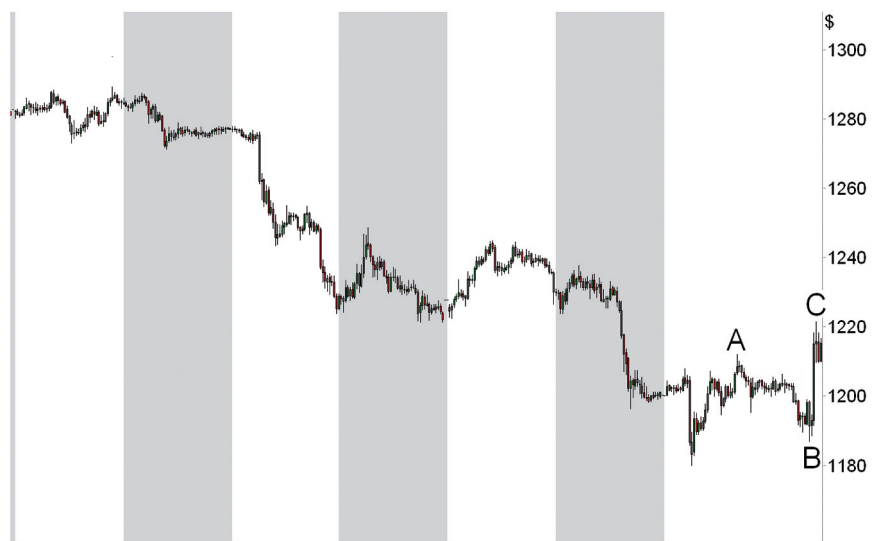
Kuyas: I always have stops firmly in the market, with the exception of short term countertrend trades. Many traders don't like to enter firm stops, but that's exactly where the problem is: The stop is designed to protect me when there is a sudden rapid price movement and I cannot react. It is also meant to protect me from myself since traders who only set their stops "mentally" and mistakenly think that they can smooth the position themselves right after reaching the stop price, may very well not be in a position to do so at that time.

More often than not, they tell themselves "there will be a turnaround in the price any minute now, and I'll continue to stay there for only a little bit longer." This is the way that much greater losses may occur than originally factored in. To be sure, things sometimes may turn out O.K. and the price does indeed turn, but when things go wrong they do so with a vengeance. And it is precisely these large losses that will ruin your trading account.

TRADERS': Why do you make an exception with countertrend trades?

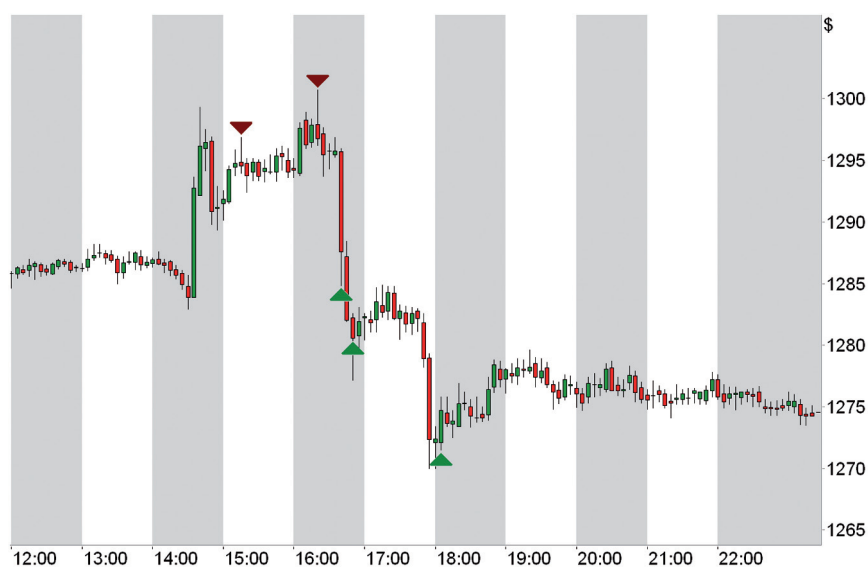
Kuyas: This is my way of trading these setups. The whole thing is based on lots of experience and I can control the typical risks of mental stops quite well by now. As a countertrend trader you (almost) never catch the final high or low, which is why the price needs a certain leeway. Precisely how much, though, I sometimes cannot exactly predict when opening the trade. In these cases, I use mental stops and decide on a discretionary basis whether to exit or give the trade a little more leeway.

F5) Elliott Waves with Gold



Gold fell significantly for several days before an A-B counter-pattern was formed (higher high and higher low). Orkan Kuyas now expected there to be a further upward thrust for the typical A-B-C countermovement to be complete. This very movement occurred on the evening of 28th June.

F6) Short Trade in Gold



On 17th July intraday Gold broke out upwards but approached the resistance at around \$1300 in the daily chart. Shortly after 3 pm, Orkan Kuyas bought his first few short certificates at 0.54 euros. After price broke out again but quickly fell back below the 1300 mark, he bought more certificates at 0.29 euros. Using the Elliott Wave Count, he had identified the target price of \$1268. During the speech made by Ben Bernanke shortly afterwards, Gold slumped, causing the trade to make a large profit. Kuyas initially placed the stop at the purchase price, then sold a portion of the position at 1.35 euros and later another portion at 1.92 euros. This was followed at around 6 pm by partial sale No. 3 at 2.50 euros. He let a small remainder continue to run, being stopped out two days later.

» Never let a trade that is already highly profitable turn into a loss again. «

TRADERS': When you set stops, what is the distance to the current price?

Kuyas: Depends on the time horizon. In DAX intraday trading there is a distance of between five and 15 points, in longer swing trades sometimes up to 50 points. I always try to have setups with a risk/reward ratio (RRR) of at least 2.0. That is, my profit should be twice as high as the stop risk incurred or higher. This in turn means that the tighter the stop, the sooner my minimum profit target is reached.

TRADERS': When and how do you exit trades again?

Kuyas: Regardless of any RRR considerations, it is first and foremost all about taking the risk out of the trade. So I will sell a portion of the position as soon as the trade has been initiated – and so much of it that the total trade ends at about plus/minus zero, should my stop be reached with the remaining position. This is in keeping with the basic rule: Never let a trade that is already highly profitable turn into a loss again. I will then watch price action on the basis of candlesticks and look to see how price behaves when approaching support or resistance. This will show me whether I should smooth the position or continue to let it run.

TRADERS': What underlying assets do you actually use when trading these setups?

Kuyas: Actually, I trade almost everything – stocks, currencies, commodities (except oil). That is people also like to call me the “Simon Cowell of trading” (*laughs*).

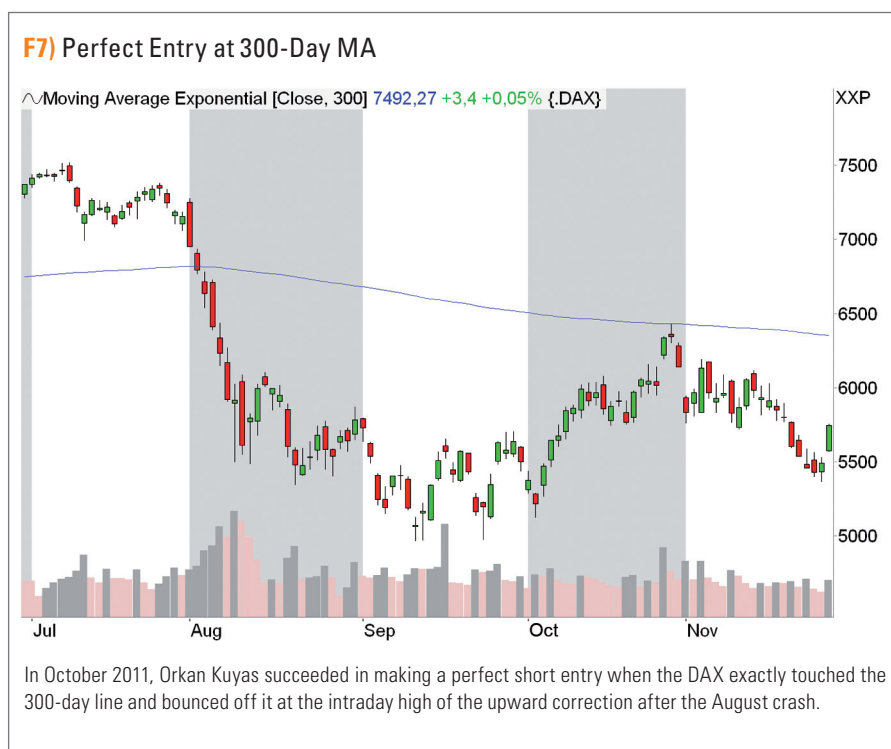
TRADERS': Why not oil, Mr Cowell?

Kuyas: Somehow I have never particularly liked the way the price of oil is moving. It just doesn't really suit my trading style. Come to think of it, though, oil would actually be perfect for longer term positions to hedge my fuel bill (*laughs*).

TRADERS': With so many trading instruments out there, how do you find the best opportunities?

Kuyas: On Sunday I sit down, take my time scanning the stocks, and watch the charts. That's how I find the candidates for my swing trades. When there are several similar stocks such as Daimler and BMW to choose from, I'll only enter a position in the stock that has the better support or resistance lines.

TRADERS': If the entire market has been particularly strong or weak for a longer period of time, does that have any influence on the number of new long and short trades?



Kuyas: It definitely does. For example, if the DAX rises rapidly by ten per cent or more, I will not enter any new long trades for the time being. Even more interesting are exaggerations in individual stocks. If the RSI is quoted above 80, for example, a correction is very likely to occur soon. I will then gradually build up short positions according to my countertrend setup. Incidentally, an RSI above 80 is a very good trading signal for the short side in the weekly chart, too. If there is a truly massive exaggeration, I will occasionally enter with larger positions than usual.

TRADERS': That's interesting. About how large would those be then?

Kuyas: For example, three per cent of the account instead of the usual one per cent. It's comparable to what a hunter does, watching out for such special situations and then pulling the trigger at the right moment.

TRADERS': Can you give us an example where things didn't go so well?

Kuyas: Of course, that happens too. In 2011, for example, there was a double whammy when the Fukushima disaster struck. Prior to the accident, I had been quite relaxed, initially holding my long trades overnight. Next morning all the positions were sent flying when the market opened with a downward gap, and the following

day saw a repeat performance. All this cost a great deal of money. Later, I changed back to the short side too early while the market was recovering from the slump. But the recovery was much stronger than I suspected, so I had to cope with some more losses.

TRADERS': And shortly after that the crash in August 2011, which was much worse?

Kuyas: I had previously been positioned predominantly long, but my positions were not going well and new long trades couldn't get off the ground. This made me suspicious and I watched the market more closely because something had changed. When the sale began, I finally switched to the short side where things were pretty much going my way. This was later followed by a super short signal occurring in October 2011 after the brief recovery: The market exactly hit the 300-day exponential Moving Average, and then immediately fell again.

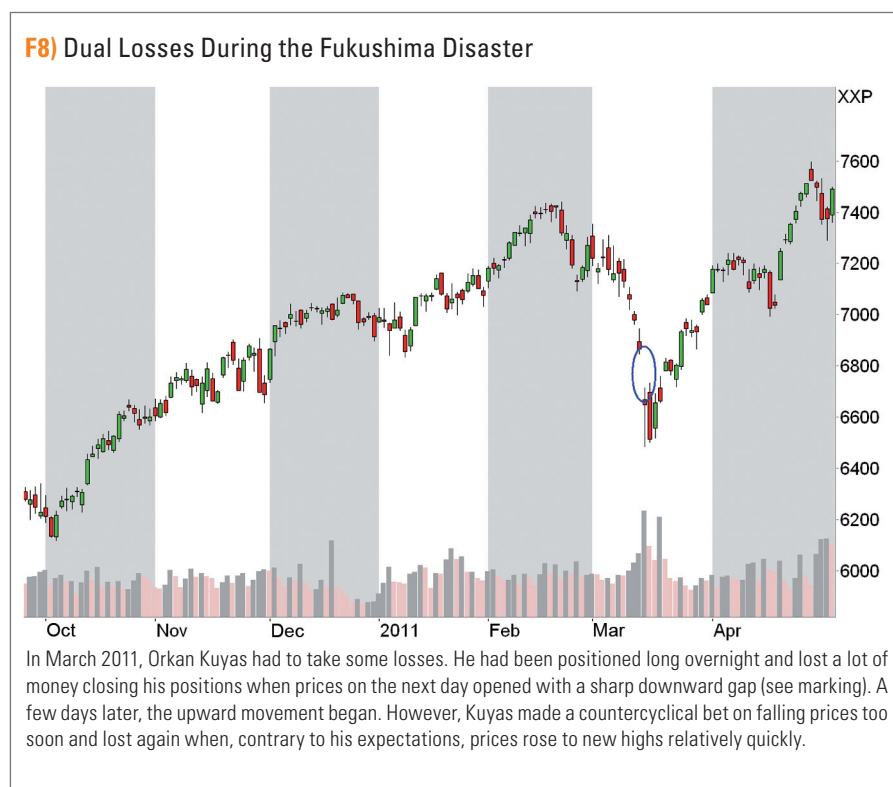
TRADERS': What do you think is the No. 1 mistake in trading?

Kuyas: Most traders do not respect their own risk management and some of them don't even have any. This is a sure path to failure. Otherwise, I advise traders not to pay too much attention to the media and if they do listen, to always interpret that as a countersignal. But the best thing is to simply ignore the entire media circus as much as possible.

TRADERS': What are your goals for the future?

Kuyas: I would like to continue working with the Facebook group as I have done before, in keeping with the motto: "Those who want to be successful in the stock market don't need a paid subscription service." The group continues to offer its services free of charge. In the future I would like to move more in the direction of swing trading, since I find day trading rather exhausting over the long term. And maybe I'll eventually have my own asset management company or fund. Who knows? «

The interview was conducted by Marko Graenitz.



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Brian Lund is co-founder of Ditto Trade and an independent trader who writes about the relationship between the markets and life in general on the StockTwits Blog Network at www.bclund.com

» Now first let me say that I think everybody should try to learn to trade. I also believe that learning to trade takes a lot of work, and it is not always evident right away whether or not someone will ultimately end up as a successful trader. But there are some characteristics that I see in people from time to time that are almost always “deal breakers” in terms of their ability to become successful traders. As long as they possess these traits, in my opinion they will never be successful at trading no matter how long and hard they try. If you possess one of these traits and are thinking of learning to trade, it is best to seriously consider, if this is something you are willing and able to change about yourself, or you risk having a very rough time in the markets.

1. Assuming Expertise in Some Field Will Translate to Trading

I don't care how great you are in sales, chess, astrophysics, yoga, or bull riding, none of those things will help you when you decide to learn to trade. Those that come in wearing their extraneous successes as a badge of honour, confident it will give them a leg up in the markets, will almost always end up busted, broke, and bitter.

2. Having a “Know It All” Attitude

We all know this person. They know everything. The mean temperature on Pluto during winter. How the President can fix the economy. Who built Stonehenge. These types will find out how much they don't know, and quickly, once they get in the markets. For them, trading will be their worst nightmare, one they probably won't survive.

3. Not Knowing When You've Had Enough

In middle school I watched a guy taunt a bully all day long, and then run away when the bully came after him. He kept doing this until the bully finally caught him, and I thought the guy would get what was coming to him. But surprisingly, the guy begged and begged the bully for clemency, and perhaps feeling a momentary flash of compassion, the bully let him go. And as soon as he

did, the guy started taunting the bully again. Suffice to say, when the bully caught him the next time, he kicked his ass. The guy didn't know when to stop, when he had pushed it enough. This is the guy that gets up for the day, but has to take “one more trade,” and gives it all back. Being up 50K won't be enough, because he could be up 100K, so he will push his positions and lose it all.

4. Not Understanding the Concept of Risk/Reward

I knew a guy in college. His standard move was, when drunk, he would climb to the top of the apartment complex he lived in off campus, and jump down into the pool in the centre courtyard. He loved this, as it gave him the distinction of being labelled a “party animal,” which was his “reward.” Then one night he missed. That was his risk. He still walks with a limp to this day. He didn't really understand the concept of risk/reward, but hey, all his drunk college buddies did think he was cool. Those with this character flaw are made mince meat of in the markets. They will take on three, four, five units of risk for one of reward. When you practice this inverse risk/reward relationship you can be right on 80 per cent of your trades and still blow your account out.

5. Being Afflicted with the “Babe Ruth” Syndrome

Everyone knows Babe Ruth (famous American baseball player) was a home run king. But “The Babe” was also the strikeout king. Of his “at bat” outs, 24 per cent of them were strikeouts. The average batter of his time only struck out twelve per cent of the time, meaning Ruth struck out twice as much as his contemporaries. It was all or nothing. Home run or strike out. In baseball you can get away with that, but not in the markets. You build your success with singles and doubles and if you are lucky, the occasional home run will pop up, but if that is all you are shooting for, you will in all likelihood have too many strikeouts. Those strikeouts will deplete your capital until you will get to the point where you can no longer play the game. «

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