

SUCCESS IS TIED TO MARKET DIRECTION

PURE LOGIC TRADING

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How many of you would like to put the odds of succeeding at approximately 70% in your day-to-day trading?

It is my goal today to help you understand the mind of the market day to day using some technical tools and methods of dissecting market activity that I synthesized from years of market study.

LET'S EXAMINE SOME RECENT HISTORY OF MARKET DIRECTION, BEHAVIOR, AND CHARACTER.

DIRECTION/CHARACTER

1999 Lots of trading geniuses

My office was full of successful traders...earning 100-1000% and more of their account values

Trading adversaries were flourishing...genius everywhere

Internet and high tech traders

AND THEN WHAT HAPPENED?

Mar/Apr 2000 MARKET TURNED DIRECTION

Guess What...9 out of 10 "genius" traders got wiped out

My office went from approx. 50 traders to 5

Guys that had made 500% and more on their money lost it just as fast.

CNBC and "Professional Analysts" buy/hold...stay the course strategies got completely wiped out

Major Funds were demolished...Some Icons of the industry were devastated...Soros, Dennis, etc

WHY?

Market direction changed...Market character change

WHATEVER SKILL LEVEL OR EXPERIENCE YOU HAD...IF YOU DID NOT CHANGE AND ADAPT TO THE NEW MARKET DIRECTION AND CHARACTER, YOU WERE PROBABLY EITHER WIPED OUT, SEVERELY DAMAGED, OR AT LEAST HUMBLLED (or should have been).

SOME OF THE TRADERS THAT DID CHANGE WITH THE MARKET ARE MORE PROFITABLE IN 2000/2001 THAN IN 1999

They “listened to the market”

They monitored the “internals” of the market, and of the vehicles they trade

Hedge fund friend...slammed Internets and techs...CIEN...

Bios/pharmas etc.

ANOTHER FRIEND...(name withheld)

Compartment caveat to overall market...

Trades long last 3 years (90+%)

Right Industries/sectors

Small caps

EXAMPLES

YHOO AMZN CSCO DELL ORCL SUNW INTC QCOM
STNR SCRI MEDQ EXPE PCAR MNTR SEIC ATRX MGEN

Before we delve into the technicals of assessing market direction, let's examine the simplest issues of market CHARACTER. HOW it gets from one price point to another. The market can move up or down in such vastly different fashions, or with different CHARACTER.

- Momentum market (b/o plays work)
- Stair step market (buying/selling pullbacks)
- Short impulsive, much longer fade/chop
- Range bound

Statistics clearly in favor of trading in the direction of the market (or trend) in the vehicle being traded. I would add to that the fact that the market ADVANTAGES come in shorter spurts now, and are often very violent...thus, the term character (that I use).

LET'S LOOK AT TYPICAL DAILY TRADING ACTION IN THE S&P 500.

S & P 500...and intraday CHARACTER

Imagine this picture:

End of day shows up 30 pts.

Advance/Decline 2.1

Up 20 pts first hour

Fades 10 pts midmorning/lunch

Up 20 pts last 1.5 hours into high of the day close

Net + 30 pts

First/last hour + = +40pts

30% increase of potential income

4.1 adv/dec during momentum versus 2.1 daily

This is an example of taking advantage of intraday market character; the character of the market changes during the day; trading the momentum phases outperforms the buy and hold strategies so often promoted

PUTTING IT ALL TOGETHER

- 1) Major market index (i.e., S & P 500 or Nas 100)

*Internals...volume (up/down), trin, tick

Note: will cover trin/tick in emini discussion

- 2) Sector, Group, Industry

*Internals there...i.e., Medicals moving, with bios and pharmas leading

- 3) Stocks

*FUNDAMENTALS do matter now...fundamentals equals internals IMO

*Trade the leadership...does not have to be large cap...in fact mid and small cap is where the action is now.

EXAMINE HOW I REVIEW THE S&P 500 GOING INTO THE TRADING WEEK

NOTE: This example is last week's worksheet that I took going into this week's trading. The information here was sent out to my subscribers.

SPX.X (S & P 500 CASH INDEX)

MONTHLY:

*closed <rising 50 sma...2nd time in >6 yrs

*closed within 2 pts of 1998 b/o pts of **1193**

*prices <**1160** to **1100** have been bought this year

*low of year = **1081.19**

WEEKLY:

*closed <10,20,50 ma's

*last week's doji bar failed to turn tide

*again...close near 1998 b/o pt...major support

*support from Mar/Apr highs app. **1183**

*closed < 50% retracement of Mar low: 61.8%=**1169.50**

DAILY:

*complex head and shoulders top...double shoulders both sides

*measured move to **1090** area

*89% success rate of pattern with vol confirmation (left shoulders vol>right shoulders).

*success= 5% move, which =59.5 pts from neckline=**1130.5**

*support @ **1183/low1170's & 1160's...major 1150**

*Mar/Apr up trendline from lows @ **1165** area

S & P AND NASDAQ EMINI FUTURES

WHY EMINIS?

- 1) Ultimate trading vehicle...most traders watch futures like a hawk to make stock trades; futures lead; usually get 1-4 good tradable moves a day
- 2) High liquidity...instant fills
- 3) Very technical...price, vol, trend lines, ma's
- 4) Internal technicals extremely helpful...cash, trin, tick
- 5) Huge advantage getting short...no uptick rule
- 6) Limit moves...almost free plays for big paychecks (watch cash)
- 7) Very liquid during pre-market reports, like unemployment...sometimes my trading day is made well before market is open
- 8) Huge advantage aftermarket...i.e., MSFT news and some good earnings reported aftermarket. You can just buy futures (globex), knowing the market is going to build on the news, and often sell pre-market for your days profits before the trading day begins
- 9) Your homework is very limited...It takes me 15 minutes pre-market to do my futures work, versus several hours a day to do stock scans and picks
- 10) You study one market, and your knowledge and feel for this market becomes more and more intimate...allowing your intuition to work for you

THE ESSENTIALS OF MY LAYOUT

4 Monitors

Left:

Cash...SPX.X over cash NDX.X

10/20 ema...50 sma

Pivot lines (floor trader numbers)

NY TICK

NY TRIN

NAS TICK

NAS TRIN

TICK...# of stocks on uptick versus # on downtick....

Excellent gauge of market health; very useful for unsustainable levels, overbought/oversold

Works back to zero threshold often in trending market

TRIN... measures breath-taking volume into account. Adv/Dec ratio to Up Vol/Down Vol ratio...

=#advances/# declines

adv. Vol/ dec vol

Generally...readings of 1.5 or > oversold; < .50 overbought

Need to get a feel for this with gaps, and market activity

10 EMA of trin...very useful historical tool for discovering oversold market conditions; not a timing tool, but usually within weeks of signal (1.3 or greater).

Note: I plot these graphically...have found patterns and thresholds work well some days

2 Center Monitors

3 day 5 min. chart

Bollinger Bands...standard with 20-ema center line

10 ema with 50 sma...slope of 50 ma determines trade mode note: trade info from Bollinger's

14 RSI ... note overbought/oversold conditions and divergences

Pivot lines... floor trader numbers

YH YL YC...TO

MACD histogram with signal line

Volume

OBV

UNDERNEATH...overlay

TICK CHART

Draw trend lines

Support/Resistance very evident in price clusters

Right Monitor

Ticker...high/low to follow leadership, and waves of color

Minder...Major indices, VIX, SOX, BTK...other leaders/+ or –

45 min. (10 equal bars)...moving linear regression

15 min Bollinger...snap fib's (my method)...use Candlestick information for major market turns and moves