

# Welcome to the Daytrading University!

DTU Campus Map:

*Module 4 is now completed.  
New Module 5 lessons and  
video content will be posted  
soon.*



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Entrance Page](#)



*Submit your  
daytrading  
screensnaps*

## **Module One**

### Essential Skills for All Daytraders to Learn:

Click on each link for a new daytrading lesson. Be sure to complete the trading worksheets and activities for each module.

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Click on each line for daytrading lessons from the list below. An underlined link means the content is now available. **Note: click on your browser's "reload" button to make sure you see the latest modules posted as they become available. Module 1's brief introductory lessons are for new traders, the bulk of the course materials are in Modules 2 and beyond - Enjoy! ...Remember to set your screen resolution to at least 1024 x 768 to enjoy DTU.**



Trading Lessons



DTU Module One Lessons:

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- [Example of a basic 2-monitor daytrading setup for new daytraders \(under 1 year experience\)](#)
- [Understanding how the different markets work: daytrading Nasdaq vs listed \(NYSE\) stocks](#)

- [Understanding how the different markets work: daytrading Nasdaq vs listed \(NYSE\) stocks](#)
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- [How to read relative strength and major sector stock patterns](#)
- [Developing trading discipline: using stops consistently for "insurance"](#)
- [Nudging more profit out of the trade: when to shake out](#)

F

#### "Fear of Trading"

#### Worksheets



[Click here for Powerpoint viewer program](#)

[Click here for MSWord view program \(3.5Megs\)](#)

- [Calling Tops and Bottoms](#)
- [Trading Skills Practice: Your Daily Trading Journal](#)
- [Opening Gap Trading](#)
- [News Plays: CNBC and Earnings Plays](#)
- [Daytrading Stock Pattern Recognition](#)

#### Activities

- [Choosing Your Trading Stocks](#)
- [Using Limit Buys, Trailing Stops and Market Sell Orders](#)
- [Scalping Under-\\$30 Stocks](#)
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**Getting Started: choosing an online broker and setting up your trading software**

● **Main Points:**

- Choose an online broker that has the **fastest execution speeds possible**. Secondary considerations include: commission price, availability of options, investment research support etc. Get the fastest ISP (eg Roadrunner cable modem) you can.
- **Selecting and using several software programs** that will help your trade successfully is a critical part of online daytrading that is frequently overlooked. **Thorough knowledge** of your trading and stock selection software is essential.

**Examples:**

**BROKERS** -There are many choices:

**DAT: Direct Access Brokers:**

Some brokers are set up exclusively for daytraders and charge a higher commission (\$15) than discount brokers. They give you touch-and-click executions and are good if you are an experienced trader and are ready to manage many executions and many order routing choices (eg ISLD, ARCA, INCA).

Some of these include:

- [CyberCorp](#)
- [MBTrading](#)
- [Tradescape](#)

Many of these use [RealTick](#) or [Esignal](#) trading software, which many professionals seem to like. I've heard mixed reviews on the RTIII platform.

**TRADING SOFTWARE** - Fortunately, there's some terrific programs that can help your trading immensely. Be aware that if you intend to daytrade for a living you should invest in professional tools, however (see examples at the bottom of the page).

Here's two "Must-Have" Free Programs:

**[Jerry Medved & Mike's QuoteTracker:](#)**



**Online/Other Brokers:**

There are many discount online brokers out there; *most* are totally unsuitable for daytrading and may give slow order executions and confirmations. There is nothing worse than getting in a trade and not having a confirmation for 15+ seconds.

In general, it's best to go with a direct access broker for the fastest possible fills.

Some of the others that are popular with traders include:

[Interactivebrokers.com](#) (aka IB)

[Datek.com](#)

IB has among the lowest commissions available, it's worthwhile to investigate several brokers to determine which one is best suited for your specific trading needs and abilities.

**[BigEasyInvestor:](#)**



We use it primarily for stock screening, has good lists to screen for, updates daily.

Powerful, professional software worth considering:

**eSignal:** I use eSignal daily to make a living. Terrific level 2 quotes, multiscreen support (I run 9 level 2 screens and 15 mini-charts on 4 17" monitors using eSignal; here's a screensnap; [CLICK here to see a recent 6-monitor display example \(scroll right\)](#))



### RTIII and Cybertrader:

Here's a screenshot of Cybertrader (below); it offer many advanced features not available elsewhere. RTIII (bottom of page) is also very popular. As with everything, I'd try out both and see which one you like the best. Consider investing in professional software and brokers once you've mastered the basics of daytrading (give yourself a year or so to do this consistently). Definitely [download and practice with the Cybertrader free simulator](#), it's great.



**Realtick:** Many professional traders use Realtick, Cybertrader is also popular

**Realtick III - SPEEDTRADER**  
 Page Design MarketMaker Window Help

TOP 10 GAINERS TOP 10 LOS TOP 10 AC... NYSE ACTIVE PENDING ORDER TRACKER

Symbol	Last	Change	Symbol	Last	Change	Symbol	Last	Change	Symbol	Last	Change
DISHP	323	+12 3/16	GNFT	139 7/16	-12 11/16	CSCO	53 1/2	-1 7/8	CPQ	23 3/8	+1 1/4
ELNK	58 1/2	+10 7/8	PHSY	74	-11 5/8	DELL	37 15/16	-1	AOL	103 3/4	-5 5/8
PHCM	82 11/16	+6 11/16	PHSY	73 15/16	-10 13/16	MSFT	86 11/16	-2 1/4	ABT	43 1/2	-11/16
CUST	43 1/2	+6 1/4	CMGI	93 9/16	-9 7/16	COMS	31 1/2	+9 1/8	AZA	49 7/16	+3 3/16
MAIL	13 5/8	+5 11/16	YHOO	151 15/16	-6 15/16	EGRP	39 7/16	-1 1/4	EMC	55	-4 5/16
DISH	158	+5 1/2	NSOL	65 9/16	-6 7/16	INTC	56 5/16	-1 1/2	LU	62 1/2	-2 7/8
VISX	79 7/16	+4 15/16	LCOS	91 1/16	-5 9/16	ORCL	34 5/16	+3 1/8	IOM	4 3/4	+5/8
MSPG	74 19/32	+4 21/32	AMZN	118	-5 1/2	ATHM	55 1/16	-2 13/16	MCK	32 13/16	-7/8
ADLAP	199 3/8	+4 3/8	FLEX	53 1/32	-5 7/32	YHOO	151 15/16	-6 15/16	G	42 5/16	-1/16
RAMP	16 3/4	+16 3/4	ASND	102 3/8	-5 1/4	ELNK	58 1/2	+10 7/8	T	56 3/16	-5/16

YAHOO INC. SPEEDTRADER TRACKER

Symbol	Last Price	Bid	Ask	Net Chg.	High	Low	Open	Tot. Vol.
\$INDBL	107 27 9/16			-88.01	10879.62	10639.95	10768.49	
DELL	38	37 15/16	38	-15/16	39 7/16	37 15/16	39 1/8	1185900
IBW	124 1/2	124 1/4	124 1/2	-1/4	127 3/4	123	123 7/8	1470600
EGRP	39 1/2	39 1/2	39 9/16	-1 3/16	43 5/8	39 1/16	41	103500
MSFT	86 5/8	86 5/8	86 11/16	-2 5/16	88 7/16	86 1/4	88 7/16	7751800
YHOO	151 3/8	151 3/8	151 7/16	-7 1/2	166 1/8	151	157 3/8	1967900
CSCO	59 37/64	59 9/16	59 5/8	-1 63/64	62 3/4	59 9/16	61	1878200
NETA	14 7/8	14 7/8	14 15/16	+1/16	15 13/32	14 1/4	14 13/16	3721700

YAHOO INC. E TRADE GROUP INC

Symbol	Last Price	Change	Volume	Q	High	Low	Open	Close
YHOO	151 15/16	+6 15/16	400	15:51	151 3/4	150	151 3/4	500
High	166 1/8	Low	151	Acc. Vol.	11942000			
Bid	151 11/16	Ask	151 13/16	Close	158 7/8			

Name	Bid	Size	Name	Ask	Size
ISLD	151 9/16	11	ISLD	151 13/16	9
PERT	151 1/2	5	REDI	151 7/8	3
USCT	151 1/2	1	ARCA	152	7
COWN	151 1/2	1	HRZG	152	8
SBSH	151 3/8	18	AGIS	152 1/16	2

Price: 151 3/8 Volume: 1000 Route: MKT Expiration: Day Bid/Offer:  Short

Margin: Buy YHOO Sell YHOO Cancel All YHOO Pref:



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Successful Online Daytrading Training Resources

Example of a basic 2-monitor daytrading setup for new traders

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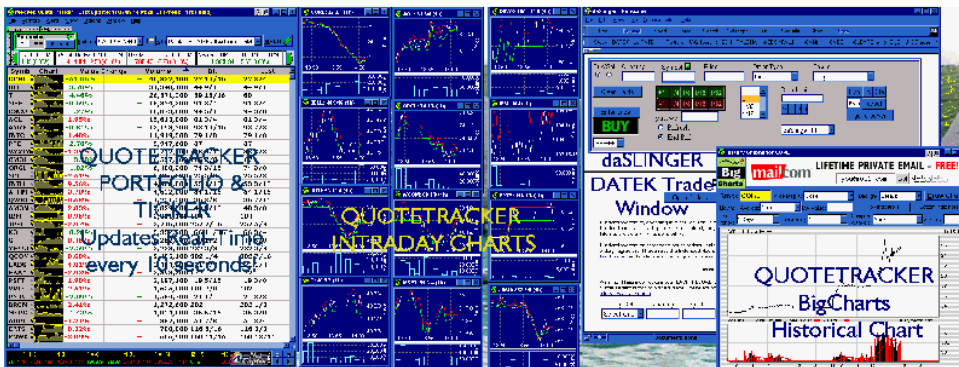
● Main Points:

- Experiment with many daytrading software setups until you find one that is comfortable for you.
- For new traders, we highly recommend using the free [www.QuoteTracker.com](http://www.QuoteTracker.com) software with [www.datek.com](http://www.datek.com) as a broker. Use daSlinger at [www.sapphirebay/trading/](http://www.sapphirebay/trading/) to enter buy and sell orders on datek; it speeds up the process quite a bit.
- Use [www.bigeasyinvestor.com](http://www.bigeasyinvestor.com) to screen for stocks.
- There are many features available in the different programs, you have to define what works best for you. I constantly experimented my first year with different setups, probably over 40, before settling on my 4-monitor pro trading screens. Here are some nice setups for RTIII pro screens at [www.phactor.com](http://www.phactor.com). The RTIII advantage is that you can choose how to route your order to the market, and you can do it faster than online brokers. I find Datek generally acceptable for now, I will probably migrate to a Cybertrader or RTIII-based system eventually.

Here is an example of how I would set up a beginning daytrading screen for you if you have two monitors. You can daytrade with one monitor, but it is so much more difficult to shuffle all the windows. I'd spend the \$250 for another 17" monitor and pci display card. You should have your screen resolution set to 1024x768 pixels (800x600 minimum).

Examples:

If I had two monitors and was in my first 6 months to year of daytrading, this is how I'd set up my system: [Click for fullscreen view:](#)



**Monitor one:** Quotetracker realtime portfolio, stock ticker and a handful of intraday 10-second charts.

**Monitor two:** more intraday charts, the daSlinger datek trade interface in a web browser, and a quotetracker bigcharts.com historical chart/news window.

If you have \$2K or so to invest on the frontend, I would strongly recommend getting a level 2 setup from [www.esignal.com](http://www.esignal.com) . (\$79/mo + \$50/mo nasdaq L2 = \$130/mo). More than worth it when you're trading fast and trying to scalp. Don't try to make a living daytrading NASDAQ stocks without level 2.

I still use [QuoteTracker](#) almost daily for news updates, it has the best news manager I've seen out there. All in all a very nice program I've used for hundreds of hours over the last couple years.

Let's see, what else? Mainly, experiment to see what's best for your trading style. If you have trouble with colors, experiment with different chart backgrounds, font sizes, data intervals etc. Each individual has their own preferences, and I would encourage you to try many combinations at first. It took me many months to settle on the trading rig I like the best.

**Understanding how the different markets work: daytrading  
Nasdaq vs listed (NYSE) stocks**

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● **Main Points:**

- In selecting stocks to trade, do not neglect the entire listed / NYSE market. Listed stock plays can be profitable, with the added advantage that those who do not yet have level 2 are still on a 'level playing field' with other traders. Most daytraders play Nasdaq tech stocks, however (as you'll see later) there are many other profitable stocks to play that are out of the limelight and still have enough volume and volatility to provide profitable daytrading opportunities.
- In general, Nasdaq stocks move with slightly more volatility due to daytraders' influence, and are thus 'more exciting' and can be more profitable. Beginning traders are recommended to play stocks in both markets, using market volatility and volume indicators as suggested later in the module.

**Examples:**

**Daytrading Stock Market:**

**NASDAQ**

**NYSE**

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- Many daytrading stocks to play
- High volatility in select stocks
- Level 2 provides substantial advantage in Nasdaq trading if you have streaming Level 2 quotes
- Rapid trade executions
- Fast moving stocks are available to play; along with IPO opportunities
- Most hi-tech growth stocks are in the Nasdaq, providing high-percentage trade opportunities with technology stocks to play
- Shadowing the ax on Level 2 works

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- Slower moving stocks give you time to enter and exit trades without hurrying
- No Level 2 means all traders on a relatively level playing field
- Less volatility also means a lower-risk, (albeit lower-reward) trading field to start in.
- Charting and technical analysis works just as well for listed as Nasdaq stocks; chart patterns are profitable to play in NYSE stocks.



- Volatility and speed can ruin your trading capital if you don't know what you're doing
- Level 2 provides substantial disadvantage for those who do not have it. Intraday Nasdaq traders are encouraged to try a level 2 service to see the difference.
- The most experienced traders in the world trade Nasdaq stocks; you are going against the best of the best, who want to take your money.
- PROFITABLE NASDAQ TRADING: depends on playing selected stocks (using Level 2 if possible) for quick momentum plays, buying on the bid and selling on the ask for scalps and large moves.
- PROFITABLE NYSE TRADING: depends on your ability and patience to know technical analysis and chart patters, trading ranges and how to enter and exit with carefully placed limit orders.
- Less volatility means your trading percentages will be lower in general daytrading NYSE stocks.
- Slower trade execution by specialists mean you may not get the best price available, losing 1-2 spreads per trade and getting filled more slowly.

**In Summary:** Try both markets - in general, the NYSE stocks w/good volume (>400K) are relatively easy to play, while the Nasdaq stocks have lots of volatility and intraday price movement. Listed stocks slower on news and earnings/M&A reports than Nasdaq stocks do, so you have more time to manage your trades with listed stocks. Try both!



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**Daytrading Educational Books & Resources: Our Top Picks to Learn How to Trade Better**

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● **Main Points:**

- **"Give a man a stock pick, he may or may not win. Teach a man How to trade stocks, and he profits for a lifetime** (and lives in Hawaii with a nice wife and goes golfing and..lol). My best advice to all traders who hope to prosper is: you can genuinely achieve financial independence, at the price of honest **hard work, study, discipline and knowledge**. Like anything else worth having. It's up to you to decide whether or not you're serious about this business.
- Ongoing education is important to your success as a stock trader. Look at daytrading like a **2-year degree program** and you'll be in the right frame of mind. Consistent studying and hard work is required to earn consistent profits from the market. This is not gambling or "playing the market to see how you do". This is how to pay the rent. Expose yourself to enough winning trading ideas and strategies, and you can achieve success if you apply them intelligently. By joining DTU, you've shown that your attitude to get an edge is there; application and follow up is where the money's at. Let's do it.
- **Losers and gamblers** look for "stock pick" sites, hoping for others to make trading decisions for them. To take consistent profit off the street, you must learn how to enter and exit successfully. Picking oversold/overbought tops and bottoms off support and resistance sounds fine, and in time, you'll learn how to do some of that. But the way professional daytraders make a living is providing liquidity bidding and selling stock like a market maker does (vs. paying up 2 spreads and hoping for a homerun trade). Market makers love guys like that. They take your money, with the commission churn eating up the rest. Not the way to play.
- Having said this, I'll still post a few stock picks (like the recent SPLS pick at 17 1/2 that ran to 24 3/4 in 4 days, predictably; good for intraday plays). In the meantime; here's a few books and other resources I'd recommend that you take a look at when you have an opportunity; they've helped me trade more effectively.

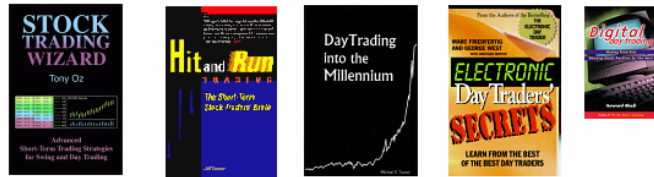
**Examples:**

These books are the ones I've found most helpful. See amazon.com for descriptions, evaluations and other information. Building a trading library for \$200-\$400 is the First thing you should do (vs. running out

and losing the same amount ++ in the market the first 6 trades you make; or, losing more than you need to for those who are experienced in trading for a living). All books are linked to their descriptions at Amazon.com



### "Must-Reads":



### Also interesting to check out:



[Complete](#)  
Idiot's  
Guide to  
Daytrading  
(really!)



### Videos:



[www.daytradingvideos.com](http://www.daytradingvideos.com)

### DTU Trader's Picks:

Let us know what your favorite trading book(s) are; we'll post the results monthly. Just [email us!](#)

Barry D. from FL recommends: "[Reminiscences of a Stock Operator](#)" by E. Lefevre

### Profitable trading idea #173:

Go through these books, highlight specific trading strategies that the authors feel are important and summarize them on 3x5 cards (especially ideas and techniques that more than 3 authors seem to agree on, e.g., "use small stops and let the winners run" lol)

Next, [keep a trade journal](#) and figure out which of your winning vs. losing trades use these trading strategies.

Finally, develop a trading plan that applies trading strategies for timing, entries and exits.

These are all basic ideas, but many traders I've worked with skip them and **end up making the same mistakes over and over again**. Then they beat themselves up.

**It helps to have structure until all this becomes automatic.**



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Successful Online Daytrading Training Resources

● **Main Points:**

- **In daytrading, you should get as many things stacked in your favor as possible prior to entering a trade.** We will go through a "checklist" of things to look for that you should memorize and practice paying attention to prior to buying stock. It's a balance: you can't wait til "all the planets line up" or you'll be buying the obvious top, where faster traders are selling to you. If you enter without having *any* of these things in your favor you are increasing your risk, however.
- It's helpful to evaluate trade risk management and entry/exits **like a funnel**, with **broader market dynamics considered first** (naz/spoos up or down?), the **sector** you're playing considered second (eg \$SOX, \$GIN), your stock's **5-day trend** support/resistance levels considered third, and finally **level 2 & time and sales momentum, volume, RSI, MACD and other technical chart patterns & indicators** for your specific stock considered lastly. Don't buy stock if the overall market's tanking, it may take level 2 a brief time to 'catch up'. Anticipate larger market direction first, then use level 2 to time your entries, exits and trade sizes.

**"A Day in the Life of a Professional Daytrader"**

**Premarket Action**



- Get your trading rig set up at least an hour before the market opens. Turn on CNBC & get some coffee.
- Read the online headlines on [CBS Marketwatch.com](#) and [ZD news](#), others if you want. Put a few of the "Stocks to Watch Today" in your software watchlist if they meet our general [trading criteria](#).
- Also look at these two 'big picture' considerations to help you "prepare for battle":

**S&P Futures on CNBC at 9:25am**

This tells you which way the market will open, not necessarily the overall trend for the next 30-60 minutes. If the S&P futures (spoos) are up over +8 or higher premarket that's bullish etc. Remember the market may open high and turn down on a dime at 9:40am. Wait to enter your stock buys til after 10am in general.

**CPI/PPI Reports Out Today? Is Greenspan Talking? Triple Witching Friday?**

Any of these three factors can influence the market in either direction. **Be aware that there is likely to be more volatility on days when these events occur.**

**Premarket Gaps  
Up or Down on  
Volume >20K**

This is CRITICAL to look at if you're going to be trading during the first ten minutes of the market open. **How far has a stock gapped in either direction premarket, and on what kind of volume?** If CSCO has gapped down 2 1/4 points premarket due to a bad news story, how do you play it? Probably buy the gap down on open if buyers start to come in.

If AMAT gaps up + .8 on positive earnings news premarket, how will you play it? Probably short it on the market's open, if you think it will sell off due to profit taking.

A final note: Make Sure to keep an eye on your stock premarket using the [island java book](#) and Level 2 (if you have it). If I have a rare overnight hold, I will frequently sell it off at 8:30-9:15 on ISLD before the market opens if I'm up with a decent profit.

In general, I usually sell into the opening momentum and wait til at least 9:35 (after initial open orders are cleared) to trade. My favorite trading times are Tue-Wed-Thur morning 9:35 til 11am. Volume tends to be lighter monday mornings, slower opens, so I avoid them. I usually do not trade the afternoon, as the pace is often slower.

**Market  
Opens**

**Ding ding.** Ok, the market's open. **There's several distinct "trading waves" in the first half hour of the market open, from 9:30 thru 10:00.** In time, you'll be able to 'feel' the momentum of these waves based on buying and selling momentum, pace and volume.

**You should almost never buy an opening gap up;** there is a favorite market maker trick called the **"gap and trap"**; designed to lure in traders who think a stock is hot and headed up. Eg EBAY closed at 57.65 the day before, now it opens at 58.8 and ticks up to 59.5 by 9:32am. Do you buy? **Probably not.** *Not unless you see higher highs and higher lows sustained for a few minutes on higher-than-average volume.*

Wait for an initial pullback to buy any stock on the open, to see how deep the pullback is. If it continues all buyers, then you might want to jump on board. **It will usually, however, sell off** as market makers who have shorted it on open will continue selling until daytraders start panicking out of their positions.

**9:30 - 9:40ish:** The first market action occurs: a rush of buying or selling. You should be following the overall Nasdaq composite index at this time very carefully. See my [4-monitor trading screen setup](#); on the far right the two large black

indexes are the \$COMPQ and the \$TRINQ. I always look at these first before, during and after I trade stocks. I also watch sector index charts, like the \$SOX and \$GIN.

**9:40-9:50:** The first reaction wave occurs; either the trend continues or starts to reverse from its initial direction. Pay close attention here.

**9:50-10:00** The main thing to remember is that the market will frequently change direction several times in the first hour of the trading day, from 9:30-10:30. Be sure your trades are on the right side of the composite trend.

**10:00** Market Pivot time: this is a key time for the open, if the market's been getting buyers 9:30-10am, here is where it will often reverse directions and vice versa. I usually close open positions I've had from say 9:52 at 9:58 am type of trading.

**10:15 - 11:30** This is a time where I trade many of my positions (60%). My daytrades are rarely longer than 15 minutes roundtrip each, unless the stock is on a steady climb up.

**11:30 - 1:30** "Deadzone Hours": Play with caution. Usually I will short a top that's starting to weaken during the low-volume, dangerous lunch hours. This is the time where stock usually stays flat or declines. I usually sit out the lunch zone.

**1:30 - 3:00** Another trade window, somewhat less volatile than the morning, I make around 10% of my trades during this time.

**3:00** Bond Markets Close: Look for sell/buy programs to kick in.

**3:00-4:00** Final hour to trade for the day; **the second-best time to trade stocks. I may do some trades here, especially friday afternoons, if the COMPQ is making a 2day high or low.** Hint: stocks usually continue their opening pattern during this time (if it trended up in the first 2 hours, stayed flat/down over lunch, it will probably trend up during the last hour as well).

The only exception is if a stock has been downtrending all day, in which case short covers may cause a small "cover rally" in the last half hour. These can be profitable and explosive plays; I've frequently seen stocks gain back 1-3% in 30 minutes here.

## Market Closes

**Post-Market plays:** If you want to see if you can get some casual investor to "buy the news" on a stock you bought and held earlier in the day (overnight/swing traders), you may want to offer to sell it on ISLD after market for a nice profit.

**How would you daytrade in the next 15 minutes, based on these two charts??**



Note the \$TRINQ went all the way to 1.45 before having a sharp reversal, when the Nasdaq composite started up. The \$TRINQ is now consolidating and headed upwards, which corresponds to a downtrend in the Nasdaq index for now. Use the two in combination.

We'll get into daytrading chart patterns and TA in a later lesson. For now, here's a profitable chart combination I use all the time:

- Nasdaq Composite Index 1-minute close line chart
- Nasdaq TRIN 1-minute close line chart: the \$TRINQ is a great contrary indicator for the Nasdaq; I use it in conjunction w/\$PREM, \$TYX, SP9 and the leading indicators to confirm market direction, pivots and trend reversals.
- **Pro Daytrading Tip:** In general, I am hesitant to buy stock long if the \$TRINQ is >1.0 and am looking to go short when the \$TRINQ is >1.50 (or, I'm looking for 'when will it bounce?'). If the \$TRINQ is under 1.0 I am much more comfortable in taking a long position, and am aggressively looking to buy stocks if the \$TRINQ is <.70.
- Many traders also use the spoos/naz futures/\$PREM/\$TYX as leading indicators.

Here's a screensnap of the nasdaq composite index and \$tring for a recent day:

**A quick intro to Level 2 screens: (we'll have much more in Module 2 on Level 2 Trading)**

MMID	Bid	Ask	MMID	Ask	MMID	Ask	MMID	Ask	MMID	Ask	MMID	Ask
NOVL	17 7/16	17 7/16	17 1/2	21 x 30	2.02K	1214						
NSLD	17 7/16	20	INCA	17 1/2	30	12-15	17 1/2	200				
NRUT	17 7/16	10	ISLD	17 1/2	17	12-15	17 1/2	500				
NRTR	17 7/16	10	ETRD	17 1/2	10	12-15	17 7/16	100				
NSCO	17 7/16	10	NASH	17 1/2	1	12-15	17 7/16	200				
NALCO	17 7/16	10	SLKC	17 7/16	1	12-15	17 1/2	200				
FBDO	17 7/16	10	LEHM	17 7/16	1	12-15	17 7/16	1.00K				
BEST	17 7/16	10	NLCO	17 5/8	10	12-15	17 7/16	800				
WEDA	17 7/16	10	SHAD	17 5/8	5	12-15	17 7/16	500				
AGED	17 7/16	1	NITE	17 5/8	1	12-15	17 7/16	500				
WSTI	17 7/16	1	SWST	17 5/8	1	12-15	17 7/16	400				
DNHT	17 3/8	20	FCAP	17 5/8	1	12-15	17 1/2	1.00K				
RSHI	17 3/8	20	JHMS	17 5/8	1	12-15	17 1/2	1.00K				
INCA	17 3/8	15	BESH	17 1/2	10	12-15	17 1/2	2.00K				

MMID	Bid	Ask	MMID	Ask	MMID	Ask	MMID	Ask	MMID	Ask	MMID	Ask
SBUX	24 1/16	24	24 1/16	10 x 10	533K	9:59						
NSCO	24	10	ETRD	24 1/8	10	9:59	24 1/16	200				
NRUT	24	1	WADI	24 1/8	20	9:59	24 1/16	2.00K				
NALCO	23 15/16	10	ISLD	24 1/8	12	9:59	24 1/16	400				
WBLR	23 15/16	1	NASH	24 1/8	10	9:59	24 1/16	100				
NSCO	23 7/8	10	OLDE	24 1/8	10	9:59	24 1/16	200				
GNWC	23 7/8	1	NSCO	24 1/8	10	9:59	24 1/16	500				
LEHM	23 15/16	1	NRUT	24 1/8	5	9:59	24 1/16	500				
NRUT	23 1/2	10	NFSC	24 1/8	1	9:59	24 1/16	500				
BASH	23 3/4	10	NWSE	24 1/8	1	9:59	24 1/16	1.00K				
DLJP	23 3/8	10	DNKS	24 1/8	1	9:59	24 1/16	1.00K				
PRM	23 3/8	1	SLKC	24 1/8	1	9:59	24 1/16	200				
FBDO	23 3/8	1	DBAN	24 1/8	1	9:59	24 1/16	1.00K				
SWCO	23 3/4	1	JHMS	24 1/8	1	9:59	24 1/16	200				

This is a **bullish level 2 screen**; eg many buyers at 17 7/16 and not many sellers. You should Buy Limit Bid 17 7/16 to join the ISLD buyers, or buy Limit at 17 15/32 to front run the current inside bid.

Note the green sell (2nd inside ask) band is paper-thin with only 2 mm's at 100 each, where there's a lot of heavyweight mm's bidding 10 deep. Again, level 2 must be the last thing you look at, also consider chart trends and market direction.

**Decimal trading note:** I will be updating many of the lessons to reflect decimal trading during 2002.



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This is a **bearish level 2 screen**, notice how many sellers (a wall of sellers) to go thru at 24 1/8 on SBUX. Also notice how thin the support levels are on the bid side, only 1-2 market makers at each of the next 4 spreads.

Buying here is a no-no; it's unlikely all the sellers will step off the 24 1/8 ask and let the price go up. This is the advantage Level 2 provides, you can see how deep the buyers vs sellers really are.



## How to choose stocks to daytrade: screening for high-percentage stocks

### ● Main Points:

A Common Mistake new traders make is to try and daytrade either:

- **The Top 10 Most Active Nasdaq stocks** (MSFT INTC CSCO WCOM etc) or
- **Cheap \$2 -\$10 stocks** because they only have a few thousand in capital

**The stocks that you daytrade should have the following characteristics:**

- Average **spreads** of less than .15
- At least 1.2Million shares per day **average daily volume** (prefer 2M+ optimum)
- **Intraday average trading range of 5% or better** (eg a \$40 stock should have a \$2 intraday range (AMAT), a \$60 stock should have a 3-point range (EBAY) etc. Where you get into "low-percentage commission churn daytrading" is trading 300-500 shares of MSFT at 65 with a 1 point intraday range, for example.
- You can also profitably play IPOs, news plays, earnings plays, upgrades/ downgrades and others, but for now I want you to start thinking about 3-5 stocks that you want to trade regularly.
- **Price of around \$25 - \$60** with a 5% intraday range are my favorites, best sectors are software, semiconductors and biotechs (for year 2002) you can of course also play the net stocks (EBAY), and other sectors as you wish.
- Here's a new one **for Level 2 players: make sure your stock has one of the "four horsemen" as an ax (MSCO MLCO SBSH GSCO)** vs archips "chippies" ARCA INCA that move the stock. Learn to follow these axes in and out of trades.
- [See this page](#) for how to choose stocks for swing trading (2 days to several weeks); including chart patterns.
- **My Favorite Daytrading Stocks for Year 2002: (SOX):**  
AMAT BRCM NVDA GNSS MXIM NVLS QLGC XLNX  
(GSO): CHKP SEBL VRSN VRTS (NBI) AMGN HGSI GENZ  
MLNM ; others: EBAY BRCD EMLX

### Examples:

I like [bigeasyinvestor.com](http://bigeasyinvestor.com) (free software) for screening as well as the one at [www.financialweb.com](http://www.financialweb.com). The best scanner out there is [Tony Oz' Scanner](#) for Realtick.

for Realtick.

Here's a page on the subject from the registered "Daytrading Stocks Successfully" Screensaver:

**"7 Deadly Mistakes to AVOID In Daytrading"**

Mistake #1:

**Don't trade the most active stocks only.**

**What to look for:**

- + Look for stocks that have between 300K-3M daily volume.
- + MOST IMPORTANTLY: Look for stocks who have a good intraday trading range for their share price.

**Example:** The trading %ages are better for a \$22 stock like SPLS with a 1-pt range than a \$90 stock like MSFT with a 2-pt range.

Company Name	Symbol	Price	Vol	Change	Percent Change	Volume	Open	High	Low
Intel	INTC	57.80	5.5M	2.0%	7.0%	21,225,400	56.00	58.00	56.00
Microsoft	MSFT	89.14	3.27M	0.8%	1.0%	7,173,970	88.00	90.00	88.00
DELL	DELL	18.35	3.87M	-0.8%	-4.3%	17,707,200	19.00	19.00	17.00
IBM	IBM	117.80	3.72M	0.8%	0.7%	1,890,700	117.00	118.00	117.00
Google	GOOG	475.80	1.88M	5.1%	5.1%	2,854,300	460.00	480.00	460.00
Amazon	AMZN	110.45	3.7M	1.3%	1.3%	11,460,000	109.00	111.00	109.00
Microsoft	MSFT	89.14	3.27M	0.8%	1.0%	7,173,970	88.00	90.00	88.00
Sym	SYM	102.85	1.87M	2.2%	2.2%	11,180,000	100.00	103.00	100.00
IBM	IBM	117.80	3.72M	0.8%	0.7%	1,890,700	117.00	118.00	117.00



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## Avoiding the "7 deadly sins of daytrading": how to stay in the game

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### ● Main Points:

The **FIRST** goal you need to have in daytrading is "How Can I Play Without Losing My Capital?".

The **Second** goal is "How do I make Profitable Trades based on things I Now Know to Look for?"

The **Third** Goal is "How Can I Make Consistent Profits by Daytrading Stocks?"

Without mastering the protective loss-avoidance techniques and high-percentage trading pattern skills, daytrading resembles gambling and over time will consume your capital trade by trade until you're out of the game. This is what happens to the majority of people who attempt daytrading without educating themselves or getting training.



*Do you golf?* Remember how important it is to avoid getting bad swing habits early in your career? Let's try to avoid topping the ball and slicing when it comes to trading:

**Below are 'Seven Deadly Sins of Daytrading' that you should add to your mental checklist before entering a trade. These help you with the first goal, preserving your capital:**

### **The "7 Deadly Sins of Daytrading":**

**#1: DON'T TRADE THE MOST ACTIVES:** we mentioned this in the page on choosing stocks to trade. The most actives also have the best traders competing on them, and volatility is often lower. Your %ages are much better on stocks one level back, in similar sectors (e.g. don't trade INTC, trade ALTR or XLNX instead. Don't trade YHOO, trade DCLK.)

**#2: DON'T TRADE DURING LUNCH "DEADZONE" HOURS:** many losing trades occur between 11:30 and 2:30 EST. The best time to trade is during the first 2 hours of the market. We'll cover more in our pages on timing entries and exits. Volume is lower during lunch hours and the market makers will not buy as much stock in this time window. More games and fades. Shorting, however, is usually fine around 11:30-1pm (in general) for stocks that are making lower highs and lower lows. Market makers often bid the price down to shake out weak traders over lunch and buy it back in the afternoon, making for eod short cover rallies.

**#3: DON'T RATIONALIZE LOSING TRADES:** the ONLY

REASON you buy a stock is because you think (or see) that OTHER TRADERS ARE ALSO BUYING THAT STOCK AT THAT MOMENT. If you're wrong and there's more selling than buying, get out fast. Just do it. The market honestly doesn't care about the stocks fundamentals, earnings, ratings etc. during the next 20 minutes that you're in that particular trade. If you're wrong, **wisely admit the small defeat and take a small stop loss.**

**#4: DON'T CONFUSE DAYTRADING WITH INVESTING:** this is one of the biggest hurdles for new daytraders to overcome. If your trading style is, like mine, in for anywhere from a few minutes to a couple of hours tops, you do not care about all the "noise" such as analysts ratings, the 30day moving average, 2month support and resistance levels...you play on momentum only. Are more people buying the stock now, and for the next few minutes or half-hour or so? That's what counts in daytrading. "INVESTMENTS ARE DAYTRADES GONE BAD". Don't hold dog stocks that went against you and you're holding on hoping for a turnaround someday. That's how to lose money. If you're way down and the stock has stabilized and isn't selling, then maybe hold them. Don't get into that predicament in the first place.

**#5: DON'T FIGHT THE TREND.** What an insightful statement. :p Daytrading successfully means to understand and **capitalize on the trading trend with 4 times more focus and concentration than you currently use.** Make sure to learn how to "read the tape", if you don't already have **level 2 time and sales** then at least look at the [java island book viewer](#) (updated realtime during market hours!) for your stock to get a partial picture of what's going on in a given day. The datek streamer is a similar device, not complete but ok if you're just starting in daytrading. One of the keys for my 'turning the corner' was to focus on just a few stocks I know like the back of my hand and follow them with intense concentration. I know the market makers, gaps, intraday trading ranges etc. and make money 80% of the time I trade these (SPLS DCLK NOVL my current favorites).

**#6: AVOID LOW-VOLUME "PUMP & DUMP" \$1-\$10 CHATROOM SPECIALS.** I wince every time I log into one of the free stock chat rooms and see people ("sheeple") following stupid stock calls on junk cheap stocks. I feel sorry for all the trading losses I witness. To learn to be a pro, play like a pro. Read the books, check out some of the good resources out there, and IGNORE THE JUNK FREE STOCK CHAT ROOMS. I won't name any names, but there's plenty I'd avoid. They're good for companionship and fun, but dont follow the crowd. Overall, I'd recommend the pay chat rooms for *learning how to trade* vs. playing the stocks that are called. There's a couple of good ones out there, but again, I can usually out-trade the 'room gurus' so they're a waste of resources for me, and a distraction.



**#7: FAILING TO LEARN FROM ONE'S MISTAKES.** Ask yourself questions such as: "What did the market teach me today?", "Where did I trade well, and why?" "Why did I lose on that last trade, and how could I have made the loss smaller?" "How can I build more consistent trading habits that will help me profit?" Use a [Daily Trading Journal](#) to help you figure out what you're doing right and what needs work.

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**The difference between daytrading and investing: stock research tips for daytraders**

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MODULE 1

● **Main Points:**

You can easily lose money daytrading the highest-rated growth stocks in the market (ex's: QCOM JDSU ADBE MSFT etc). *Daytrading requires us to use a much finer "magnifying glass" than investors and analysts use.*



Just because a stock has a ton of volume, has a great 120-day MA or uptrend, and is frequently talked about in the media does not mean it's the best stock for daytrading. Be sure to review the [stock-choosing tips page](#) to see if your stocks meet the criteria.



Mentally, this is a difficult concept to translate into practice as an intraday stock trader, which we are. According to Gary K., one of my students, "most of the time I feel like I'm looking for a needle in a haystack".

This is often the case, and it can be frustrating if you do not develop a lot of patience, much like a hunter or pool player does. Rushing and firing away trades without knowing what you're doing leads to trading losses. *It's ok to buy a low-rated stock (eg all "hold" ratings) if it's going up nicely on higher-than-average volume. It's bad to buy a high-rated stock (eg 7 "strong buy" ratings) if it's in a downtrend on average volume.* ([For analysts ratings click here; change the ticker in the location bar of your browser vs in the page itself \(faster\)](#))

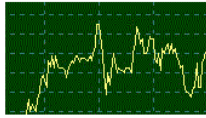
*If you are saying to yourself "I don't know, it might go up, let me buy some", you are making a trading mistake.* Only when you can say "this is a high-percentage play, I'd be surprised if it doesn't go up from here" should you put thousands of dollars of money into the stock. On the other hand, you can't wait for "all the planets to line up" or you'll be in the trade too late and buy the obvious, at which point sellers will come in and you'll lose as well. It takes balance and speed.

**Examples:**

**WHICH OF THESE TWO STOCKS is better to buy as a daytrade this very moment, based on the buy/sell pattern alone? (we'll look at RSI/MA/Stochs/Volume in other lessons)**

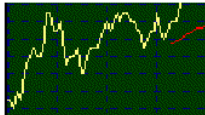
**STOCK**

**#1:**



Number of brokers recommending as:		Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)	
Strong Buy	9	This Week	1.44
Moderate Buy	7	Last Week	1.50
Hold	0	Change	0.06
Moderate Sell	0		
Strong Sell	0		

### STOCK #2:



Number of brokers recommending as:		Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)	
Strong Buy	1	This Week	2.30
Moderate Buy	4	Last Week	2.41
Hold	5	Change	0.11
Moderate Sell	0		
Strong Sell	0		

(scroll to bottom of page for answer)

### Answer:

**For a DAYTRADE, Buy stock #2: Higher highs and higher lows (an ascending triangle, the stock went on up an additional 1 1/2 points from 25 to 27+ that day!). The analysts ratings are irrelevant to daytraders, except for an intraday upgrade/downgrade that could influence the momentum (or a gap play on the following day). This is difficult for most people to fully adopt into their daytrading.**

For an INVESTMENT, Buy stock #1: If you want to buy and hold for 6 months or 2 years or something, well first of all you're in the wrong site lol. Analysts ratings mean nothing to us except to the degree that they influence trading for new upgrades/downgrades, and perhaps overall trend direction. We care about momentum, not ratings.



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● **Main Points:**

- Most of us who daytrade for a living use both Level 2 and 1-minute tick charts that have a number of indicators we rely on. After awhile, these will become like "second nature" to you (much like the dashboard is while driving a car).
- You need to develop the skill to quickly respond to relevant technical indicators while avoiding too much complexity that detracts from your trading skill and speed.
- As you can see from my setup; I find that it's useful to have a level 2 window, a one-day interval chart and a 5-day chart all together for each of the 9 stocks I am watching at any given point in time.
- In this and other pages we will give you many handy tips for daytrading technical analysis not found in the books, but essential for success. The books generally aren't real-life or practical enough; we want to provide specific technical patterns and indicators that work for daytrading today's stocks.
- You need to experiment to develop a setup that works well for you; many traders like to just watch 1 to 3 level 2 screens at a time. If it works, use it! Experimentation is the key.

click for full 4-screen  
snap:



### Basic Technical Analysis for Daytraders

- Note: I will not waste your time with kindergarten TA you can get in any book; we will instead give you practical methods and ideas. The stuff they don't tell you.
- It is useful to keep an eye on **2 simultaneous charts for every stock you trade**: The First is what I call a "closeup" intraday chart, with a short time interval (1 to 5 minutes). The Second is a 5-day or 10-day chart to help you identify current support and resistance levels, and to see "where the stock is coming from" (the time interval for a multiday chart should be 13 minutes).
- Trading with only today's intraday chart is not enough, you need to



see at least the previous days' open/high/low/close and volume to understand buying/selling behavior for the current day. Especially useful for playing opening gaps.

**The first TA decision you must make is:**

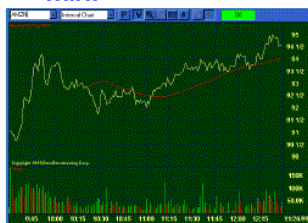
**How often should you set your intraday charts to sample data for?**

Some traders like 3min/13min setups, others use 5/15 etc.. I like 1/13 myself.

- For those of us who scalp and trade in intervals of a few minutes to an hour or two, set your intraday chart data interval to a one minute close-line chart.
- For those who trade longer time intervals (many hours, overnight holds, swing traders), you may want to use 3-minute charts instead to filter out the minute-by-minute 'noise'.

For this intraday chart, should you use a close-line, bar or candlestick chart? I use a close-line 1 minute intraday chart and a 5-day candlestick or bar char. Here's what three intraday AMZN charts would look like with each of these displays:

**Close line 1-min:**



**Candle 1-min:**



**Bar 1-min:**



**Which is easiest to read?** I like the close-line myself, although you don't see the minute-by-minute range. With level 2, you don't need to see that on the chart, since you can "read the tape" and you know what action is going on at each price level. The close-line chart lets me see key support/resistance and trend data.

**So, have you set up your 1-minute intraday charts for your 3-5 core daytrading stocks yet?** Remember, you should have two charts for each stock. If you don't have a data feed, at least use a [bigcharts.com](http://bigcharts.com) 5- or 10-day chart in addition to the intraday 1-minute chart you use to trade from.

If (and only if) the stock is giving me uncertain signals and I can't see what's going to happen from the level 2 patterns, then I will use my "microscope" intraday TA momentum chart with a few more bells and whistles.

Most of us who are daytraders don't use bollinger bands and other TA that's designed for multi-week or multi-month investing. We are daytraders. We may use stochastics and oscillators, volume breakouts and tape patterns. That's all we need. Here's an example:

**1-minute Close Line Chart with:**

- 50 MA (red line main graph)
- Volume (of course)
- RSI (12)
- Slow stochastic (18)

I will not bore you with the details of "how to set up your indicators" other than these examples I'm providing; there are plenty of resources out there to help you with TA.

[See next page](#)

How to Use the Indicators: Typically, I rely on support and resistance levels plus patterns I've memorized to help me enter and exit trades. We'll look at patterns on the next page. Stochs are a daytrader's favorite, like MACD lines they cross, giving buy/sell signals. RSI for oversold/overbought conditions. Use with caution, market direction and tape flow in time and sales are most important.



Here's an example of a DCLK 5-day chart (minus one day for Thanksgiving; I'll change the chart next week). Notice that I like to use candlestick 13-minute charts for 5-day or 10-day charts. On the chart itself I like to include a 50MA (experiment, anywhere from 28- to 50- MA is decent) as a trend/support line. Notice that the red/green bars show buyers/sellers during each 13-minute interval. This is used for support/resistance spotting. Another nice feature from [eSignal](#) charts.



**Intraday Support and Resistance Levels**

- Hint: start with a 5-day chart to identify the past 5 trading days' support and resistance, also paying attention to volume and spotting larger patterns (cup and saucer, triangles, pennants, flags, breakouts from a trading range etc). Volume breakouts are great to trade, as are bottom bounces off support levels. Here's an example of a multiday "double bottom" XRX chart showing support at 28ish:

**5-day XRX chart thru 11/26 showing**

### support at 28:



I drew the yellow line at 28, a support level for XRX. How to trade it? Buy it at around 28 to 28 1/4, using 27 15/16 as a stop.

If we're right, XRX should run up for a half point or more. If we're wrong, we're out with a very small loss.

It works. (having said that, now watch XRX plummet to 19 on Mon lol)

### 3-day COMS chart showing double top resistance:



Here's a multiday "double top", showing temporary resistance. Do not buy this stock until it breaks through the resistance level on decent volume.

Double and triple bottoms & tops make for easy plays; you can "trade the channel", surfing long and short between the boundaries, using close stops for protection. The double top indicates an "overbought" condition, where sellers will gain momentum.

### Overbought, in a Trading Range, or Oversold?

Remember to always try and play overbought or oversold conditions (with volume and market directions as confirming indicators). The only time to play stock that's in a range is if you're playing market maker and scalping teenies (another very valid and common way to daytrade).

High-percentage trades are off the tops and bottoms. Look for double-digit

swings (eg down 11% on the day with no news) for high-potential trading opportunities. Here's a couple of examples:

**Can you ID support/resistance for this Disney 6-month chart?**

**Can you say "oversold" for this 5-day Disney chart? Predictable top, time to short it:**



Here's an example of an oversold HRL chart. Given all the good news that just came out the same day (and CNBC mention), it was an obvious buy at the close of the day:

Of course, I posted this in the "stock picks" page and bought at the bottom, selling on the opening gap up.



Since I don't normally play this stock, I just played a very conservative 200 shares. Still, \$250 on 200 shares of an overnight hold is an ok profit.

11/23/1999 15:51:58	Bought	200 HRL	40 1/2	\$-8,109.99
11/24/1999 09:47:45	Sold	200 HRL	41 7/8	\$8,364.73

**What fund managers look for: why you should care as a daytrader.** These guys have pre-entered buy and sell programs

based on the \$PREM, indexes and most importantly the **50- 100- and 200-day MA** (moving average) lines on stocks they play.

These give you ideal support and resistance levels...look them up on 6-month charts, then narrow in to 5-day and intraday charts, watching for blocks of at least 10K shares going off in time and sales for buy and sell signals.

**QCOM 6-month chart:** a thing of beauty.

Notice the stock never loses its 50/100/200 MA lines.

Other charts do. lol

Look for when a stock price tests, retests and bounces off any of these key three lines for institutional buy/sell signals.

Scope down to a 5- or 10-day chart to see the latest action (esp volume), then put on the watchlist for intraday trading. It's easy.



#### **Intro to TA for Momentum Trading**

- Momentum trading includes "jumping on whatever's hot", such as IPO's, morning gappers (either gainers or losers), and news plays. We'll look at reading stochs and advanced momentum oscillators in a later module.
- TA is primarily concerned with both momentum oscillators such as stochastics, which may be helpful, as well as the slope of the close line: the steeper the slope the faster the retracement will be. [See our next page for more examples and "how to's"...](#)
- **Here was what is in my opinion the "momentum play of the year"**. I've never seen anything like it. If I'd a just bought 1K shares at 28-30 I coulda woulda shoulda make 20 grand in under an hour. Of course, I didn't jump in (I rarely play stocks I don't know, or IPOs). **Triple Doh!** And, the chart was easy to play, gained 30 points over a slow steady hour of trading.

Gee Marge we shoulda bought some of this at the open. Doh!



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● **Main Points:**

- **Successful daytrading depends on your ability to correctly interpret high-probability chart patterns that will provide you with buy and sell signals.**
- Learning technical analysis of stock charts is a critical skill that takes time and many hours of observation and practice to master. **It is not easy.**
- **Once you take the time to learn what to look for and how to trade it, you will gain confidence in your trades and very seldom be 'surprised' by price momentum.** You will be able to better anticipate where to enter stops, how to identify support and resistance, and manage your daily trading activity with more certainty and profit.
- Some daytraders use only intraday charts, others use only level 2. **Our belief is that mastering both sets of skills will give you a competitive edge against other traders whose capital you are trying to take.** Like windage and elevation scope controls for a high-powered rifle, you want to use the tools to be able to consistently hit the bullseye for winning trades. It is very much a learned skill. Daytrading is a zero-sum game. Mastering 1-minute intraday chart TA is a very useful skill.
- **We will give you a synopsis of exactly what to look for with the most frequently-used daytrading chart patterns: Volume, Formations (triangles, channels, flags, breakouts etc.), Stochastics, MACD, MA and RSI.**
- For this and other modules, we will be developing quizzes and "test yourself"-type trading scenarios to help you further develop your daytrading skills.
- Entire books and chapters within trading books have been written about TA, so I will provide examples and recent charts, along with new information, to help further your understanding of technical chart analysis.

### **TA 101: How to Read Intraday Charts**

- **Overall market trend is king**, so always watch Nasdaq (\$COMPQ), spoos, (/SP9) and sector charts (eg \$GIN, \$SOX) as the highest priority.
- Second, look at the **5-day** historical chart for your stock to identify recent support and resistance levels.
- Third, look for the **specific 1-minute (or 3-minute) intraday chart patterns** we'll be discussing on this and our other two pages (intraday bull and bear charts) to identify high-percentage patterns

to trade.

- Finally, look at **volume accompanying the patterns** you see. Remember, traders "vote with volume", so a trend on low volume (eg during 11:30-1:30EST) is suspect.

### BASIC INTRADAY TREND PATTERNS: Up, Down and Sideways

Stocks tend to follow through on their patterns, until volume and price direction change. Here's a few examples:

**UPTRENDING CHARTS:** Notice higher highs and higher lows w/volume. No serious selling, price gets higher throughout the trading day.



**DOWNTRENDING CHARTS:** Notice lower highs and lower lows w/volume. No serious buying, price gets lower throughout the trading day. The CIEN chart below shows it sold off then settled into a consolidation, or **TRADING RANGE**, from 10:30 to 12:30. Notice 3 volume spikes, even though block buys of around 100K shares went off it wasn't enough to lift CIEN's price. A weak stock.

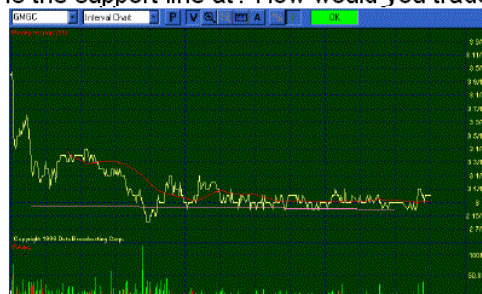
For the COMPQ (NASDAQ Composite) screen, notice the trend lines I drew in, showing the composite index wasn't getting much buying after the morning run up (12/8/99).





**IDENTIFYING SUPPORT AND RESISTANCE** is an important skill to learn, particularly when you're looking to improve your skill at buying bottoms and shorting tops (as well as the basic "buy into the trend" approach). Again, start with a 5- or 10-day look, then narrow your focus into the current day's trading momentum.

**SUPPORT:** In the CIEN chart above, support is at 47 1/2. In the GMGC chart below, where is the support line at? How would you trade it?



(answer: the support line is in pink, buy the stock if it breaks through the resistance level 1/4 point above the support line - the resistance level. Buy on a breakout above the resistance, or buy off the support level and sell it at the top of the trading range - this is a "channel play").

**DOUBLE BOTTOM INTRADAY (or 5-Day) SUPPORT BOUNCE:** In the XRX 5-day chart below, we see that support is at 28. You could either buy the next time it hits 28 (with a stop at 27 7/8), or wait until it breaks through its resistance line at 28 3/4.



**DOUBLE TOP INTRADAY (or 5-Day) RESISTANCE SHORT:** Can you identify the "double top" in the chart below? What's the play? Short it at the 2nd top, especially if it's reaching the 2nd top on *lower volume* (or during lunch hours). The price will probably fade. On the other hand, you'd want to go long if it broke through the resistance level on the 2nd or 3rd try.



## Advanced Intraday TA: What the Pros Use

On the next two pages, we will go over specific chart patterns to be on the lookout for: [Bullish Intraday Chart Patterns](#) and [Bearish Intraday Chart Patterns](#).

Below, we will learn **how to daytrade using advanced intraday technical indicators** that pro daytraders and mm's use to scalp trades and better time their entries and exits. The equivalent in Level 2 (which we'll cover in Module 2), involves shadowing the lead market maker, identifying t&s momentum patterns, and managing your bid/ask sizes.

*Please study this chart carefully for a few minutes:*

**50 MA**

**RSI: Relative Strength Index**

**13 Slow Stochastic**

**12,26,9 MACD**



There are dozens of technical indicators out there (Bollinger bands, envelope channels etc). **The ones on the chart above are the only ones that pros use. We will cover how to use them to daytrade effectively** (although I was a Ford Motor Co. statistician 8 years ago, I will not put you to sleep with the computational details; see a good TA book for that):

**50 MA** Use an **MA line** to help you see the average price trend throughout the day. **Think of it as a dynamic support/resistance line.** It plots the average price for you. Buy when the price dips to touch the 50MA and starts to rebound. In the DCLK example above, look at the price at 14:30 (2:30pm). A **buy signal** would be when the price touched the 50MA red line and started to rebound. Buy Limit DCLK 167 1/4. Sell anywhere over 170.

By the way, the only reason we use charts and level2 is for us to be able to **correctly respond to the buy and sell signals** they are giving us. It takes lots of practice (months and months) to develop a sense for reading the charts and level2. So be patient with yourself and start practicing.

### **RSI: Relative Strength Index**

RSI is somewhat useful, though not my favorite indicator. **RSI is a momentum indicator** which measures an equity's price relative to itself. RSI is less responsive to big swings in the price, so it filters out some of the "noise" in a stock's trading activity. **A buy signal is seen when the RSI line drops below 20** and starts to touch the bottom line - in the DCLK example above look at the 11:00 RSI curve - this was RSI's contribution to the day, told us to buy when RSI kissed the 20 line. A **sell signal** occurs when the RSI goes **above the 80 line**, although I've found many false signals in using RSI. Therefore, **use RSI only as a confirming indicator** for the other technical and momentum price signals you see. Also, **check for divergence between RSI and the price curve**; eg if you see a downward sloping price curve and upward sloping RSI curve the price may rebound up, if you see an upward sloping price curve, declining volume and a downward sloping RSI then the price is probably ready to pull in (drop). RSI is a 'just ok' measure.

### **13 Slow Stochastic**

The stochastic, along with volume, is the **daytrader's favorite** momentum oscillator. See this [Clearstation link](#) for a complete description. Stochs are used to identify "pivots", or turning points, in a stock's price momentum. Again, this needs to be weighed against overall market direction and volume for your stock. How to use the stochastic in daytrading? It rapidly oscillates up and down based on the stock's price momentum. **Think of it as a "red light/yellow light/green light" momentum flag for your trades.** If the two lines on the stoch have just reached the bottom and are heading up, the stock price will probably head up as well.

In the DCLK example above, look carefully at the stoch curves and DCLK price curve at 13:20 and 14:30. You'll see the stochs (red/white lines) bottom right before the DCLK price rises. Next to volume, stochs are my favorite indicator. Experiment with different settings, I find 13 is the best (the crowd uses 15, so I set mine in by 2 to gain a bit of an edge). It's a trustworthy tool, like a screwdriver. Learn how to use it. Practice with it.

#### 12,26,9 MACD

MACD ([also see this link](#)) is a slower, more gradual indicator that can be used as an overall trend indicator. I always like to **look for the two lines crossing and turning up off the bottom to indicate a good time to buy**. It's also an "ok" lagging indicator, you can see in the DCLK example it provided a confirmation of the 11:00 bottom to buy off of, nothing original however. I find MACD to be a reassurance and a confirming trend indicator. As we said, **a buy signal is generated when the two MACD lines cross and start turning up**. It's a fairly decent indicator, use in combination with the others.

Ok, that's it for the advanced indicators. They're not rocket science; the most difficult part for me was learning how to see them on autopilot, along with Level 2, to generate true buy and sell signals. Your first months will be full of seeing false signals, not knowing "for sure" what they're telling you (and by then it's too late, etc.).

Our advice? Be patient with yourself, get a bunch of historical intraday charts with these indicators and practice for yourself with my "3x5 card at the monitor" technique (it really works!). Pull up a chart, then cover the right half of it with a 3x5 card and slowly move the card from left to right, to simulate what the chart would look like in a real trading day.

Look at the indicators and 'papertrade' to see if you are reading the chart correctly. Also be sure to reference the composite and sector index charts while you do this, to simulate your real daytrading efforts. Good luck.

Now, on to "[Bullish Intraday Chart Patterns](#)" and "[Bearish Intraday Chart Patterns](#)"...



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Successful Online Daytrading Training Resources

## How to Daytrade Bullish Intraday Chart Patterns

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### ● Main Points:

- There are two primary 'bullish' stock buys to become familiar with: buying into an uptrend and buying on an anticipated 'bottom bounce'.
- Within those two categories there are several specific intraday chart patterns that you should gain familiarity with. These patterns show you how and when to enter trades based on what you see.
- Remember that from a "big-picture" perspective, you are looking for several signals to converge, telling you when you have the best chance of making a winning trade. This includes the overall market trend, the specific 3- and 13-minute trend of your stock, volume and time-of-day. Then, we look at the intraday trend and level 2 to enter specific profitable trades.
- Becoming a 'sniper' trader means you are very selective, like a hunter waiting for prey. 95% of your energy is spent figuring out when the time is right to buy your stock. Our automatic small and trailing stops make selling the easiest part (contrary to what you hear out there; it's the 'should i buy now?' that's agonizing; once you're in the trade you firmly stick with your trade rules no matter what.)
- I do not advocate highly active trading, particularly in your first year. Be content to make 1-2 trades per day, maybe up to 4 or 5. You can make a living at it. I average 80 round trips a month, or 4 buy/sells per trading day.
- Ok, let's look at some chart patterns you need to recognize:

### **Uptrending Chart Patterns for Daytrading: Breakouts, Triangles, Steady Channels**

- **BREAKOUTS:** When a chart has been in a steady "trading range" for a length of time (5 minutes to half an hour, or an hour or so during the lunch break) and breaks above the resistance line on volume. This happens after the tug-of-war between buyers and sellers shifts in favor of buyers, with sellers being finished.
- Note: Level 2 can help you spot these as well, when a given market maker who's been sitting on the inside ask cleaning up a client order is finally finished and steps off the

ask; the stock price will pop up when he goes away. He may flip to the bid as well, if he stays through 10k shares or so of buying he may be a net buyer at this point and the stock price will rise. We'll cover more level 2 in Module 2.

- See if you can spot the breakouts in these plays:

**Breakout Play #1:**

This was a buy as soon as it broke through its resistance at 42 on decent volume. It climbed another 3/4 of a point before a selling volume spike occurred.

This sell signal tells you it's time to take your profits and run. You had at least 15 minutes on both the entry and exit to make 5/8 point. Easy money.



**Breakout Play #2:**

This stock had a hard time breaking through 12 3/4 resistance. When it did, it ran up way too fast for most of us to get on board with.

The easy play? Wait for a retracement to the resistance level, buy it when you see it's consolidated above 12 3/4. Buy on the uptrend following the breakout/selloff. Be cautious and set your stop right underneath the support line, in this case I'd set it at 12 5/8.



**Breakout Play #3:**

Oftentimes the stock price will set an initial resistance (and total day's range) within the first hour. In this case, the fact that we had buyers push it up past the day's resistance line (a new hod=high-of-day) tells us more buying is likely ahead.

The volume surge at the bottom confirms this, so it's a buy at 51 3/4 or so, using trailing stops (or a stop set at right under the resistance line). Easy play.





**Uptrending TRIANGLES:** Look at the triangle that's drawn in white lines on this CPQ chart. Triangles are one of the easiest and most profitable plays to spot. The buyers keep raising the lowest price they'll pay for the stock, while the sellers keep the price at the same resistance level. Finally, the point of the triangle narrows and a big price movement occurs, either up or down.

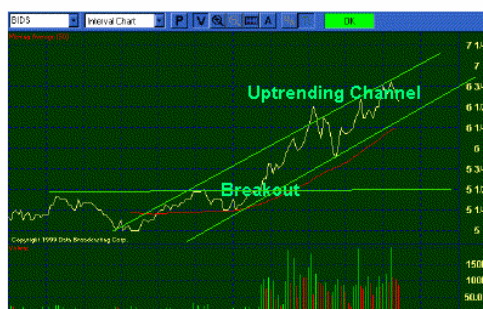
The buyers and sellers get closer and closer on the price they think is fair, followed by "a winner" - note that these can break to the downside as well, so: **Buy when you see the stock price break to the upside above the top (flat) resistance line by 1/8 point. Immediately set a stop 1/8 - 1/4 point under the resistance line for protection.**

**This is what CPQ went on to do that day:**



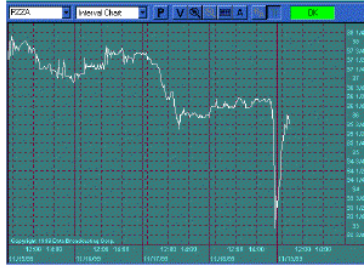
**STEADY CHANNELS:** predictable uptrending price movement that oscillates within a fixed range (eg 1/2 point). Buy off support in the channel and use trailing stops to lock in profit.

Hint: The **50MA** often provides an excellent uptrending 'support line' for stocks in an uptrend channel. See the red line in the chart to the right. >>



**Bottom Bounce Chart Patterns for Daytrading:**  
**Oversold Overnight Holds, 5%+ Intraday Drops, Strong RSI**

**Oversold Overnight Holds:** can be very profitable. Remember our oversold PZZA bounce (chart at right>>)? That's worth a quick 1 5/8 point in 20 minutes. These types of plays happen routinely in the market. Note they also hold the danger of a gap down on open.



Here's how to trade it...first, look at the 10-day chart to see **how often** your particular stock has gapped up on the open after end of day selling recently. Some stocks, you will observe, will either gap up or open flat during a timeframe of a week or two. Capitalize on these moves.

**Oversold Overnight Bounce Play Example: SBUX**

Look at this two-day chart of SBUX...it sold off from 25 1/2 to 23 3/4 on no news. It looked oversold, so I bought a conservative 500 shares for an overnight hold at 24 1/16. I sold premarket on ISLD at 24 7/16...it went higher, but I was satisfied with a quick 3/8 (\$167) profit overnight.



12/09/1999	15:58:29	Bought	500 SBUX	24 1/16	\$-12,041.24
12/10/1999	09:26:52	Sold	500 SBUX	24 7/16	\$12,208.35



**Intraday Channel Bottom Bounce Plays:** Continuing on w/SBUX that day, you can see it bounced off 24 1/8 3 times... a "triple bottom". That's a bullish pattern to watch for.

Buying off the bottom at 24 3/8 each time and selling up towards 25 resistance was also profitable. These are bottom plays because you're buying off what you hope will be the bottom of the price, usually at a resistance level.

As always, do not try to guess where the bottom is, let the market tell you, as evidenced by an uptick (higher highs, higher lows), with volume.

Look at this chart carefully. Note the volume at the bottom of each bounce. If you do not see this, you may not have the real bottom. Where should you set your stop? at 23 15/16 (right under whole number support).

**5% + Intraday Drops:** If a stock suddenly sells off (and there's no bad news), you can try to find the bottom and buy the "dead cat bounce". I like to see at least -5% selloff w/no bad news as a high-probability place to consider entering a trade. (as soon as buyers come back in, that is!).

**5% drop play:** spls 21 1/8...see how the price dropped; there was no 'reason' for it, it made a good buy off near-whole number support at 21 1/8...good for a quick 1/4-3/8 point scalp.

Don't try to guess or anticipate the bottom, ever. Let the market tell you when it's done selling, not your perception of how far down the stock price can go. Wait for a volume reversal to prove you right. Buying bottoms is always risky, but it is one of my favorite plays.

Think of buying bottoms in this way: the stock price is like a shock



absorber spring; it can only be depressed so much before buyers come in and it starts to spring back up again. Likewise, as it gets extended upwards, it will contract and sell off again.

In summary, the 5% intraday drop tells you to be on the lookout for these oversold stocks (preferably ones that you follow regularly) as potential buys.

**Strong RSI Bottomfishing:** Finally, consider buying stocks that drop less than others in their sector do during a market downtrend.

Say for example you're playing semiconductors (\$SOX; INTC AMAT KLAC XLNX ALTR) and you see the \$SOX and most of the semis tanking except for XLNX, which is holding up fairly well during the selling. What's the play? Have a Buy XLNX order ready for when the market and the \$SOX turns back up...XLNX should be one of the first ones to run.

We say it has strong relative strength in its sector; people would rather sell other stocks. Look at the RSI line too in comparison; if the other stocks are down near the 20 and XLNX for example is still 40-50 than we can feel confident that it should run strongly when the rest of the market starts to head back up.

As someone said, "Buy strong stocks. Sell weak stocks." Not the other way around.

## SUMMARY:

Recognizing and using the basic daytrading chart patterns on this page will help alert you to high-percentage trading opportunities. Get to know them, and papertrade these patterns using your 4-5 favorite stocks for at least 3 months. See how your predictions and the patterns match up. You'll get good at this in time.

Too bad the books don't give you these fine points you need to win. This is experience talking on the page; I hope it helps you become a more successful daytrader! **Alright, lets move on the the bearish patterns shall we? Click on...**



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**How to Daytrade Bearish Intraday Chart Patterns**

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● **Main Points:**

- **The main thing I want for you to learn in this lesson is how to recognize and avoid buying stocks that are about to go down. I want you to 'stay in the game' and preserve your capital. The odds are already against you, so let's even it up a bit while you learn.**
- **There are many more 'dangerous' or low-percentage chart patterns than there are high-percentage bullish patterns. When in doubt, stay out.**
- **Here's a tip that will help you mentally toughen up and get sharper in your daytrade quality and profits you are able to take from the market -- Before you buy any stock, or enter any trade, I want you to identify -**
- **Which of these three categories does the trade fall into?:**

**HIGH-PERCENTAGE  
DAYTRADE**

- Stock is rebounding from an extreme oversold condition w/volume; or
- It's heading up in a steady trading channel on good volume; or
- You got in early on a positive news release and the stock is running; or
- Technicals (stochs, MACD, RSI, level2) tell you it's going up
- CNBC mentions the stock price being oversold w/no good reason, or a new deal etc. in a favorable way; or

**"I DON'T KNOW"  
DAYTRADE**

- You are not certain which way the stock will go
- You are bored and want to trade something, anything
- The stock has been fluctuating in a trading channel on flat volume
- The Level 2 bid and ask columns look similar, and there is no clear pattern in time and sales to follow

**"LOW-PERCENTAGE"  
DAYTRADE**

- Cheap chatroom stocks (eg EFA to 2! its running!)
- See above
- Read it again
- It's lunchtime (11:30-1:30EST) and you like the stock's analysts ratings or the company's products/services
- Stock has run up over 20% in a spike upwards and you're chasing it
- Stock is gradually selling off and you think you found the bottom (famous last words)
- Stocks with wide spreads (1/4pt or bigger) and low volume (under 300K) Can you say

- You're scalping the stock off a support level that you are familiar with; also
- You're not buying it during the lunch 'deadzone' and
- The market is headed up

- "the mm's will eat you for lunch"?!  
 • Shorting hi-flyers that have strong volume  
 • Many many others to avoid

Obviously, you should avoid any but the high-percentage trade opportunities. Many new traders make trades "all over the map" instead of being selective.

To win at this, you must use a microscope and have the patience, strength, focus and determination to make solid trades. In time, you'll get a "it just feels right" trading sense based on all these factors that you now know to look for. "It gets easier in time; but it takes a lot of time before it gets easy."

Let's look at specific intraday chart patterns to be wary of: (Hint: as you look at these charts, put your hand/paper over the chart and move it slowly to the right, uncovering the chart, to simulate what happened over time during the trading day. See what "the first sign of trouble" was, based on the price and volume movement, along with the observations in text):

## Downtrending Chart Patterns To Watch Out For: Breakdowns, Triangles, Down Channels, 'Pop n Drop' Spikes

- **Making lower lows and lower highs** is a sign of weakness.
- Here YHOO fails to make a higher high (warning #1), next, it bounces off a support line for a while. As soon as it makes a lower low, you know the **sellers are stronger**. Not a time to buy this one.
- (Shorter's note: Selling the stock where it failed to make a higher high is the short play here at 222, use the previous peak as your stop). We'll cover short plays in a later module; I



advise traders against shorting their first 6 months or so of trading).

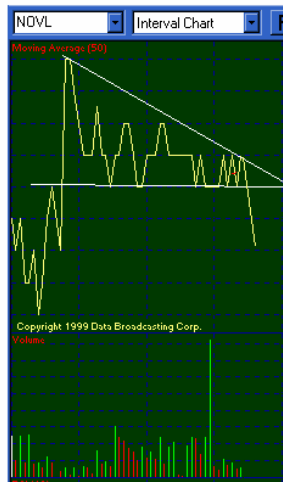
**DESCENDING TRIANGLE:**

The opposite of the bullish ascending triangle, what does this one tell you?

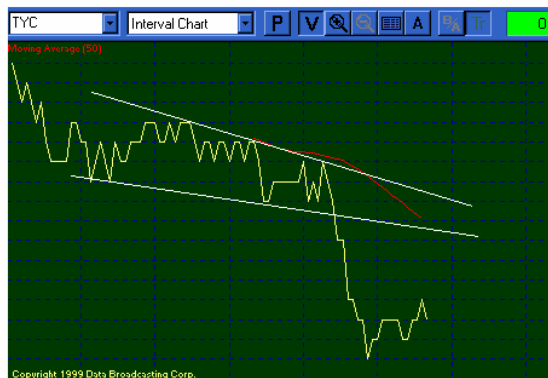
Right, there's not enough buying interest to keep the price headed up. So, we can expect the sellers to win the battle for now as the price drops.

Notice the volume spike followed by no uptrend? That's also a warning flag; it means there's more stock to sell than there is to buy, for now.

Where's a buy signal? Wait until the stock hits a low and rebounds w/higher highs/higher lows, or, wait til it breaks thru the previous top on strength.



- **DOWNTRENDING CHANNEL:** Here TYC is trending in a downwards channel, giving you plenty of warning before the price breaks to the downside.



- **Chatroom POP n DROP Spikes:** Avoiding

"JUST SAY NO" to Chatroom Hype Stocks Like These:

- **Chatroom POP n DROP Spikes:** Avoiding chatroom pump n dump specials is important. In their desire to have someone show them how to trade, many new traders will occasionally log onto the various free Mirc chatrooms to see "what's hot".

"JUST SAY NO" to Chatroom Hype Stocks Like These:



- Sometimes these calls are ok; many other times they are **junk**. I like to trade hi-percentage trades, of which most chatroom plays are not. They frontrun a stock, hype it and sell to the newbies while they're hyping it.
- It's dangerous, distracting communication that keeps you from learning how to trade for yourself. Talk to any pro daytrader who's made it; we'll tell you we do it the hard way, by learning daytrading mechanics.
- Anyways, avoid pump n dump chatroom specials. 'nuf said.



#### Other Times Not to Buy or Sell Stock:

- When you're tired - you need to be at your most alert to daytrade.
- When you've just had an argument or conflict with someone.
- When you've had alcohol to drink (save that for after hours!)
- When your computer and/or broker is "iffy". It's tough enough without that headache.
- Trading scared or in a losing streak: scale back and paper/smallshare trade til you get it back.
- When you're bored and you just feel like trading for trading's sake. Play a videogame instead.

#### Thoughts to trade by:

- Take a break from trading now and then; don't worry about "missing a big run"; they occur daily and the market will be here long after you and I are gone. It'll be there.
- Seize the moment and go for a walk or a cup of coffee somewhere, get a dessert, exercise, look out the window, go golfing etc.
- Your attitude is important: expect to win, but only after you learn, concentrate and practice.



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Selling Opening Gaps Up and Buying Opening Gaps down:

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● **Main Points:**

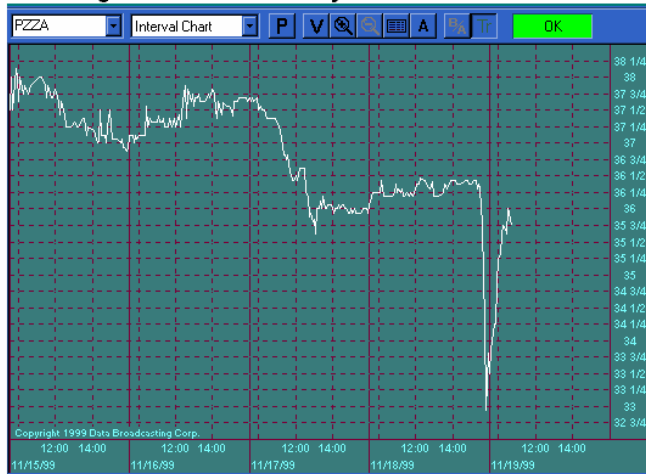
One of the easiest daytrades you can make is to *buy stocks that have gapped down by at least 5% or to short stocks that have gapped up over 5% on the open.*

Why does this happen? In overreaction to news or earnings reports.

**Guidelines:**

- This is a trade executed at the **open** of the market (around 9:35)
- You will probably **exit the trade by 10-10:30**, depending on momentum
- Be cautious on these plays by setting **stop losses** as always within 1/4-1/2 point max. Especially with earnings plays, the gap down may continue. The bigger the gap, the more likely some retracement will occur. If a stock gaps over 30% then keep an eye on it. These happen daily.

**Gap Down Example:** PZZA gapped down to 33 on 11/19 before rebounding to over 36. The play? We bought at 34 1/8, sold at 35 7/8 for a 1 3/4 point gain in 20 minutes. This was brought to our attention by CNBC.



**Gap Up Example:** SBUX gapped up to 30 3/4 premarket before tanking to around 28 1/2. It would have been a "short on open" at 30 3/4. We caught the bounce play for

a [fractional gain](#) later, but the big play was the short on open.



Use your quote service to flag volume breakouts and "day's gainers/losers" to identify gap plays. These can also be played later in the morning, so you can check [bigcharts](#) etc. for the day's losers/winners.



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**Tomahawk scalping techniques: taking small consistent daily profits**

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● **Main Points:**

- **The books tell you to "go for base hits not home runs". While that's true, they don't give you the trade mechanics of how to do it. That's what this page will help with.**
- **Using a combination of scalps and trailing stops will help you take consistent profits out of the street.**
- **Many new daytraders make the mistake of keeping large stops, becoming confused with investing vs daytrading, and end up with 1/2-point to 1-point (or more) losses on their trades. Those of us who trade for a living have a very intense concentration while in our positions and try to protect every 1/16th. Beginners say "hey what the heck it's only a 1/4 point and its a good stock, it'll go up" (famous last words). I like to trade against guys like that.**
- **Realize traders, that if you take just 4-5 quarter points a day on 1K share trades, that gives you an annual income of almost \$300K. Not too bad.**
- **Just a net positive 2 quarter point trades 1K shares gives you \$120K/yr.**

**Daytraders' scalping guidelines:**

- You should to trade 500-1K shares for 1/16ths, 1/8ths or 1/4 points. If the trade is going your way, stay in it for the 1/2 point or more. *Usually*, though, it's in and out in under 30 minutes.
  - Only scalp trade stocks with solid volume, over 300K at the time you enter the trade. You want to be able to sell quickly.
  - Your time in and time out on scalp trades can be anywhere from 15 seconds for 1-2 spreads to "as long as the stock is going your way".
  - You can scalp short as well as long.
- The easiest scalp is when you see a stock oscillating between two prices (eg stuck at 24 1/8 x 24 1/4 for 15 minutes or longer)
  - As always, make sure to use a Buy Limit order at the Bid and Sell at the Offer to avoid paying up 2 spreads.
  - Scalping is a high-frequency repeated type of trading that is not glamorous. You don't buy at 35 7/8, watch it skyrocket to 39 and then sell. That's the rarest of trades. Money is made grinding out teenies like a market maker does.
  - Scalping is the easiest and fastest way to take profits off the street. You make the market for the stock and pocket the spread. Market makers don't like this :o

I find that scalping stocks within a half-point trading range for a stock priced in the teens to mid-twenties on volume of 1M-3M is an easy way to make money on the NASDAQ market.

The toughest part is to be happy flipping several spreads over and over and over ...but when you see you're up \$650 or more each day that you do that, it's rewarding.

The second toughest part is getting comfortable with buying on the bid (you have to wait for the stock to come in and take out your bid) and selling on the offer. Of course, if the stock is selling then you want to pull your offer and hit the bid, though you'll give up one spread this way.

**Time of day to scalp:** avoid the highest- and lowest-volatility times; scalping is best done from around 10:30am to 11:30am and from 2:30pm to 3:30ish. First half hour of the market and last half hour tend to be volatile - great for daytrading momentum, but not for scalping plays.

**Other Notes on Scalping:** Making the market in a stock by 'playing market maker' takes a lot of patience. It should be considered an intermediate/advanced technique, not for someone who has less than 6 months experience in front of a level 2 screen. You must have Level 2 to scalp stocks. Scalping also requires a fast trade pace, our scalps are usually from 20 seconds to 3 minutes round trip using a daytrading direct-access broker.



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**How to read relative strength and major sector stock patterns**

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● **Main Points:**

- **Stocks in each major sector (telecom, internet, chips, boxmakers, retailers etc) tend to follow the "sector leaders".**

*Examples:*



- **INTERNET SECTOR LEADERS (\$GIN) :** AOL YHOO AMZN DCLK
- **CHIP SECTOR LEADERS (\$SOX):** INTC AMAT XLNX
- **COMPUTER SECTOR LEADERS:** GTW DELL IBM SUNW AAPL
- **TELECOM SECTOR LEADERS:** T WCOM FON GTE

*Note that sector index symbols vary by quote source (eg esignal, bigcharts and quotetracker may be different, etc.).*

- **Learning how to identify intraday divergence between a particular stock in a sector and the sector leaders can prove very profitable.** If the whole sector is down, say internets, but one stock hasn't sold off with the rest of the sector, it's a solid candidate for being the first one to bounce up strong when the sector & market turn up (either intraday or across 2 or more days). We say its **intraday relative strength** is higher. Conversely, stocks that are not being bought as much as the sector leaders are in an uptrend (the "generals" of the army) will tend to sell off the fastest as soon as the market and sector head down.

**Examples:**

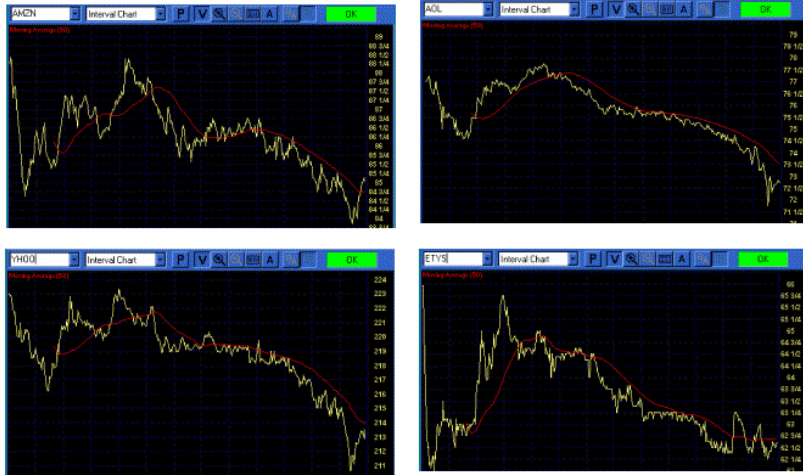
**This is a picture of the \$GIN (Internet Index) for Tuesday, November 30th:**



Except for our "10:30 bounce" (remember I told you about that pattern

earlier), the nets pretty much sold off all day. Notice please: \$GIN made a lower low towards the end of the session. The previous low was at 580, the new low at 573.

**Pop Quiz:** Which of the following net stocks have the 1) strongest and 2) weakest relative strength to the index? And, what price action would you be watching for during the remainder of the week in these specific stocks?



**Hint:** Remember we're looking at price action relative to the sector index, relative to the "generals" of the sector, as well as the buying strength and selling weakness.

What do these four charts, taken with the sector chart above, tell you you should keep an eye on to buy during the next trading day? Who's strong? Who's weak?

(Answers at bottom of page)

**Answers:**

**Weakest charts are AOL and YHOO. (also made new lows on the day at the end of the day, lots of selling).**



**Strongest charts are ETYS, then AMZN. Notice that ETYS did not make a lower bottom, and AMZN only weakened slightly in comparison to the \$GIN and other 'net charts.**

The trading play? Watch ETYS and AMZN for pre-market gap on the next trading day, and buy **if** the buying volume and higher highs/higher lows are being made on the tick chart. We could expect more selling before buyers come back, so wait to see volume buying and blocks going off in time & sales before entering a trade.

It's easy!

Remember, you just need to 'follow the buyers' and don't go against the sellers, for long plays. Common sense.

Notice please also that ETYS has the strongest run-up in the morning, meaning a lot of buyers were there for it. Another bullish signal for ETYS making a run again within the next few trading days.

Also, know your stocks' trading behavior, e.g., YHOO tends to gap up after being oversold on a close. So, I would have covered a YHOO short at the end of the day.

Traders, *do you understand why there's a small 'hook upwards' at the end of the day for all four stocks? It's caused by mm's covering their shorts, which drives price up. That's another play, the "last-30-minute-ride-the-short-covers-up-on-a-down-day" action.*

*(note: we will cover volume and time-of-day patterns in another page)*



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**Developing trading discipline: using stops consistently for "insurance"**

Back to  
MODULE 1

● **Main Points:**

**Enter a stop market sell order *immediately* after buying stock (and getting confirmation from your online broker) so that you know your "downside" as soon as you enter the trade.**

It's up to you to decide how close your stops should be. West & Friedfertig say your maximum should be 3/8 of a point in their [daytrading book](#). I use even closer stops, particularly when trading lots (1K shares), usually no more than a few spreads down.

Don't EVEN THINK about using so-called "mental stops" for several reasons:

***TECHNICAL PROBLEMS: Broker and Internet Connection slowdowns:***

FIRST: You may easily run into the problem of a downed or slow ISP internet connection to your broker. You do Not want to frantically try and close (sell) a position when your ISP is dead and you see the stock plummeting 1/2 point or more. Not fun, gang.

SECOND: Your Broker may be experiencing delays and problems in receiving a sell order if you depend on fast executions. Even pro daytrading brokers slow down sometimes and you do not want to be on the wrong side of a trade when it happens.

THIRD: Your pc may have a problem; even though I have a P2350 128megs memory etc. the ram can run out and freeze up your computer. You may accidentally hit a wrong key, have a power outage, spill coffee, have a nagging wife (lol); any of a hundred distractions may keep you from selling manually. Use automatic stops instead.

***MENTAL PROBLEMS: You hope it's going to go up after you buy it:***

Hope, fear and greed - welcome to the daytrading casino! Anything you can do to make your trading activities more automatic, using solid trading techniques, will help you become profitable. Entering a stop market sell order after buying stock will help you with this.

## How to Use "Trailing Stops" To Lock in Profit

### Examples:

Ok, so you've just bought 500 shares of SPLS using a Limit Buy SPLS 17 3/8 order.

You've clicked "Daily Activity" until you see the confirmation (in bold) that stock is "Bought":

11/08/1999	15:26:03	15:26:05	Buy 100 SPLS	17 <sup>5</sup> / <sub>16</sub>	Bought *	\$-1,731.25
11/08/1999	15:41:26	15:41:28	Buy 400 SPLS	17 <sup>3</sup> / <sub>8</sub>	Bought	\$-6,959.99
11/08/1999	15:45:25		Sell 500 SPLS	17 <sup>1</sup> / <sub>4</sub>	Cancelled	
11/08/1999	15:46:16		Sell 500 SPLS	17 <sup>3</sup> / <sub>8</sub>	Cancelled	
11/08/1999	15:48:34		Sell 500 SPLS	17 <sup>7</sup> / <sub>16</sub>	Cancelled	
11/08/1999	15:50:01		Sell 500 SPLS	17 <sup>1</sup> / <sub>2</sub>	Closed	
11/08/1999	15:50:32		Sell 500 SPLS	17 <sup>9</sup> / <sub>16</sub>	Cancelled	
11/08/1999	15:51:33	15:52:50	Sell 430 SPLS	17 <sup>5</sup> / <sub>8</sub>	Sold §	\$7,580.17
11/08/1999	15:51:33	15:51:34	Sell 70 SPLS	17 <sup>11</sup> / <sub>16</sub>	Sold *	\$1,238.08

The very next thing you do is enter a Sell Stop Market order at, say 1/8th point under where you bought (in this case Sell SPLS Stop Market at 17 1/4). (Datek was slow this am, took 4 mins to confirm order).

Now, I nailed it correctly and more buyers came in. The stock moved up another 2 spreads. So, I Cancelled my original Sell Stop Market 17 1/4 order, clicked "Daily Activity" til the confirmation came through, then entered a Sell Stop Market order at 17 3/8. Congratulations - you've "cleared the spread" and can now sell stock for what you bought it at. Well, that's ok but I'm here to make money, so...

Repeat the process: cancel your original Sell Stop Market orders as the price gets bid up and enter one spread higher each time. You can see I used "trailing stops" very close to the current market - I want to lock in every penny of profit I can.

Finally, sellers start to come in at 17 5/8, and my stop is taken out. I am up 1/4 point on 500 shares for a profit of \$125 in 15 minutes. Continue doing this throughout the trading day and make a good living.

If I was wrong, I'd be stopped out at -1/8 point, or just \$60 (+\$20commis) or -\$80 on the trade.

Does that make sense? It's a tight "scalping" play, and shows just one of many ways to daytrade.



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Successful Online Daytrading Training Resources

Nudging more profit out of the trade: when to shake out vs. staying in the trade

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MODULE 1

● Main Points:

- As you know, I advocate keeping small stops of no more than 2-3 spreads under where you originally bought the stock for all daytrades.
- There are, however, many different trading styles and stocks that can be played; so I will give some tips and guidelines here for those who use somewhat larger stops and may be swing/position players.
- These tips are also applicable to the higher-priced and more volatile of the internet and hi-tech stocks that I trade: DCLK AMZN YHOO EBAY BEAS JDSU QCOM etc., as this particular group of stocks often need to be played with larger (say 1-point) stops, due to the large spreads, sometimes as big as 1/2 point.

The daily challenge in trading highly volatile internet-type stocks is, "do I stop out with a small profit/loss, or should I take on more risk for a bigger reward (or loss)?"

Examples:

Here is an example of the 1-minute eSignal tick chart setup I use. Close-line, 50MA, RSI 12, Slow stochs 13, MACD 12,26,9.

*DCLK on 11/23. The play?* It was in somewhat of a trading range all morning (155-164); spotting the correct long play seemed difficult.

So, I waited til I saw higher highs and higher lows (roughly 2pm, 14:00), to enter a small shares trade.

I had spotted that 164 was the prev. resistance (now





support), so I bought 200 at 164 1/4 at 14:00 (2pm). Stop set at 163 3/4 (1/4 point under support level).

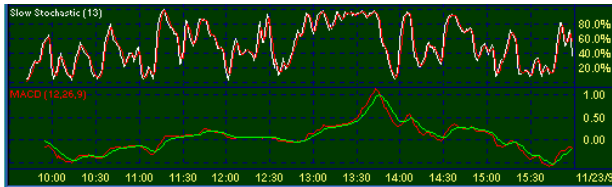
I could've shaken out after the initial peak before 2:30, but decided to stay in, with the stop at 164. I sold out right under 170 (decade number whole resistance) for a nice profit of \$1125 at 3pm. I could've held for more, but DCLK seemed overbought...it went up a bit more, that's ok, I'm out with profit. This is an example of an internet play that I used a somewhat larger stop based on support/resistance levels.



AMZN on 11/23: The play? I was busy watching DCLK so I didn't play AMZN, though it had a nice run as well.

#### *The buy signal?*

Volume breakout on higher high at 1pm (13:00). I would have stayed in the trade until it began making lower lows on the pullback (around 83ish), even though it did continue up the safe exit would have been using the technical indicator of lower low and lower



high as soon as it lost 83.

Notice that volume started to decrease around the pullback at 83 right before 14:00 (2pm) as well, another bearish indicator. It still ran up a bit before fading, as 85 was the real top.

**Mini-Activity:** Stay or shake out? See if you can identify where you would stay vs. sell. Hold your right hand up over the chart and move it slowly from left to right (or use an index card) to simulate the actual trading day. What technical indicators (volume etc.) would you use?

#### Tips for Daytrading Net Stocks Through the Shakes and Wiggles:

- The overall market is king of course, so always check the \$COMPQ and especially the \$GIN to help you manage entries and exits. Where is it headed? When will buyers return? When will they sell?
- Use the 3-stop guideline for net stocks as well, this time in combination with intraday support and resistance levels and volume and \$GIN direction.
- Be more sensitive to when institutional "buy programs" and "sell programs" kick in for net stocks. Follow the \$prem and \$trinq etc. as well as the \$GIN for additional timing tips.
- Use stochastics and MACD if it helps. I rely on these, with volume, RSI and an MA curve for good measure, to give me an overall "feel" for what's going on with this stock. Level 2 is alright, but not as useful for net stocks. I find level 2 gives false signals since there's so many daytraders/chippies (archips, players on ecn's like ARCA/INCA/ISLD) moving the stock price.
- Shakes and wiggles: I always like to use small stops and re-enter the position, perhaps as many as 4 times, before capturing the true move. Playing net stocks is exciting, not recommended for players with less than 6 months full-time trading experience. Start with the 'baby nets' like MSPG CNET LCOS before playing with the pros on AMZN YHOO DCLK CMGI etc.



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**What the market makers and pros dont want you to know**

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MODULE 1

● **Main Points:**

- There are a few things that professional traders and market makers do differently from the general daytrading public.
- Capitalizing on these tactics and protecting yourself, moving quickly and with more concentration, will help you to profit consistently in the market.
- You should not try to make a consistent living trading Nasdaq stocks without investing in level2 equipment and quotes.

**Examples:**

**What the Daytrading Pro's Don't Want You To Know**

**How You Can Make the Market & Frontrun**

Professionals do not make their living buying stock at 30 1/2 and selling at 33 for a 3-point gain.

**We make much of our living off the less dramatic but more consistent order flow derived from buying on the bid and selling at the ask many times throughout the trading day ; this works in flat and choppy markets.**

NOVL	-	17 7/16	b	17 7/16	a	17 1/2	21 x 30	2.02M	12:14
NOVL	Bid	17 7/16	21	INCA	17 1/2	30	12:14	17 7/16	2,000
ISLD	17 7/16	10	ISLD	17 1/2	17	12:14	17 1/2	350	
BRUT	17 7/16	10	BTRD	17 1/2	10	12:14	17 7/16	100	
BTRD	17 7/16	10	MASH	17 1/2	1	12:14	17 1/2	200	
SSCO	17 7/16	10	BKNC	17 9/16	1	12:14	17 1/2	500	
MALCO	17 7/16	10	LEHM	17 9/16	1	12:14	17 7/16	500	
PBCO	17 7/16	10	MALCO	17 5/8	10	12:14	17 7/16	500	
BEST	17 7/16	10	SHWD	17 5/8	5	12:14	17 7/16	500	
WEDD	17 7/16	1	HITE	17 5/8	1	12:14	17 7/16	500	
AGED	17 7/16	1	SWST	17 5/8	1	12:14	17 7/16	500	
WSTI	17 3/8	25	FCAP	17 5/8	1	12:14	17 1/2	1,000	
DNNY	17 3/8	20	JPM5	17 5/8	1	12:14	17 1/2	1,000	
REDI	17 3/8	15	SSSH	17 1/4	10	12:14	17 1/2	2,000	
INCA	17 3/8	15							

[Farrell's book](#) has some ok insight into doing this for listed stocks; but it's not a very good book imo.

If I can join the ISLD bid for 1K shares NOVL at 17 7/16 and then offer it out on the ask at 17 5/8 I've just taken \$187 profit off the street. I do this 20 times in a day and I've made \$3600/day income. Not bad. If I really nailed the bottom (rare) and use trailing stops I'll take even more off the street.

If I really want the stock I may split the market and offer to buy 1K shares at 17 15/32. This is my "plan b". Unless the stock

is in a dramatic upswing with no sellers in sight, I almost never - REPEAT NEVER PAY THE ASK. For 1K shares I'm down \$62 + commis. already if I do that. I can't make a living paying up 2 spreads. Neither can you.

### Concealing Patterns for Large Orders

- Many times a market maker like MSCO will get an institutional buy order for, say 200K shares of a stock. He doesn't want you to know about it, or else you'd buy too, and the price would go up. He'd look bad to his client.
- What do you do? Look for whether the mm stays on the bid consistently, the size of blocks that are being traded, the overall volume of the stock at that minute, and where his "trade box" is at. (trade box = the spread between where he buys vs sells the stock, eg MLCO above is at 17 7/16 x 5/8).
- If he returns to the inside bid more often in size (10) than the ask, he is probably a buyer. But, he will frequently camouflage his intentions using ISLD/INCA/other ECNs (See next point).

### Detecting mm's on INCA/ISLD

- Market makers (and us too, for that matter) like SBSH can route their orders several different ways: INCA/ISLD/Selectnet/etc.
- So, you may see SBSH offering to sell 3 spreads away from the market, but he's really selling a boatload via ISLD on the inside ask.
- **How we detect this is to see how many times the order is refreshed.** If you see ISLD 24 1/4 ask 10 size and yet time and sales shows over 40K being sold at that price, for example, you know there's probably one or more market makers routing their orders on ISLD. Their "public

MMID	Bid	Ask	Size
MSCO	24	10	
WONT	24	1	
WLECO	23 15/16	10	
WBLR	23 15/16	1	
GSOC	23 7/8	10	
GHWC	23 7/8	1	
LEHM	23 13/16	1	
BESH	23 3/4	10	
SBSH	23 3/4	10	
DLJP	23 3/4	10	
PIPP	23 3/4	1	
FBCC	23 3/4	1	
BWCO	23 3/4	1	

- **This is why "tape-reading" is such a vital skill you must master.** Homework assignment: watch the tape and 1-minute chart for one of your stocks that has over 2M average daily volume. See if you can detect tape support and resistance levels, along with the "pivot points",

face" is what they show on level 2, the "true action" happens when orders are routed via different ECNs to the market. Know what to look for.

where stock is changing hands between the market (eg at 24 1/32 for the I2 box above).

### Shorting with the ax

- **If you want to daytrade for a living**, it will be much easier if you learn how to short as well as go long.
- More money can be made shorting than going long; however I'd recommend getting at least 6 months experience daytrading the long side first.
- You have to be able to play both sides of the market to succeed at daytrading.
- You should have no preconceptions about what your stock is going to do over the next hour; you are a speedboat darting in and out of positions in response to the larger trend: up, down or sideways.

Shorting with the ax: first of all figure out how to [identify the ax](#). [This link](#) will give you some likely candidates for your particular stock; just look at who in the top 3 is one of the major players (MSCO MLCO SBSH GSCO). Ignore nite, pwjc, mash etc.

Next, make sure the market direction is in a selling mode. This can be at the open (shorting an open gap up), or a safer short at lunchtime, on a stock that's making lower highs and lower lows. The open gap short will probably be covered within 15 to 45 minutes, while a short during lunchtime will probably be covered by 2pm.

Find out which ax stays at the inside ask and keeps refreshing his bid. He may back away now and then to avoid being obvious, or he may keep selling. Enter a sell order at the uptick you feel is a good place to short, and of course enter your stop market buy order after receiving confirmation.



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Successful Online Daytrading Training Resources

## Getting Your Trigger Finger Ready: How to Overcome "Fear of Trading"

### ● Main Points:



All of us have a "Fear of Trading", (usually often!), as we fear losing money in our trades. This is healthy and normal. What is unhealthy and stupid is to fail to **protect** your capital and enter a daytrade as though you are an investor, thinking "it's a great stock for the long term."

"Scared Money  
Doesn't Win"

*The minute you confuse daytrading with investing is the minute you start losing capital to those of us who are daytraders. In fact, we count on it. (This was my most difficult lesson to learn as a new daytrader.)*

### Tips for Building Daytrading CONFIDENCE:

#### Examples:

**First:** To **REDUCE** the Fear of Trading, **Enter a Sell Stop Market Order** IMMEDIATELY after receiving your buy confirmation from your broker. This will protect your capital and let you know what the downside is upon entering the trade. (click the link for more on this). My stops are always within 2-3 spreads of my buy price. This is an ultra-conservative strategy that limits my losses to \$20 - \$200 per trade maximum.

As you'll find in other pages, it's fine to get "stopped out" several times til you get the real bottom, or on wiggles. It's *not* fine to take a 1/2point or larger loss.

**Second:** Practice papertrading until you get correct on at least 1/2 your trades. Because of your use of trailing stops and stop market orders, you do not need to be right 80%+ of the time to make money. Your risk:reward ratio is profitable.

**Third:** Start with small share trades (100-300 shares) until you build confidence in your trading skills. Increase your share size to 500+ shares only after you've been trading 6 months or longer.

**Another Idea :** Celebrate small stops taken well. That's as important, probably more important in your first couple of years, than making profitable trades.



Have you ever taken **karate**? The **FIRST** thing you Learn is How To Take A Fall and Not Get Hurt. Same thing in daytrading. Before you get to be a black belt in the offensive, you **MUST LEARN HOW** to **PROTECT YOURSELF** from pro traders like me and the market makers who want to take your money. Be happy with losses under \$200. Be ecstatic for getting out at 1/16th-1/4 point losses.

These things build your confidence as a trader. If you're trading scared, you'll probably lose more. If you have several winning trades in a row, don't get cocky and rationalize that you're "playing with house money". You earned the money. Now, continue trading with the same intensity and care that you did before your winning trades.

**What Else Works?** I tell many of my traders to make sure they have a **comfortable, well-lit trading area with motivational messages and trading tips** posted around to reinforce what works. I still have "Tight Stops - NO EXCEPTIONS" posted on all my monitors.

**Don't drink too much coffee**..you don't want to have to run to the bathroom in the middle of a trade. After a few \$80 cups of coffee I learned that one! lol

Make sure to **communicate your trading goals** to family members and others for support.



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Successful Online Daytrading Training Resources

Worksheets



**Module One: Worksheet 1 - Calling Tops and Bottoms**

- **A key skill in trading is to develop a sense for the approximate intraday bottoms and tops of stocks. Many say it can't be done. It can.**
- **We learn how to play "pivot points" using a combination of techniques:**
  1. Fibonacci retracements (38%, 50%, 62%) of the average daily trading range are worth looking at.
  2. Looking for higher highs and higher lows off a bottom w/volume
  3. Seeing the trade sizes and blocks at potential pivot points on Level 2
  4. "Momentum Patterns" that you recognize as being tradable
  5. Knowing the 5- and 10-day trading range of the stock helps - see [bigcharts.com](http://bigcharts.com).

**You should use this worksheet (or a similar one you make yourself) to help develop your skills to play the tops and bottoms of stocks you trade.**

**Directions:**

1. Choose 3-5 stocks to follow.
2. Write down the multiday trading ranges (top and bottom) for each stock in the space provided. Choose somewhere from 3 to 10 days' range.
3. During each trading day, try to guess where the stock's **most likely** top and most likely bottom will be (write in the space provided).
4. This technique works best for stocks that are in a trading range (eg UIS, NOVL).
5. Use this worksheet to help you learn how not to get "surprised" by a stock's price movement, and to develop patience in entering and exiting trades.
6. Circle an "S" or a "B" to indicate whether you are buying the stock as it is still in an uptrend (B) or if you are trying to pick the bottom as it is selling off (S).
7. Remember that the trading range is often established by 10:30-11:00am EST, so try and call the bottom and top earlier in the trading day. Good luck!





Worksheets

**Module One: Worksheet 2 - Trading Skills  
Practice: Your DAILY TRADING JOURNAL**



- Failing to learn from mistakes and capitalize on gains has been the downfall of many potentially successful daytraders.
- Keeping a daily trade journal like the one included here will help you to spot both profitable and unprofitable trends and patterns in your daily trading style.
- We encourage all our traders to keep a daily trading journal for at least the first 6 months of their trading career.
- You should also keep one whenever you're in a strong winning or losing streak to capture the why's and how's of your trades. You'll start to see patterns developing after awhile that will help you to become a better trader.

**You should use this worksheet (or a similar one you make yourself) to help you see what types of stocks you play best, how long your profitable trades are, and reasons for entering and exiting trades.**

**Directions:**

1. Download and print at least 30 copies of this Microsoft Word file: [tjournal.doc](#)
2. It can be viewed with the word viewer ([link here](#)) or word pad (wordpad doesn't include the table borders, though)
3. Keep a daily trade journal that details your trades for the next month. Start by just making one trade per day minimum for the next two weeks (100-300 shares), depending on market conditions.
4. At the end of each day, study the time of day, reasons for trade entry/exit, and sector you were trading in (internet/techs/boxmakers/retail etc.).
5. Modify your trading style based on what you learn about yourself: your trade management. What did you do correctly? What was an error? Do you know why you entered and exited that last trade?
6. Modify the Daily Trading Journal to include more spaces for areas that you want to capitalize on (for winning patterns) and stop doing (for losing habits).

# Daytraders' Daily Trade Journal

Date: \_\_\_\_\_ Net Profit/(Loss): \$ \_\_\_\_\_

STOCK You	Sector	# SHARES	BUY Price	SELL Price	Net GAIN or LOSS	TIME of DAY Bought/Sold	Total Time in the Trade?	Reason You Bought	Reason Sold
--------------	--------	----------	--------------	---------------	---------------------	----------------------------	-----------------------------	----------------------	----------------


A final note: you should also track your daily profit/loss and trade sizes on a graph (I use excel), so that you can see your progress over time.

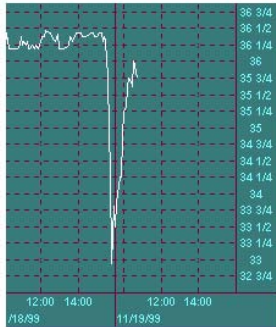
Worksheets

Module One: Worksheet 3 - Opening Gap Trading

Two of the most profitable daytrading plays on the market open are to:



Buy a stock either premarket or on the open that has gapped down at least 5-10%:



Sell a stock on the open that has gapped up by at least 5-10%:



Remember the module 1 trading examples on this topic? (click for review)

Let's practice how to do this over the next week of trading, ok? Remember these are plays that are made premarket and into the open.

Perhaps buy on ISLD premarket after a stock has tanked and buyers are returning (then sell somewhere from 9:30 to 10:00 depending on momentum). Or, short a stock that's gapped up on the first uptick on the open (at 9:30-9:40am)

A second daily skill you should master is to keep an eye on the volume and price action from 9:00am to 9:30am - is a stock you watch gapping up a bit before the market on good volume? If so, there's a good chance it will continue higher on the open before sellers come in. **This is different from the large gap plays you see above** - this is small gapping of under 2-3% generally that is a good indicator of the first half-hours' price movement (9:30-10:00) ahead for the stock.

Medved QuoteTracker - Last Update: 11/29/99 09:14:39 ET (Press F1 for help)

File Portfolio Alerts View Options Window Help

Trade Manual [to] [cancel] Portfolio: !!!ACTIVE YAHOO BC Site: Datek OPTIMIZED (Cus

65 Composite 09:14:28 AM 3,103.57 0.00 (0.00%) NYSE Composite 09:14:28 AM 639.95 0.00 (0.00%) Nasdaq Composite 09:14:28 AM 3,447.81 0.00 (0.00%)

Symbol	Chart	Volume	Bid	Last
MO		3,352,600	26	26 5/16
IBM		3,108,400	104	105
G		2,168,000	40 1/2	40 13/16
KO		1,653,300	66 3/16	66 9/16
ADPT		695,400	56 1/8	55 7/16
AMZN		216,200	97	93 1/8
CSCO		121,700	94 1/2	93 3/16
INTC		83,400	80 3/4	80 1/4
MSFT		43,000	91 1/8	91 1/8
DELL		51,400	42 13/16	42 15/16
CMGI		30,900	152	146 5/8
YHOO		27,000	231	226 1/2
EBAY		17,800	180	177 3/16
EXDS		13,500	129 3/16	126 5/16
JDSU		11,600	267	265 1/2
INTU		9,600	60 1/8	58 13/16
OCOM		9,200	385 1/2	384 3/4

In the example to the right, you can see CSCO has already traded over 120,000 shares at 9:14 am and has gapped up 1 1/4



Worksheets

**Module One: Worksheet 4- News Plays:  
CNBC and Earnings Plays**



- **Profitable Play #1:** The day after earnings are released, many stocks tank (regardless of whether they beat, meet or miss the street's expectations). Buying the opening gap down on stocks that have met expectations is a profitable play, if the bottom consolidates and buyers begin to return.
- **Profitable Play #2:** Stocks will frequently jump up 1/2 point or so on a CNBC mention of the type that "there's no good reason for the stock to be down this much; analysts are positive on it" etc. Of course, you need to be in quickly (within 30 seconds) of the mention or you'll buy the top, where "sanity returns" and the price drops back down to it's earlier level.
- **Note re: CNBC** - these plays are haphazard and there may be a 'delayed reaction', so keep an eye on the intraday chart for a stock you think had a favorable CNBC mention to see what it does. A good example is BEAS, it skyrocketed in the 2nd week of Nov 99 a couple of hours after a CEO appearance and favorable comments from the CNBC gang. It didn't pop up immediately, though, it took an hour or two.

**You should use this worksheet to keep track of the impact of CNBC mentions and day-after Earnings Release stock price momentum.**

**Directions:**

1. Download and print 5 copies of this Powerpoint file.
2. **Choose 3 stocks** that have upcoming earnings releases sometime during the next week. (Note: for Earnings Play and CNBC mention stocks, they do not have to meet our usual stock daytrading criteria, as we are not trading them intraday on a regular basis. Just make sure the average daily volume is over 500K shares). [Click here for Earnings Release Calendar.](#)
3. Also keep an ear open for the type of CNBC mention we talked about (oversold, or great news that hasn't been factored into the stock price etc.)
4. During the week, keep track of the impact of earnings releases for stocks, especially if they meet the street's expectations (earnings are usually released from 4-6pm, after the close of the regular market). Look to see if a gap down (over 5%) occurs on the open of the day following earnings releases, and track



Worksheets

Module One: Worksheet 5- Daytrading Stock Pattern Recognition



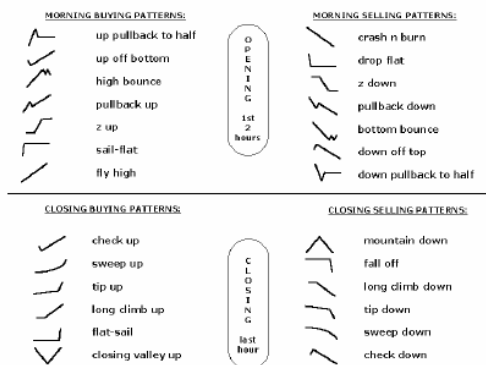
- Another key skill in trading is to develop a sense for the chart patterns that can be profitable when you see them. This is more than simple pennants, flags, triangles and consolidating ranges that you read about.
- In time, you will learn to recognize and be able to trade with common stock chart patterns that occur during the first and last 2 hours of the market.

You should use this worksheet (or a similar one you make yourself) to help develop your skills to identify common opening and closing stock chart patterns.

Directions:

1. For the 3-5 stocks that you've chosen to follow, make sure you can see intraday 1- or 2-minute interval close line charts. (These are easy to read than bar charts).
2. Go back over the last 10 days trading activity for these stocks (see [www.bigcharts.com](http://www.bigcharts.com)) and classify both the opening 2 hours and closing 2 hours into one of the patterns you see in the worksheet below.
3. Write the name of the ticker symbol next to the chart pattern in the worksheet below. See if it repeats (eg tanks at the end of the day, runs up on the open, retraces to about 50% of the opening range etc.).
4. *The purpose of this activity is to help you develop a better sense for the common daytrading patterns you find in stocks that you trade.* Good luck!

Screensnap: Worksheet 5- [Click here to d/l Powerpoint worksheet file \(64K\)](#)



The most common patterns are the "up pullback to half" and "down pullback to half" during the opening. Be sure to understand Fibonacci %ages to help you time trade entries and exits for these.

Virtually all stock movements follow one of these 7 morning patterns (buy or sell charts) and 6 closing patterns (again, buy or sell charts). Note that the "cup and saucer" and other formations are frequently true for multi-day and longer term trends. We are interested in daytrading trends here. We also look at the simplistic pennants, flags and triangle patterns in our first TA page, [click here](#).



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Activities

Module One: Activity 1 - Choosing Your Trading Stocks



- One of the most important decisions you'll be continuously making is "Which Stocks Should I Trade?"
- Be sure to read the "[How to Choose Stocks to Trade](#)" page first before doing this online trading activity.

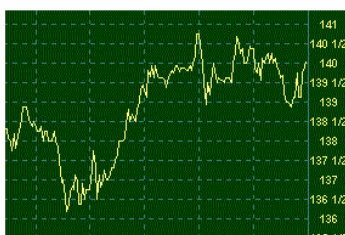
**GOAL** for this activity is for you to be able to pick 3-5 "core trading stocks" you would like to daytrade for the next several months.

**Directions:**

1. Choose 3-5 stocks to follow (you can use the stocks from [Worksheet 1](#) if you want).
2. Using the criteria on the "How to Choose Stocks" page, **create a new portfolio** in your favorite portfolio-tracking program or web page. Again, I'd recommend the [QuoteTracker](#) program.
3. Double check to make sure your stock picks meet the following criteria: average volume around 1M-3M shares/day; intraday trading range of 5% or better (critical), and a price that would allow you to trade 100-300 shares at a time, given your trading capital. *(Note: for any new trading training activity, always use small shares and don't worry about making a ton of money; these are to help you develop and apply the "on-the-job" skills. Later, you'll be increasing your trade sizes to 500-1K shares).*
4. Figure out how much you could've made if you'd successfully traded 80% of the best intraday range for each stock during one of the next several trading days.
5. Using your worksheet 1, figure out what your current profits would be in this "papertrade activity".

**Examples:**

You decide to keep track of DCLK, TDFX, NOVL, SPLS and EGRP.



In looking at the chart to the left (DCLK), you see the max range is:

**bottom = 136 1/2**

**top = 140 1/2**

or a 4-point difference. This doesn't quite meet our 5%-

rule, but is close.

If you had made a good trade in this stock for 80% of the range, your profit would be 80% of 4 = **3 1/4 points**.

I use 80% because almost nobody nails the exact top and bottom consistently; 80% is a realistic target to trade for.

At the end of several days, you'll find out how you did using these initial trading system approaches. There are many more things to learn in order to daytrade effectively; this activity will help you *get started* with the objective, logical trading skills you'll need to trade successfully. These type of activities help you build **trading observation and discipline skills** needed to survive.



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Successful Online Daytrading Training Resources

**Activities**

**Module One: Activity 2 - Using Limit Buys, Trailing Stops and Market Sell Orders**



- You should master using **Limit Orders to Buy and Market Orders to Sell**
- We should also practice using trailing stops in this online trading activity.

**Examples:**

Your **GOAL** for this activity is for you to be able to get comfortable routinely using **Limit Buys, Trailing Stops and Market Sell orders** for your stocks using your brokers' order execution interface.

**Directions:**

**BUYING STOCK ACTIVITY:**

1. Choose 1 of your core stocks to trade. You will look for a good time to buy from 100-300 shares of this stock in the next couple of trading days.
2. Enter a **Limit Order to Buy** your stock at the Best Inside Bid price. You want to see if someone will "hit your bid" and buy from you on the bid, versus you paying full retail (buying the Asking/Offer price).
3. If you don't get a fill, don't chase it if it's running up fast.
4. If it's still in a narrow trading range and you haven't gotten a fill yet, try again, and this time use a Limit Buy at 1/32 Above the current Best Inside Bid price. (for example, if SBUX is trading 26 5/8 x 26 11/16, enter a Limit Buy 300 SBUX at 26 21/32). Now on 300 shares you're only saving \$9, but when you start trading frequently, and in larger lots, it makes a big difference to your profits.

**Limit Buy Orders**

**Datek Online Express**

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I understand that any extended-hour order I enter will be represented exclusively on the Island EON. By placing an extended-hour order, I agree that I have read the Extended Hours Disclosure, and understand the unique risks associated with [Extended Hours Investing](#), and understand the unique risks associated with Extended Hours Investing.

Please [click here](#) to enable Extended-Hours.

Warning! Please do not use your BACK, RELOAD, or REFRESH button on express servers. In addition, please do not double click on the "Enter Order" button to place a trade. These actions will duplicate your order. Access other areas of the Datek site from <http://www.datek.com>.

Buy/Sell	Quantity	Symbol	Price	Order Type	Expire	Stop Limit
Buy	300	SBUX	26 5/8	Limit	Day	

Password

Datek Online does not provide a quote at the time of order entry on this Express server. You should consult a reliable quote source prior to entering an order.

## TRAILING STOPS ACTIVITY:

1. Now, immediately enter a Stop Market Sell order for the number of shares you bought at a conservative level. If I had just bought 300 SBUX at 26 5/8 I would use a stop of 26 3/8. Don't worry about making the stop "too tight"; tight stops are what gives you 'more chances to play'. Personally, my stops are always 2-3 spreads under my buy price.
2. If your stock goes down, ok you get stopped out with a small loss.
3. If your stock begins to head up, wait til it has ticked through another 2 spreads, then Cancel your existing open Stop Market Sell order (and hit 'daily activity' to confirm it has been cancelled) then immediately enter a new Stop Market Sell order 1/16 above the old one (a trailing stop). Repeat this as the stock price moves up.

## Trailing Stops

**Datek Online Express**

[Open Orders](#) [Portfolio](#) [Daily Activity](#) [Messages](#)

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Buy/Sell	Quantity	Symbol	Price	Order Type	Expire	Stop Limit
Sell	300	SBUX	26 3/8	Stop Market	Day	

Password:

Datek Online does not provide a quote at the time of order entry on this Express server.  
You should consult a reliable quote source prior to entering an order.

## MARKET ORDER SELL ACTIVITY

1. **Let's assume you have a trailing stop that's 2 spreads (1/8 point total) under the current market. You're in the green by 11/16 of a point (SBUX is at 27 5/16). Do you take your profit?**
2. First, check the overall condition of the sector index of the stock you're playing (eg \$GIN, \$SOX), then the \$COMPQ and the \$TRINQ. If the large indexes are headed back down, you might want to sell. If they're storming up, consider holding.
3. More importantly, check the volume, market maker orders and time & sales trend (if you have level 2) for your stock. What's it telling you? Is the tide turning and more sellers are selling than we have buyers that are buying?
4. **When in doubt, get out.** I get rich taking profits off the table too early. Fella by the name of Rockefeller said that too lol. Maybe the stock runs up another 1/2 point. That's ok, I booked a profit and made a good trade. I got the 'sweet spot' in the middle of the trend.

5. So, you see buyers drying up and your trailing stop is 1/8 pt. under the market. The major indexes are headed south. What do you do?
6. Cancel your current Stop Market Sell order, hit 'daily activity' to confirm it has been cancelled.
7. Enter a Sell Market Order immediately to lock in the extra 1/8 pt profit. (in this example it would be Sell 300 SBUX Market). Let's say I get it all sold at 27 1/4 (it ticked down a teeny as the order was selling). That's a profit of 5/8 (or  $$.62 \times 300 = \$186$ ) in a few minutes.
8. Get a drink of water (or coffee). Watch the gang on CNBC for a few minutes. Then, back to the charts. Where's the naz headed in the next 20 minutes? Volume? Time of day? The trade wars continue. You have just won a battle. Congratulations

## Market Sell Orders

**Datek Online Express**

[Open Orders](#) | [Portfolio](#) | [Daily Activity](#) | [Messages](#)

I understand that by choosing the server, I have agreed to bypass a confirmation page. I agree to review every order before entering it. I understand that trades placed electronically may be executed before I can cancel it. I understand that all trades entered via the Internet are solely my responsibility.

I understand that any extended-hours orders I enter will be represented exclusively on the Island ESN. By placing an extended-hours order, I agree that I have read the Extended-Hours Disclosure, and understand the unique risks associated with [Extended-Hours Disclosure](#), and understand the unique risks associated with [Extended-Hours Trading](#).

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Warning! Please do not use your BACK, RELOAD, or REFRESH button on express servers. In addition, please do not double click on the "Enter Order" button to place a trade. These actions will duplicate your order. Access other areas of the Datek site from <http://www.datek.com>.

Buy/Sell	Quantity	Symbol	Price	Order Type	Expire	Stop Limit
Sell	300	SBUX		Market	Day	

Password:

Datek Online does not provide a quote at the time of order entry on this Express server. You should consult a reliable quote source prior to entering an order.

That's it. This is one successful approach I use to take small consistent incremental profits out of the market. It will take practice to get right. Remember my "10:30 Nasdaq bounce" observation; when the nasdaq starts on a down note and sells off in the morning, it will frequently bounce back up around 10:30am maybe 60% of the time. This is a high-percentage time to buy stock. Don't ask me why - perhaps institutional buy orders are triggered at that time. Also watch the market at 3pm when the bond market closes.



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Successful Online Daytrading Training Resources

Activities

Module One: Activity 3 - Scalping Under-\$30  
stocks



- Learning to take daily small incremental profits ("sips") from the market via basic scalping techniques is a core daytrading skill to develop.
- For now, we'll focus on scalping without Level 2 (L2 scalping will be covered extensively in Module 2).

**Examples:**

Your **GOAL** for this activity is for you to be able to get comfortable routinely taking **1/4 point - to 1/2 point wins** from the market (remember to use stops of 1/8 or 3/16; you need to have a profitable win/loss ratio).

To do this, **you will need to buy at the bid** (most important). New traders, sell at the market when you see the first 'pullback' (price is dropping back). If you bought and the stock starts dropping immediately, exit the trade quickly (stop at 1/8-3/16pt).

For the more experienced traders (over 1 yr experience), **sell at the ask** if stock is going your way (enter a sell limit order while the stock is still upticking, before it turns). If you're late and the price is fading back, then cancel your sell limit order (wait for confirmation), and fire off a sell market order.

**Directions:**

**SCALPING STOCK ACTIVITY (Basic Non-Level 2 Approach):**

1. Choose 1 of your core stocks to trade that has a spread of 1/16th point and is currently trading at over 1million shares volume at the time you want to enter the trade. Also pick one that has a relatively flat intraday chart (new scalpers). (*why? Liquidity, you do not want to scalp stocks with low volume and large spreads, you'll lose. You need to be able to buy and sell very quickly*). Make a note of the support and resistance levels for this stock. You will look for a good time to buy from 100-300 shares of this stock in the next couple of trading days.
2. **Note that you will plan on spending no more than 20 minutes in this trade.** I usually like to make these 5- to 15-minute round trip trades. **Note that winning trades are almost always "winners from the start"**. You might get a 1-spread shake and then it moves up. If you entered the trade incorrectly,





Activities

**Module One: Activity 4 - Daytrading Relative Strength Patterns**



- **Learning to trade within sectors (like the pros do) will help you spot the strongest stock in a group to trade. See Module 1 page 12 for an intro.**
- This is a professional, easy-to-use technique that should help your trading profits increase.

**Examples:**

**Your GOAL for this activity is for you to be able to learn to follow 5 stocks within either the internet or semiconductor sector. By doing this, you should be able to identify the strongest vs. weakest relative strength stock to trade within the sector.**

**Directions:**

**Your first decision: choose either the semiconductor (\$SOX) or internet (\$GIN) sector to watch for a 1-week period of time. (note: your quote source may use / or ^ instead of \$)**

- Put up a small 3-minute index chart (either \$SOX or \$GIN) at the upper left corner of your screen. (it should take up 1/9th upper left corner of your screen).
- Now, put 2 same-size charts for the "sector leaders" in the upper center and upper right corner of your screen. Sector leaders for \$GIN = YHOO and AOL, for \$SOX = INTC AMAT.
- This upper third of your screen is now your "primary indicator": you've got the composite index for a sector plus two of the "generals" or lead stocks.
- Finally, put 2-4 intraday charts in the bottom 2/3 of the screen for your favorite stocks within the sector you've chosen. Do not, for example, put MSFT or WCOM in here! If you're learning sector strength for internets, then choose other net stocks (MSPG LCOS CNET DCLK ATHM etc.). For semi's, choose stocks like XLNX KLAC etc.

**Your screen should look something like this** when you've finished setting it up and are ready to follow the stocks you are trading:

\$GIN Internet Index Chart ( Intraday)	YHOO Intraday Chart	AOL Intraday Chart
---	---------------------	--------------------



### **How to Build Your Sector Relative Strength Trading Skills:**

You are watching for RELATIVE WEAKNESS or STRENGTH for your stocks **in COMPARISON with** the index and sector leaders. Your skill is developed as you learn to IDENTIFY DIVERGENCE between the index/leaders and the specific stocks that you trade.

**Question:** If the index and/or sector leaders show weakness and seem to be selling overall throughout the morning (or day, if you're playing the afternoon session), yet your stock remains flat/choppy, what does that tell you?

It tells you that your stock has a **STRONG** relative strength and that you should watch it for a buying opportunity once the index and/or sector leaders start to head back up on buying.

And the inverse is true too, of course: if your stock is selling and the index and leaders are buying, then you have a weak stock that you should not buy (or should consider shorting).

**As always, check the current volume of your stock compared to it's average daily volume for the last 10-20 days to see if it's being bought on higher-than-average volume (a bullish sign).**

Learning to play within sectors is a great way to make a living. I tend to like the semis and nets because they have good volatility and range. You might also want to watch and trade the boxmakers, wireless/telcos, retail or other sectors. This is a useful trading skill to develop.

Activities

Module One: Activity 5 - Just for Fun



Examples:

- Your daytrading efforts should never feel like gambling
- That having been said, some of the money management techniques involved in gambling can occasionally be useful to the astute daytrader

"Just for Fun" Activities:



1. Rent the movie "Rounders". Which of these four gambling types do you think you should try to be like as a daytrader? Which should you avoid?

- **Matt:** the up and coming legal student (star of the movie) who has the skill, but lacks the discipline, to be an effective poker player. He gets swept up by emotions such as hope, greed, and fear; especially when around others like his friend (stockplayers, this is equivalent to being in some of those chat rooms out there!).
- **Worm:** Matt's friend, the guy who gets out of jail at the start of the movie. Always in trouble, tries to cheat at cards all the time. Gets in hock using friends' money. This is equivalent to the stock trader who always looks at "pick lists", borrows on margin and from family/friends' money (including the rent money!) and tries to "beat the market".
- **Knish:** the older guy who tries to help and mentor Matt; his best line in the movie was "I don't take chances, I depend on my playing to pay alimony, to pay my rent. I push when the cards are hot and back off when I'm down. I do this for a living".
- **Teddy KGB - the Russian:** he's "the house"; plays by the rules and is very skilled. Extremely well-capitalized. Let's say he's the equivalent of a market maker like SBSH or MSCO.

*Answer: you definitely don't want to trade like Worm. Let's say for now you're Matt, but your goal is to be like Knish. He doesn't go for homeruns. He does this steadily for a living. As Kenny Rogers said, he "knows when to hold them and when to fold them". He makes a living at this. He doesn't get surprised. He knows his limits. Note: this movie isn't a great movie, it's 'just ok' maybe 7/10 rating ([Casino](#) is a great movie, 10+/10), but it has an interesting lesson to learn re: the emotions of putting money on the table to try and win. A must-see for daytraders.*



## "Just for Fun" Activities:

1. Rent the movie "[Wall Street](#)". What trading characteristics does Gordon Gekko (Michael Douglas) have that are admirable? What do we want to avoid? How about Bud Fox (Charlie Sheen)?

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a shrewd market maker working for SBSH. He becomes a rogue trader, breaking the law.

- **Bud "Newbie" Fox:** the new kid, way in over his head, gets blinded by the instant wealth that's possible from trading stocks. Unethical trading spoils his future as he lets himself get caught up in Gekko's illegal and unethical insider trading methods. Think of him as a new trader with a "hot stock tip" or as a current well-known chat room figure who is being investigated by the SEC for pump-and-dump practices.

How would you respond to the temptation that Gekko presents in this film? How do you struggle with trading decisions based on data that you have available? Ok, we'd all say we'd never participate in insider trading, but how about responding to pressure to buy specific stocks (often questionable) that you see hyped in chat rooms and message boards?

What's the right answer? Hopefully we all know it's old-fashioned hard work and DD, relying on our knowledge of TA and trading discipline, especially small stops, to keep us in the game and playing profitably.

What personal trading struggles have you dealt with? Make sure to understand and apply the concept of trailing stops for your trades.

## Module Two

### Comprehensive Level 2 Trading Techniques:

Click on each link for a new daytrading lesson. Be sure to complete the trading worksheets and activities for each module.

[Back to  
DTU CAMPUS MAP](#)

Click on each line for daytrading lessons from the list below. An underlined link means the content is now available. **Note: click on your browser's "reload" button to make sure you see the latest modules posted as they become available.** Remember to set your screen resolution to at least 1024x768 to enjoy DTU.



#### Trading Lessons



= Updated pages w/in last 48 hours.

DTU Module Two Lessons:



- [Level 2 Basics: Understanding Level 2 and Setting Up Your Level 2 Windows for Trading](#)
- [Understanding how to read market makers' true intentions](#)
- [The market maker's tools: Understanding NWII - Nasdaq Workstation II](#)
- [Looking for 'headfakes', reversals & pivot points, recognizing net buying vs. selling](#)
- [How to spot the ax using Level 2](#)
- [Trading with the lead axes: MSCO, GSCO, MLCO, SBSH](#)
- [When to enter and exit trades based on Level 2 signals](#)
- [Using TA and 1-minute charts with Level 2: the big picture](#)
- [Time & Sales part 1: Reading blocks and volume](#)
- [Time & Sales part 2: Reading tape speed and momentum plays](#)
- [Time & Sales part 3: How to read and trade tape resistance & support](#)
- [Anticipating upticks in price movement using Level 2](#)
- [Using trailing stops and "3-spread stop loss rule"](#)
- [Seeing pivots and momentum pauses in Level 2](#)
- [Order Routing via ECNs, Selectnet, SOES;incl pop quiz](#)
- [How to avoid getting shaken out/faked out on Level 2: using your charts to confirm trade entries and exits](#)
- [Additional insights into how & when to use Level 2](#)

All-new! Click the realplayer logo for a video clip to illustrate Real-Time trading relevant to that lesson. Another trader service to help you from DTU!

#### Worksheets

[Click here for Powerpoint viewer program](#)

[Click here for MSWord view program \(3.5Megs\)](#)



- [Stops and Spreads in Level 2](#)
- [MM Headfake Plays](#)
- [Graphs, T&S and Level 2](#)
- [Shadowing MM Buyers](#)

### Activities

- [Name that Ax](#)
- [Finding T&S Support and Resistance](#)
- [Reading the Outside Bid and Ask-](#)
- [When the Market Maker Flips Over](#)



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24 7/16	100
24 7/16	200
24 7/16	1.00K
24 7/16	500
24 7/16	1.00K
24 7/16	200
24 7/16	200
24 1/2	200
24 1/2	500
24 1/2	100
24 1/2	500
24 1/2	100
24 1/2	100
24 1/2	500
24 1/2	100
24 7/16	100
24 7/16	200
24 7/16	1.00K
24 7/16	500
24 7/16	1.00K
24 7/16	200
24 7/16	200
24 1/2	200
24 1/2	500
24 1/2	100
24 1/2	500
24 1/2	100
24 1/2	200
24 1/2	500
24 1/2	100

• **Level 2 Basics: Understanding Level 2 and Setting Up Your Level 2 Windows for Trading**

• **Main Points:**

- **Level 2** is a tool that's best used **in combination with other indicators** to fine-tune your daytrading entries and exits. Level 2 is a microscope that must be used with intraday chart patterns, time & sales and overall market direction for successful trading.
- The Level 2 window shows you all the **market participants** for a stock at a given moment in time, including the **relative strength** of buyers vs sellers.
- **Market participants** can be classified as: trades represented on **ECNs** (ISLD, INCA, ATTN, TATO BTRD), **Instinet** (INCA), major **market makers** (GSCO SBSH MLCO MSCO), ARCA, and others. Knowing the difference in what it means when these people are representing their trades on Level 2 is important to success in daytrading. (eg HRZG frequently posts phony bid sizes, SBSH rarely headfakes, etc.). Following 'the ax' is an important skill to develop.
- The **Time & Sales** window (on the right, 'the tape') is the most important part of the Level 2 window to master, not the width and sizes as represented by various color bands.
- Level 2 bid and ask sizes alone will fake out the inexperienced trader. You cannot daytrade with the level 2 window alone.

Understanding NASDAQ Level 2 Charts

Take a look at this level 2 chart for CHRX, trading 10.5 million shares as of 11:51 am EST. A block of 40K has just gone off at the bid (bearish).

**Inside Market (Yellow band)**

Where the best bid and ask offers are displayed, in order of size, by market participant. Most important band to watch.

**First Outside level (Green band)**

A key band to pay attention to; a leading indicator to see where the mms think the price will go.

CHRX		Best Market		P	T	OK
CHRX + 12 1/16 b 12 a 12 1/16 81 x 7 10.5M 11:51						
MMID	Bid	B...	MMID	Ask	A...	
ISLD	12	81	WARR	12 1/16	7	12 1/16 200
WASH	12	48	ISLD	12 1/8	33	12 1/16 1,00R
HRZG	12	43	INCA	12 1/8	30	12 1/16 400
SHWD	12	28	HRZG	12 1/8	20	12 1/16 500
INCA	12	15	SHWD	12 1/8	10	12 1/16 1,00R
REDI	12	11	LEGG	12 1/8	10	12 1/16 300
ARCA	12	5	REDI	12 1/8	6	12 1/16 300
HMQT	12	3	WASH	12 1/8	5	12 1/16 1,00R
SLKC	12	2	NITE	12 1/8	1	12 1/16 40,00R
NITE	12	1	FBCO	12 1/8	1	12 1/16 300
SELZ	11 15/16	10	SELZ	12 3/16	1	12 1/16 1,00R
JANY	11 15/16	1	SBSH	12 3/16	1	12 1/16 100

2nd/3rd Outside levels  
(Blue/Red bands)

Not very important, except to see where the ax fades to. This defines their "trade box" (more later).

BUYERS  
(Demand)

This column shows the price levels at which mm's are willing to pay for stock at this moment.

SELLERS  
(Supply)

Shows the price levels at which mm's are willing to sell the stock for at this moment.

TIME & SALES

The most important part of the display, T&S shows the size and price that stock changes hands at. It also shows the momentum of the stock as it scrolls by. (time is not displayed on this t&s ticker, just the price and quantity).

Note also that the "spread" between best bid and ask prices for this stock is 1/16, which is common for cheap stocks. The more expensive the stock, the wider the spread can get (from 1/4 point to 3/4 or so).

### Understanding What You're Really Seeing on Level 2:

- Level 2 shows the supply and demand, the transaction pace, the tape trend and the market participants in a stock all in one handy display.
- The numbers that are supposedly used to indicate the number of shares that a market participant (either a mm or via an ECN) is a worthless indicator and can be misleading. In the level 2 chart above, you see there's 8100 bids on ISLD, 4800 from MASH etc. (add 2 zeroes to the number to get the number in the bid or ask). Why is this? Market makers and traders on ecns can quickly cancel their orders, and mm's almost always use their "REFRESH" key to either keep buying or selling stock at a given price level. The T&S shows what's really happening.
- The width of the color bands (especially the first outside level, in green) can be a very useful indicator, it shows how many "new faces" are entering orders at each price level in the bid and ask columns in anticipation of a price move.
- The Time & Sales column shows the actual trades as they occur, and is the most important piece of information I use when daytrading. We'll devote at least 3 entire lessons to this critical skill of tape-reading momentum support and resistance levels, pivots and trends.
- An overall clockwise motion indicates selling in the Level 2 display (eg if buyers at 12 were to evaporate and 11 15/16 became the new best bid, 12 becoming the best ask).
- An overall counterclockwise motion indicates buying in Level 2 (eg if sellers at 12 1/16 are taken out and 12 1/16 now becomes the best bid, 12 1/8 rolls up to become best ask).
- We're usually in an out much faster than this clockwise motion shows us, to succeed you need to intensely focus on the tape and the number of market participants in the yellow and green bands.
- The more buyers you have lined up in the yellow bid column, the wider the "safety net" is to give you time to sell without losing much.

### Examples:

Remember our daytrading approach is always like a funnel; we make a very rapid mental checklist prior to entering a trade of these things:



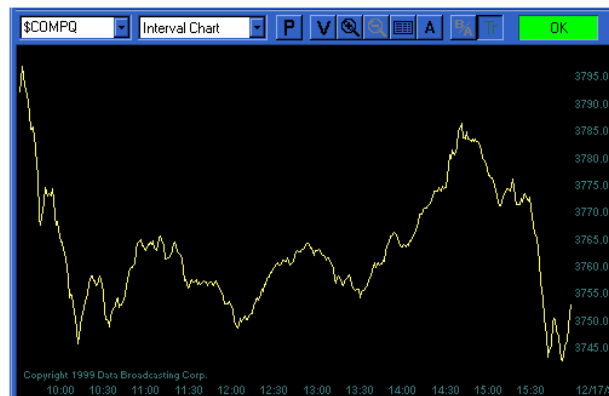
- **FIRST**: Overall Market Trend and Time-of-day, \$TRINQ, spoos/naz futures
- **SECOND**: Trend for Sector/sector leaders (eg \$GIN/\$SOX),
- **THIRD**: Review the 5-day support /resistance of the stock we're playing
- **FOURTH**: The intraday double bottoms/tops/trend of the stock (unless it's a news or bounce play), along with volume, stochastics/RSI/MACD,
- **FIFTH**, the width of the bid/ask levels in our Level 2
- **FINALLY**: Time & Sales, which we watch like a hawk prior to entering/exiting all trades.

**How long does this scan take? Less than 10 seconds for the first five steps above.** You patiently watch time and sales to see the true momentum of the stock prior to buying or selling it.

Your trading rig should be set up to make this like seeing the dashboard of your car. You know where things have come from and can anticipate "where they're going" with a fair amount of certainty very quickly.

Let's look at an example here, VRTY buying on a bottom bounce on volume strength:

**FIRST**: Checking the NASDAQ composite direction, see the naz bounced at 10:30 as usual (my 10:30 naz bounce on an open selling day rule). I was looking to buy stock on this second bottom bounce at 10:30. Also check the trinq, prem, spoos, naz futures if you like.



**SECOND**: Sector index or trend; Since VRTY was a special case (bottom bounce on oversold after bad news play) we didn't check the sector players. We usually do, however.

**THIRD:** Five-day chart (on the bottom right below in my setup, the horizontal graphic w/level 2), shows support at 27. The stock oversold from 52 to 27 and has bounced from there. A loose stop would be at 26, my stop is always 2-3 spreads down from the current inside bid. I know where the stock is coming from, and the upside potential based on fibonacci bands. (you should review the 5-day charts prior to market open for the stocks you're going to trade). **FOURTH:** I quickly scan the intraday chart's technical indicators (RSI, stochastics, volume and MACD) to see if it looks like a good place to buy. 10:30 seemed like a good place to buy - see the MACD lines crossed and headed up, the slow stochs had just made a double bottom, and the RSI touched the top yellow line. Volume also jumped. Time to zero in on the trade. All systems go.



**Level 2 and Time & Sales:**

VRTY	c	33 3/8	b	33 1/8	a	33 3/8 x 20	13.0M	Dec778:23
MMWD	33 1/4	22	ISLDc	33 5/8	3	33 1/4	1000	
REDC	33 1/4	22	ISLDc	33 5/8	3	33 1/4	300	
ISLDc	33 1/8	2	SHWDc	33 1/2	14	33 1/4	800	
HRZGc	33	10	WASHc	33 1/2	3	33 1/8	5,000K	
WASHc	32 7/8	1	HRZGc	33 1/2	2	33 1/8	1,000	
COWMc	32 5/8	1	AGISc	33 1/2	1	33 3/16	500	
AGISc	32 9/16	10	WONTc	33 1/2	1	33 3/16	200	
SHWDc	32 9/16	1	BESTc	33 5/8	40	33 3/16	1000	
BESTc	32 1/2	5	REDC	33 5/8	10	33 3/16	200	
WONTc	32 1/2	1	NITEc	33 5/8	10	33 1/8	500	
INCSc	32 1/4	1	COWMc	33 5/8	1	33 1/8	1000	
WAGLc	32 1/4	1	YESTc	34	30	33 1/8	700	
PLTC	32 1/2	20	SANAc	34	1	33 1/8	500	
CANTc	32	1	CANTc	34	1	33 1/16	500	

**Intraday thumbnail:**



**5-Day CHART below:**



**FIFTH:** Although this level 2 chart is after the market close, it was all buys with wide bands on the ask from 10:30 up

**FINALLY,** We look at the Time and Sales ticker window to carefully see the pace and momentum of buying vs. selling. Is there more green/white than

**Time to trade!** Elapsed time for this quick market scan: under 10 seconds. It's watching the time and sales window carefully that tells us when to pull the trigger.

through noon. In this chart, you can see a lot of selling pressure (profit taking) after the market closed and VRTY had its 6-point run.

red/white? What are the blocks (institutional buys/sells) telling us? What's the consensus of the players in this 5-minute to 15-minute timeframe? T&S tells us this, and more.

Once you're in, you watch t&s for any sign of weakness or selling. Is it "shaking", or are there really more sellers in the stock for the next few minutes? These are the questions we'll learn how to answer in future lessons.

I encourage you to use a similar setup for your level 2 windows: have the level 2, time and sales, thumbnail intraday chart and 5-day chart all together to give you a macro-to-micro look at the stock you're trading. Also have a single expanded intraday chart like the one above with all your technical indicators on it. It works!

**The Role of Using NASDAQ Level 2 to Help You Manage Your Trades**

- Lots of pretty flashing colors. Billions of dollars are made and lost using this deceptively simple-looking device.
- **Remember that Level 2 can fake you out - it's the tape and TA that counts.**
- **A pros' skeptical look at this level 2 chart:** In this example, SBUX went to 5/8 and backpedaled all the way down to 24 1/16 before bouncing again. The yellow looks strong. But look at T&S: lots of trades going off at the 1/2, indicating selling. MWSE and HRZG are no-name market makers on the bid. Tough to tell what the traders on instinct (INCA) and ISLD will do. Meanwhile, solly (SBSH) and MONT are selling stock. In a battle of chippies (ARCA etc) vs big mm's the

MMID	Bid	B.	MMID	Ask	A.
MWSE	24 1/2	102	MONT	24 9/16	1
INCA	24 1/2	20	NITE	24 5/8	9
ISLD	24 1/2	13	SBSH	24 11/16	10
FBCC	24 1/2	10	SLKC	24 11/16	1
MADF	24 1/2	10	PIPR	24 3/4	1
HRZG	24 1/2	6	MLCO	24 13/16	10
PERT	24 1/2	1	GSCO	24 13/16	10
SLKC	24 1/2	1	MISCO	24 13/16	10
ARCA	24 1/2	1	ISLD	24 7/8	20
BEST	24 7/16	10	INCA	24 7/8	10
MASH	24 7/16	1	DLJP	24 7/8	10
BRUT	24 3/8	1	LEHM	24 7/8	1
SWCO	24 3/8	1	MASH	24 15/16	1
MLCO	24 3/8	1	MADF	25	18
ADAM	24 3/8	1	FBCC	25	10
LEHM	24 3/8	1	DAIN	25	2
RSSF	24 3/8	1	HMQT	25	1

**Quick tips:**

Again, the bid/ask sizes are pretty much worthless and misleading. Look at the tape: MONT has just sold 800 shares of SBUX even though his advertised ask size is for just 100 shares (a "1"). Refresh key in motion. He might have 100K shares to sell for all you know. This is level 2, not level 3; you don't know the true order size, and the mm sure as heck isn't going to let you know. They're a bit more useful for the

...and they're big firms and market makers win.

### **How do You manage your trades with Level 2?**

Don't get me wrong, I'd be very hesitant to daytrade without level 2; however it's just one of a handful of things I consider before I buy a stock. Hopefully the method outlined above will help you make a lot of money, as it has for me and other traders.

Go with the tape flow; use the relative width of the bid/ask bands to help you manage your trade exits. Level 2 primarily helps me decide whether to jump in on an ask level that's about to evaporate, to shadow a lead market maker as who's buying or selling in size, and to exit when the buyers are drying up and backing off the inside bid.

you know. They're a bit more useful for the ECNs, such as ISLD, but even those can get canceled in a quick second. Doesn't count.

**The "flow" of time and sales, and the volume going off at the ask price, is a much more useful indicator.**

Use the level 2 price level thicknesses to **help you decide how to bid for stock and how to offer it out on the ask.**

That's all the pretty color bands are for. Again, you never pay up two spreads by buying the ask and selling at the bid (unless you're in a panic to buy/sell, which should occur less than 20% of the time).

Follow one of the major market makers (GSCO MSCO MLCO SBSH) for a stock all day and trade like he does. You don't see a professional pay up retail and sell at wholesale, neither should you. He will have a "trade box" that he makes money in, buying at one level and selling at a higher one. Use level 2 to help you manage your trades like a market maker does.

- Understanding how to read market makers' true intentions

• **Main Points:**

- Market makers' (mm) primary obligation is to their client accounts; they often buy or sell large quantities of a given stock ('work an order') and need to disguise their actions.
- Market makers' secondary role is to "make the market" in the stocks they trade, providing liquidity by buying and selling within a given 'trade box' from 2-6 spreads wide.
- As daytraders, we can profit from learning how to read the intentions of one or more market makers by seeing patterns in the level 2 window (eg., number of times they are at the bid vs ask, when they flip, how many times they refresh).
- Learning how to trade on the side of the primary market maker can be profitable, learning how to avoid trading against the ax is important.
- Some market makers are "bigger" (better capitalized, trade more share volume) than others, and you should pay more attention to these big players (MSCO MLCO SBSH GSCO etc.). Identify the main mm's for your stock with [this link](#).
- Market makers frequently disguise their order flow buy buying and selling on the ECNs like ISLD, ARCA etc. - therefore, watching the action on "ECN buying/selling" vs "Big MM buying selling" is an important skill to develop as well.

There are 3 main Market Maker trading actions you should learn how to read on a level 2 screen for a specific mm:

- BUYING IN SIZE
- SELLING IN SIZE
- 'GRINDING' (making the market)

Let's look at how each of these works, and how to profit from it:

**Examples:**

You have to understand how this whole system works before learning how to daytrade within it. I'm going to take the market makers' perspective first, to show you how these guys deal with the stocks they trade, then show you how to profit from it. This whole market maker section takes up 3 different lessons, starting with this one.

**Example #1 - BUYING IN SIZE:** Let's say you're a market maker working for MLCO and you're working WCOM again today. You get a new client order to buy 250K shares WCOM for your client, a mutual fund manager over at Vanguard. Your performance is measured, in part, by your ability to buy near the lower end of the

Are you going to just jump on the ask and buy up 250K shares? No, you'll run the price up 2 points in the process and buy up for your client at the top of the day. They won't be calling MLCO to work WCOM any more, and MLCO's trading desk director won't be happy with you.

Let's say the level 2 chart on WCOM looks like this:

- **First**, ask yourself "where is the trade box for the market maker I'm watching"? In other words, what price is he willing to buy stock at, and what price is he willing to sell stock at?

Answer for MLCO: Trade box is inside the market at 77 bid WCOM, outside at 77 1/8 ask WCOM. Notice he's on the inside bid and one spread out on the ask (yellow band for bid, green band for ask).

MMID	Bid	B.	MMID	Ask	A.		
MASH	77	214	INCA	77 1/16	17	77 1/16	100
SBSH	77	77	NFSC	77 1/16	7	77 1/16	2.50K
MWSE	77	68	ISLD	77 1/16	7	77 1/16	300
ISLD	77	57	COST	77 1/8	10	77 1/16	300
MADF	77	52	MLCO	77 1/8	10	77 1/16	100
BRUT	77	46	PWJC	77 3/16	1	77 1/16	100
PERT	77	36	OLDE	77 1/4	10	77 1/16	300
LEGG	77	35	FBCO	77 1/4	10	77 1/16	100
MLCO	77	27	HRZG	77 1/4	2	77 1/16	100
HRZG	77	19	ARCA	77 5/16	22	77 1/16	200
PWJC	77	17	SLKC	77 3/8	10	77 1/16	100
GSCO	77	10	MSCO	77 3/8	10	77 1/16	100
NITE	77	10	JPMS	77 3/8	1	77 1/16	100
ARCA	77	10	SBSH	77 7/16	10	77 1/16	100
BTRD	77	10	DLJP	77 7/16	10	77 1/16	100
COWN	77	10	MASH	77 1/2	3	77 1/16	100
DLJP	77	10	NITE	77 9/16	10	77 1/16	100
SWCO	77	10	PRUS	77 9/16	1	77 1/16	100
PRUS	77	9	SHWD	77 9/16	1	77 1/16	100
FCAP	77	9	SALI	77 5/8	9	77 1/16	100
AGED	77	8	AANA	77 5/8	1	77 1/16	100

- **Second**, look at the order flow on Time & Sales: what's the pattern you see? A string of transactions going off mostly at the ask is bullish, at the bid is bearish.
- **Third**, look at whether the market maker is "holding the bid" at a certain price level (bullish) or "holding the ask" (bearish). In other words, lets say in this L2 box sellers using INCA (Instinet) don't budge from 77 1/16 and you see well over 10K shares being sold at 77 1/16. If the bid tier at 77 starts to evaporate (as buyers realize there's a lot of stock being sold) then the price will drop. This is why T&S is so important, the levels may be fake since the mm can refresh or buy/sell thru an ecn to cover his tracks. **T&S is so much more important than the**

Ok, back to our MLCO WCOM example. MLCO may in fact be buying stock through ISLD, and may fade his ask by a level or two if sellers start to fade. He may be sitting out the action for now, waiting for a more favorable entry.

**Daytrader's Play:** The lead MM who is buying in size may go short and sell some stock either directly or through an ECN to push the price downwards initially, then buy a bunch at the bottom, working his order up.

We play it by carefully watching several things:

- The **number of refreshes** at the inside bid vs inside ask (eg a mm is showing 10 bid (1000 shares) but we see him buying 13K shares in T&S).
- The **technical indicators** on our 1-minute chart (stochastics, RSI, previous support/resistance levels and volume).
- The **response from other traders** as they see what's happening. You may well get a bunch of buying (ever see a 'volume spike uptick?'). Don't chase at first, you should have entered when you saw the mm

color bands alone, use them in combination.

What else is useful? In esignal, you can highlight specific market makers, as I have for MLCO, and see even more info in T&S if you wish.

Other software, such as [Ensign](#), also gives you the opportunity to plot market maker activity against the stock price. Some programs let you see the "number of times at best" bid or ask for the market makers playing a stock; a good way to see net buying or selling for the time period you're watching.

**Example #2:** This time, let's say you're the market maker at SBSH and you're working NOVL today. You get a new client order to sell 700K shares NOVL for your client, a mutual fund manager at Fidelity.

- SBSH is in line sell NOVL at 21 1/2, not in a big rush here. How do you tell? In level 2, your "order in line" preference is determined first by the price, second by the order size. Now, SBSH may want to sell more NOVL than all the mm's joining him at the 21 1/2 bid, but he's not going to tell you that. MASH gets first in line by saying he's offering out 107 (10,700 shares) at 21 1/2. It means nothing. He can drop that in the blink of an eye, he is only obligated to buy the tier size on SOES (which is 100, 500 or 1000 shares etc). What counts is the

following one of these patterns we've identified.

- **Ax flips/reversals vs headfakes:** if MLCO suddenly disappears from the inside bid (or 1-2 levels outside bid) to the inside ask, he's telling everyone he wants to sell. The question is, how much volume does he sell? If its over 20K or so you can be pretty sure he's not trying to fake you out.

MMID	Bid	B...	MMID	Ask	A...		
DLJP	21 7/16	10	MASH	21 1/2	107	21 7/16	1.00R
INCA	21 3/8	10	BRUT	21 1/2	53	21 7/16	2.00R
WETH	21 3/8	10	NITE	21 1/2	22	21 7/16	500
ARCA	21 3/8	10	INCA	21 1/2	15	21 7/16	1.00R
MASH	21 3/8	8	MADP	21 1/2	15	21 1/2	200
SHWD	21 3/8	5	WPCO	21 1/2	10	21 1/2	300
ISLD	21 3/8	2	HRZG	21 1/2	10	21 7/16	1.00R
BTRD	21 3/8	1	SBSH	21 1/2	10	21 7/16	1.00R
WPCO	21 5/16	10	GSCO	21 1/2	10	21 3/8	100
REDI	21 1/4	25	PERT	21 1/2	8	21 7/16	700
NITE	21 1/4	22	MWSE	21 1/2	6	21 7/16	700
SBSH	21 1/4	10	PRUS	21 1/2	5	21 7/16	1.60R
BRUT	21 1/4	2	FLTT	21 1/2	3	21 1/2	400
SLKC	21 1/4	1	ISLD	21 1/2	2	21 1/2	300
						21 1/2	200

**Daytraders' Play?** What do you think, gang? Well, we're on a downtick, so you can't short it here right now (see the minus sign in the upper left corner next to NOVL in

refresh rate that you observe in T&S, along w/traders' responses.

- This looks like a bearish level 2 chart, confirmed by the frequency and size of trades going off at the 7/16 in T&S. You'd have to watch the tape for a minute or two to get the feel for the momentum in the stock.
- Please note that most level 2 chart buying and selling is not as obvious like these two L2 charts appear; typically you'll see inside levels of 2-5 mm's wide. You need to pay attention to # of refreshes in T&S. Tape reading is how to daytrade successfully. For example, when do you see "the tide turning" and trades going off in between the bid/ask? (especially for net stocks like DCLK YHOO AMZN). This indicates potential reversals.

the dark green band?). If you've been following NOVL and know that SBSH is the ax (which he usually is, by the way), then you might want to join SBSH's bid at 21 1/4 for the stock (LIMIT BUY NOVL bid 21 1/4).

Ok for the "A" students, lets say 21 1/4 is a support level, and you think the price will bounce hard off 21 1/4 and give you at least 1/4 point scalp on the rebound. **How do you frontrun SBSH and buy before he does?** (which will run the price back up before you can get in?).

**Answer:** Don't bid up higher than 21 1/4. Don't wait til it bounces off 21 1/4 and you have to enter at 21 3/8 in the middle. **Bid 21 1/4 size 11.** That will put your bid in ahead of solly and behind NITE/REDI. If you could get a short off here ahead of the 21 1/2 wall of selling that would be great, but it's unlikely. Again, use 1-minute chart TA to help identify support/resistance and trend info. in addition to level 2.

**Example #3:** Today, it's a choppy low-volume day on the street, not much market direction. But, you still have to make money for Mayer Schweitzer, MASH, your employer. You have to make the market by **grinding out 3/8's**; buying at the bid and selling at the ask for AMZN a few spreads/levels up all day. It's boriing, but you make money doing it consistently. As MASH's AMZN market maker you need to correctly set the limits of your "trade box" based on volume, price momentum and technical indicators.

Again, **identify the market makers' "trade box"** to see where he is playing it. Make note of what causes him to back off or lift stock at each level. Eg, is there a time of day effect (I find may axes often sit out lunch and fade a few spreads in either direction, or

M...	Bid	B...	M...	Ask	A...		
INCA	91 7/8	10	ISLD	92	22	91 7/8	200
MWSE	91 7/8	1	ARCA	92	12	92	100
ISLD	91 13/16	6	MASH	92	10	92	100
MASH	91 3/4	2	BRUT	92	6	92	400
NFSC	91 3/4	1	INCA	92 1/16	10	92	900
MADF	91 3/4	1	DKNY	92 1/16	1	92	100
REDI	91 9/16	5	REDI	92 1/8	2	92	100
SELZ	91 9/16	1	MLCO	92 1/4	9	91 15/16	600
UPMS	91 1/2	1	MWSE	92 1/4	5	91 15/16	100



bid it down to buy for an afternoon run).

**To grind a stock by following**

**the ax**, simply trade like he does: join his bid if he stays there through 5K-10K or more shares of buying (perhaps front run by 1/32 or a size increase); as soon as you have a trade confirmation then offer to sell it at the price level he is at.

**Note that you have to be able to fade and lift like the mm does in order to scalp using this method.** So, a professional direct access broker like cybercorp.com or mbtrading.com is recommended, so that you can immediately sell or cancel your bid with rapid speed. The ax will drop his bid if he sees a lot of selling pressure, and you need with speed. Waiting for a browser-based broker to give you confirmations etc. is probably too slow for this type of trading.

COWN 91 1/2	1	SLKC 92 1/4	1	92 15/16	100
SLKC 91 7/16	1	MONT 92 1/4	1	91 15/16	100
MSCO 91 1/8	10	NITE 92 1/2	20	92	100
STRK 91 1/8	5	MADE 92 1/2	11	91 53/64	100

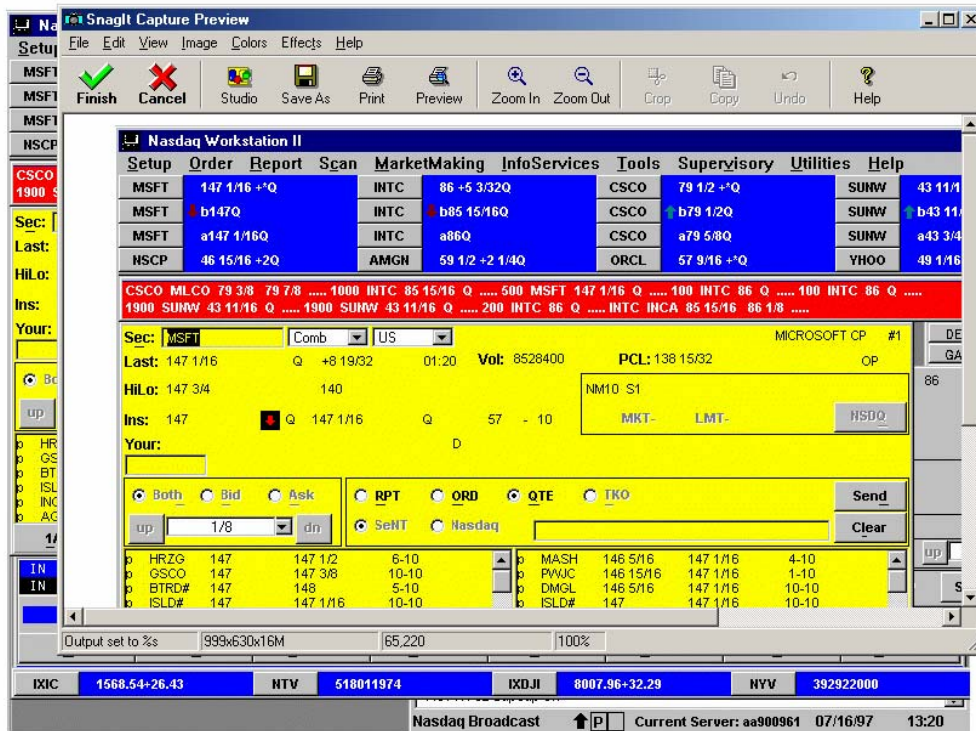
Ok, what's MASH doing here? His trade box is outside bid 91 3/4 size 2 by inside ask 92 size 10. What's he doing? Offering stock out here. Which is a good idea, whole number resistance is a good place to park your sell orders to see if you get a sell.

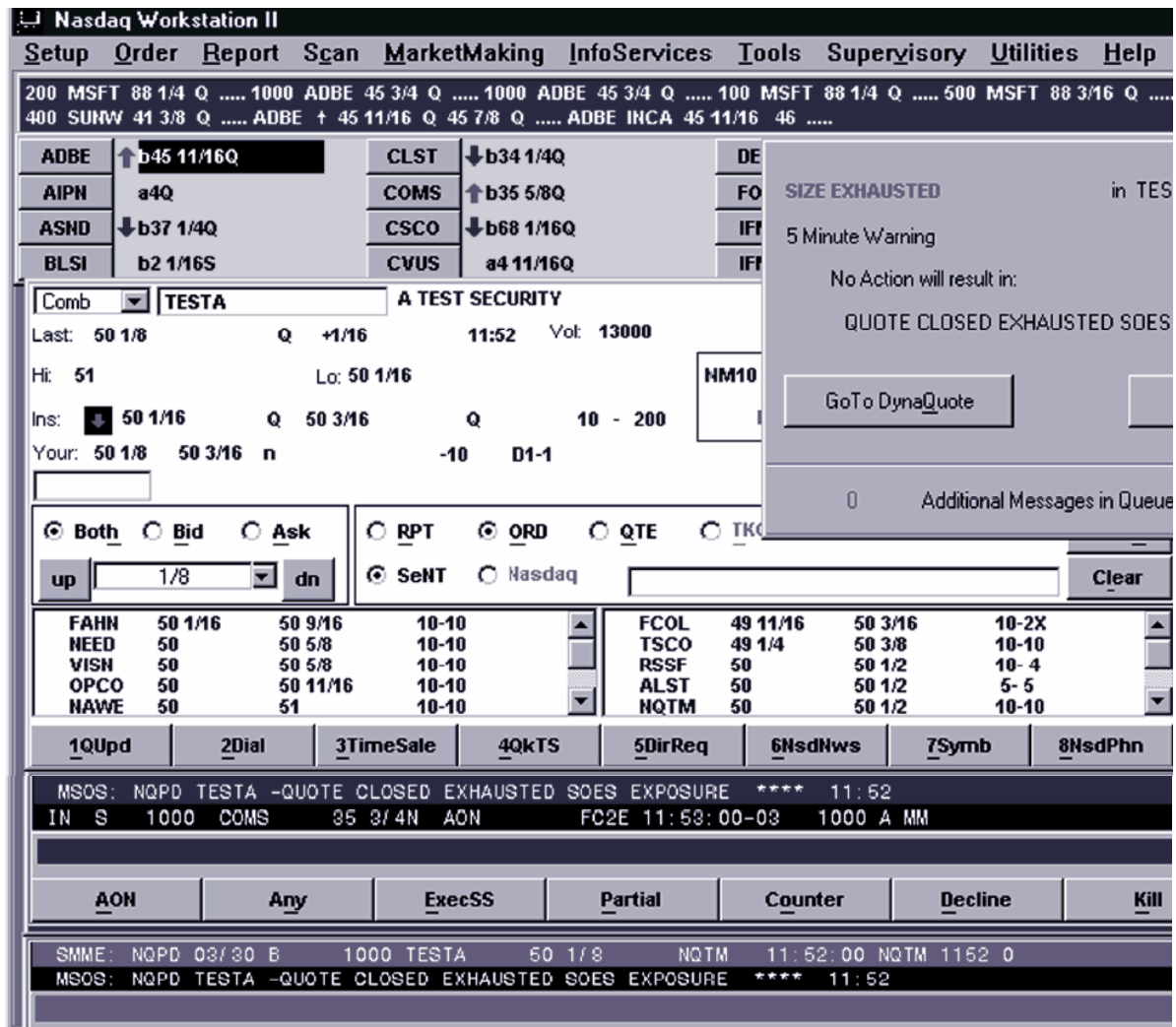
**What would you do?** Since there's a lot of sellers at 92 I'd wait until the bid firms up a bit more before entering a bid (or, you could enter a bid far away from the action, say at 91 1/2). Time and sales is bullish in this screen, as more sales are going off at the ask than the bid. It's a "indeterminate" or low-percentage situation here; I'd wait til you get better indicators before trading the stock. Grinding it with MASH would say, if you're already in from lower, than offer it at 91 15/16.

• The market maker's tools: Understanding NWII - Nasdaq Workstation II

• Main Points:

- Market makers use a software tool called the Nasdaq Workstation II (NWII) to manage their trading activity.
- Sun Tzu says "Know your enemy's strengths and weaknesses..."
- As a daytrader, if you understand how the market makers' key tool works you will be better equipped to trade against them using your level 2 screen.
- There are several Adobe Acrobat .pdf guides on how NWII works available at this [www.nasdaqtrader.com](http://www.nasdaqtrader.com) link; download and review them, especially the NWII Users Guide, Market Making Guide, Selectnet, SOES and Optimark users guides.
- It is very surprising that not a single book or other daytrading site on the internet mentions this critical tool of the market maker and how you can understand and benefit from this knowledge. DTU scores another scoop.
- I'll add examples of how to trade against the market makers as I develop them; for now just familiarize yourself with this market makers' tool.
- Market makers are charged \$1500/month each to use Nasdaq Workstation 2! That's \$18K/yr.





As I gain insight into the market makers' limitations and constraints using this software platform, I will post strategies and tips for exploiting those weaknesses to our advantage.

A quick example is the SOES tier size, the mm automatically fills your order at tier size if you are first in line to buy/sell.

We'll look for other ways to "fight back" using our commercially available broker and 3rd-party software tools, along with trading strategies.

If any of you are former or current market makers who have experience using NWII we'd sure like to hear your insights; we'll be sure to post them here to help others.

- Looking for 'headfakes', reversals & pivot points, recognizing net buying vs. selling

● **Main Points:**

In this lesson you will learn how to spot 3 key market maker (mm) trading actions to help your Level 2 daytrading become more effective. They include:

- **HEADFAKES:** MM initially buying to make the stock look attractive as he gets short in the position, then selling the stock down, covering at bottom. "Gap and trap" is an example. You buy what looks to be a good stock, then the price drops abruptly, you sell in a panic and then it goes back up.
- **REVERSALS & PIVOT POINTS:** When the current trend (either buying or selling) reverses itself...eg. sellers are done and buyers come into play, or buying finished and selling starts.
- **NET BUYING vs SELLING:** Using the "number of times at best" feature and visually watching Level 2 action for major market makers to identify who is actually buying vs. selling (and how to tell when they are masking thier intentions).

Let's look at how each of these works, and how to profit from it:

**Examples:**

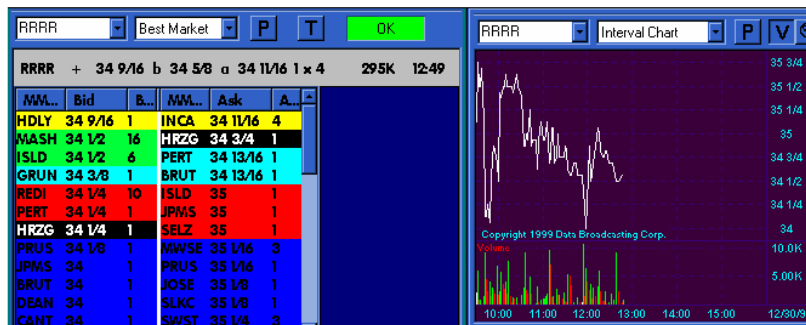
**Examples:**

**Headfakes:**

Some of the medium-sized market makers like HRZG SLKC etc. are more prone to playing games than are other market makers. The larger market makers tend not to play games with bid/ask sizes.

Looking at RRRR here, you can see on the one-minute chart that the stock was bid up starting at 10am. Traders who bought this "second top" were in for a surprise as HRZG sold it off down to the low of the day at 34. What's the stock's trading range? 34 to 35 3/4.

What else would you look for to identify headfakes? The best advice I can give is to closely follow 3-5 stocks on Level 2 for a month or so each day and get to know the behavior of the different market makers and ECN players on the stock. You'll soon learn who the real players are. Remember, to



**Daytrader's Play:** Buy off the low-of-day 2nd bottom and short/sell at the second top, unless there's a breakthrough in either direction. Do not buy the second top of the day unless it's broken through (in this case I wouldn't have been a buyer until it broke through 36 on decent volume). Buying the second or third bottom off support (in this case 34) would be a good play. Don't buy when it's choppy within the trading range, you will get shaken out. Play close attention to the volume and other TA indicators to confirm entries and exit points.

**Avoiding Headfakes:** The steeper the price increase, the more likely a reversal as traders who bought in low sell the stock for a profit. Avoid buying stocks that have run up in a vertical line until there's some kind of consolidation (sideways

succeed in daytrading takes a lot of patience and concentration, using the tools like the professionals do. It amazes me to see the losing gambling behavior of people in many of the chatrooms who are clueless as to how to trade stocks. People like me and other professionals scoop their capital off the table with ease.

trading holding in a pattern for 10-15 minutes), then a continuation of an uptrend.

Especially avoid chatroom under-\$10 stocks that run up on thin (less than 300K daily shares) trading volume.

**On Level 2**, watch for: **fake volume sizes by mm's** (eg HRZG posting 88 bid then fading), **flipping back and forth** from inside bid to ask, and **mm's fading back** a spread at a time even when time and sales looks bullish. These are warning signs that a reversal is about to occur.

### REVERSALS & PIVOT POINTS:

These are my favorite plays, buying the bottoms and knowing when to sell at the top.

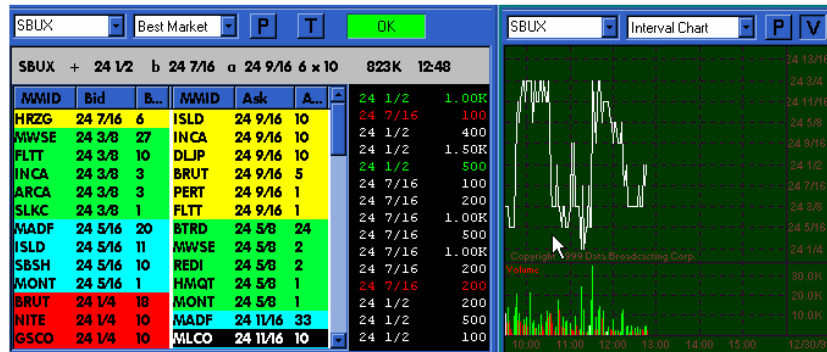
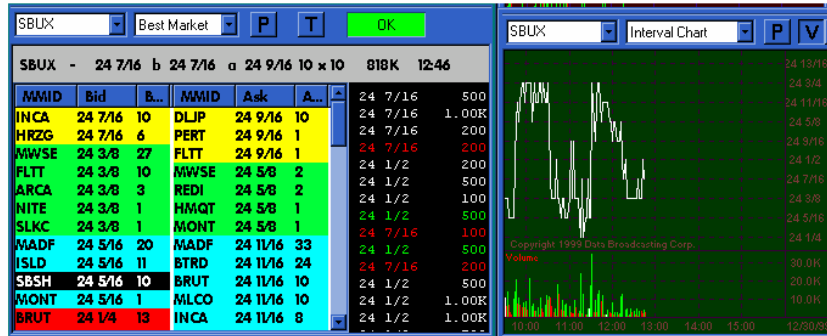
Looking at the intraday chart for SBUX here on 12/30, where is support and resistance? Can you see? Support at 24 1/4 and resistance at 24 3/4. A **profitable trading channel** to play in.

How does level 2 help you with this?

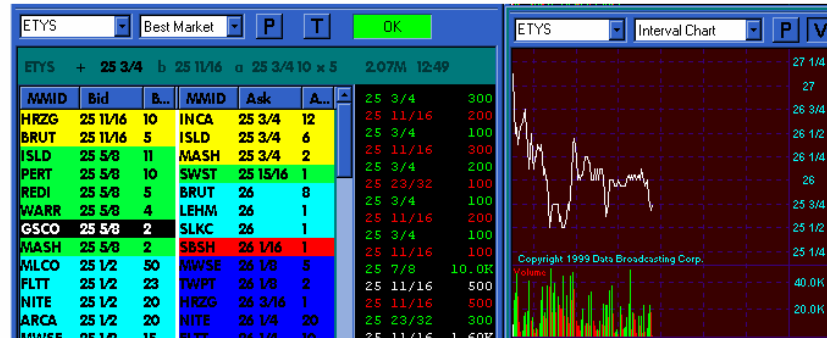
See how I've highlighted SBSH at 24 5/16 bid? Solly knows support is at 1/4 and will buy stock here, unless the market sells off (in which case he'll lift his bid). But, SBUX is a slow moving stock, he waits for it to come down to his level to buy it.

Now see in the second chart how I've highlighted MLCO at 24 11/16? He knows this is the initial resistance level, and has parked his sell tier order here.

Knowing how these two trading desks trade SBUX is very profitable. Join the ISLD bid at 24 5/16 then offer it out at 24 11/16 or 3/4 for a nice profit.



Now let's look at ETYS, a current favorite for bottom-fishing (as of 12/30/99). Where is support and resistance? Well, we can see support at 25 1/2, and I highlighted GSCO as the ax to follow with a thin size 2 bid at 25 5/8. I would place a stop loss in at 25 3/8, as I see MLCO at 25 1/2 bid, and the stock has made 3 reversals at around 25 1/2. It's making lower highs, though, so I'd only play it for a scalp, joining the 25 5/8 ISLD bid here.



**Daytrader's Play:** Reversals on higher volume and second bottoms/tops are key places to look for pivots and reversals. Knowing to follow the ax particularly at the places he puts his bids and asks will help you get better at determining likely pivot points and reversals. As always, use tight stops (under 3/8) to minimize losses if you're wrong. If the stock wiggles and heads in the direction you originally thought it would you can re-enter the position with a small lost trade potential (1/8 max loss potential).

General level 2 reminder notes: watching time and sales as well as volume and overall market direction is important. Remember not to trade during lunch in general (11:30-1:30 or so), and know your stock's intraday market maker ax and support/resistance levels.

**NET BUYING vs. SELLING:**

Talk about a run! Look at NOVL here on 12/30 going from 35 to 40 in the space of an hour. SBSH is the ax for NOVL and was on the inside bid all morning (a bullish sign). Joining him at 35 1/2 and selling at the second shake near 38 is profitable.

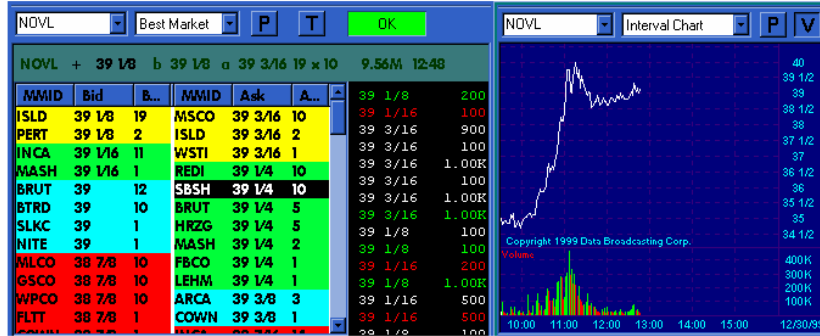
Now that he's on the second inside ask, I'd be more cautious about buying and would look to short the stock where he is offering to sell it at (offer it out at 39 3/16 stop market buy/cover at 39 3/8).

Recognizing net buying vs selling is a tricky business; some software identifies the "number of times at best" bid/ask for the trader; however this doesn't tell you the number of shares that were traded, number of refreshes and size/order flow information.

The best way to spot net selling vs buying is to see the length of time the market maker stays at the inside bid/ask (eg if MSCO stays here selling at 39 3/16, and the stock ticks down to 39 x 39 1/8 and he still stays at 39 1/8 selling, you'd call him a net seller). This depends on the volume of order flow being sold, of course, I'd expect a mm to sell at least 8-15K shares to call him the 'ax' in a stock that trades more than 500K shares/day.

**Note: Market makers will frequently lift off the inside bid/ask to mask their order flow, so keep an eye on their behavior in the green (1st outside level) band as well.** On the whole, are they buying or selling, and have you identified the "biggest player(s)" in the stock at the time you are watching? Remember, the 'ax' will change, especially for the most actively traded stocks.

Also, be sure to know the difference between ECNs (INCA ATTN ISLD ARCA) and market makers (SBSH MLCO MSCO GSCO).



**Daytrader's Play:** Once you spot net buying by the market maker you are following, join his bid and stay with it until he flips. When SBSH flipped to the ask you know it's time to sell this stock, as he has bid it up all morning and wants to lock in his profit at the current price level.

Also be cautious of thin volume, eg here at 12:48pm it's the middle of lunch hour and you can expect some selling down to a fibo retracement level. In general, you should exit your morning positions before lunch (or put in a trailing stop) to lock in your profit. Notice how volume has thinned considerably from the morning runup period.

Looking at this level 2 chart, you also see sellers include heavyweights MSCO and SBSH, and the green outside ask band is thicker than the green outside bid band. This is bearish. Buyers are on thin levels and are mainly ecn players on ISLD/INCA. I'd sell it here and wait to buy on a breakout through the high of day at 40 1/4 or so.



- How to spot the ax using Level 2

● **Main Points:**

In this lesson you will learn how to spot who the "ax" is using a Level 2 screen. The "ax" is the market maker who, at this particular moment (eg for this 3- to 15-minute timeframe) is either buying or selling the most stock. We'll look at how to trade with the ax in the next lesson; this lesson shows you how to spot who the ax is.

- **MM ECN Routing headfake:** MMs will frequently disguise their intentions by routing their orders through INCA or ISLD. See through this ruse by determining how strong the buy/sell action is on the inside bid/ask w/INCA or ISLD...eg if you see the inside ask stay firm w/INCA or ISLD you know some market maker is working a large order and that the situation is "indeterminate" or low-percentage to enter a trade. Wait until a clearer signal is available to enter the trade.
- **Spotting the ax on Level 2:** As we've learned already, **First** always keep an eye on MSCO MLCO SBSH and GSCO; these are your "first picks" to see which of them are the ax at a given point in time. The **second** indicator is the "number of times at best" inside bid/ask AND (more importantly) the refresh rate or 'depth' of their buying or selling when they are at the inside (that's what T&S is for). A third indicator is the "trade box" they are playing, eg where is their bid/ask spread on level 2. A **final** indicator is the # of times they are at the first outside (green) band on level 2. This lesson covers these four areas.
- **Following the MM Axe to Daytrade:** Even with the ECN routing that mm's use to hide their order flow, there's still plenty of profitable trading to be had by correctly: #1) Avoiding buying when a major mm/ax is selling (eg if you see MSCO and MLCO both sitting on the inside ask you probably shouldn't buy if their bid is 3 levels outside the market) and #2) "Shadowing" a the ax's buying/selling behavior, if you see that all else looks okay, eg no suspiciously strong ECN buying/selling on INCA/ISLD.

**Examples:**

## Four Ways to Spot the Ax on Level 2

When the stock is not being moved around primarily by daytraders on ECNs (like DLCK is) or a mm routing order flow through ECNs, consider following one of these four main mms as one of your primary indicators.

Let's study an example of NETA from Thursday, January 6th, where MSCO is the ax.

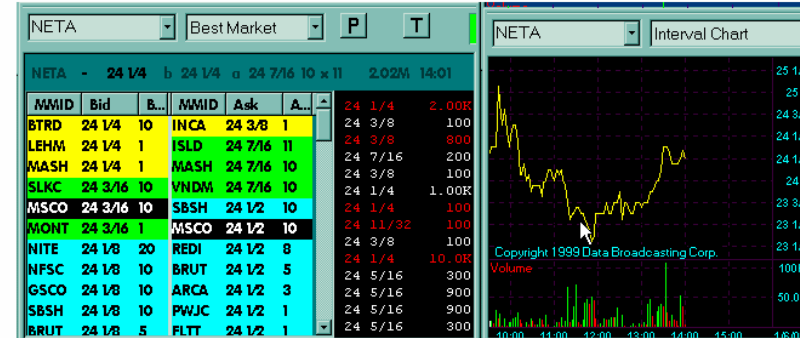
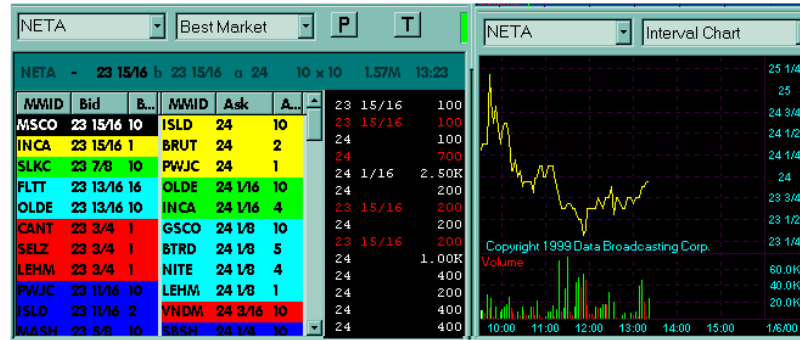
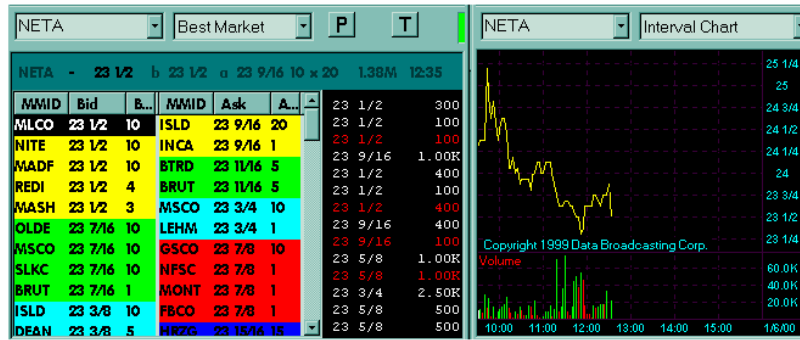
Noticing unusual volume at lunchtime, we see a trend reversal at 12pm...BUY signal generated at 23 1/2 here on volume pivot.

In the first box, I highlighted MLCO, thinking he might be the ax. He dropped out entirely though, leaving MSCO on the bid (2nd).

Third box, we see our initial scalp SELL signal as a volume spike at 24 3/8 followed by a lower high/lower low.

P/L = +7/8 points profit in an hour trade. NETA went on to close at 24 1/2. Nice ride.

MSCO is the ax on this, we saw him stay on the inside (or 1 level outside/green) bid all the way up.



## #2: Number of Times at Best (Inside) Bid/Ask

Ok, now we know who to look for, now let's look at how to interpret their position in the level 2 box.

This indicator is simply looking at the ratio of times the market maker you believe is the 'ax' is buying vs selling stock visibly on the inside bid or ask in a given time period.

Let's say in the box to the right that I've been watching this stock for the last hour or so and SBSH keeps popping up on the inside bid. Further, I see in Time and Sales that he buys at least 5000 shares of stock in 200-1K trade sizes every time he's there.

Sure, he fades to an outside bid level now and then, but overall he's buying and let's say the stock is holding it's own (or even a slight uptrend) in a down market. I'd look to buy the stock when the market starts to head back up if SBSH is still on the inside bid.

Also, as a mental 'checklist' item, at least do not go against one of the four major mm's who is refreshing his bid/ask repeatedly. Example: I don't short SPLS when MSCO is on the inside or green band, as he tends to hold SPLS up, and SPLS has up days whenever he's on the inside (at least the last 6

MMID	Bid	B...	MMID	Ask	A...
SBSHc	27 3/16	10	INCAc	27 1/4	10
GSCOc	27 3/16	10	ISLDc	27 1/4	1
PACSc	27 3/16	1	MONTc	27 1/4	1
ISLDc	27 1/8	9	NITEc	27 5/16	1
SWCOc	27 1/8	1	MADFc	27 3/8	10
NITEc	27 1/8	1	PACSc	27 3/8	1
MASHc	27 1/8	1	DAINc	27 3/8	1
WBLRc	27 1/8	1	SELZc	27 3/8	1
SLKCc	27 1/8	1	LEHMc	27 3/8	1
FBCOc	27 1/8	1	SLKCc	27 3/8	1
BESTc	27	10	SHWDC	27 7/16	10
INCAc	27	4	GKMCc	27 7/16	1
MADFc	27	1	MLCOc	27 1/2	20
GKMCc	27	1	HRZC	27 1/2	18

We look at the Number of Times at Best (some software will calculate/display this for you), to try and determine if this mm is a net buyer or seller.

The caution, of course, is that they may try to appear to be buyers when they're really selling thru INCA or ISLD.

One tip for this: Trade stocks with less skilled market makers on them. In choosing stocks to play, find ones that trade on lower average daily volume (let's



months of '99 to present).

say 700K-2M, \$25-\$40 share price range), as they are likely to have a market maker dividing his attention trading it and 4-5 other issues simultaneously. Headfakes are more common with popular stocks, as the major firms put their best traders on them.

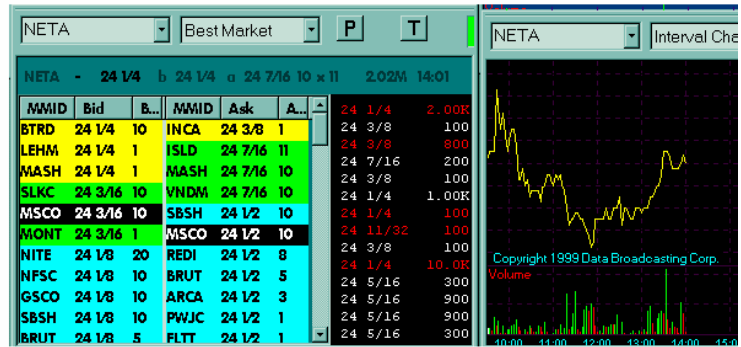
### #3: Market Makers' Trade Box

Looking at our NETA example again, you can see MSCO's "trade box" is:

Bid 24 3/16 x Ask 24 1/2

for the moment. This is a **5-spread trade box**, telling you he's not particularly bullish or bearish on this stock **publicly** (again, watch ECN order flow for disguised order routing).

FYI, trade boxes of 2-5 spreads are common; what you want to watch for is both the **width** of the ax mm's trade box (does he suddenly go from 3 spreads wide to 6?), and the **bid/ask direction** of where he's parking his trade volume. That is, is he 4 spreads wide but on the inside (say at 24 1/4 bid NETA x 24 7/8 ask). This can clue you in as to the direction that this mm thinks the stock will go in.



*Trading note:* having a very intense focus is critical to success in daytrading. Make sure you know the behavior of the "4 major mms" for 3-5 stocks that you follow like the back of your hand. As you know, I like NOVL SPLS DCLK SBUX for daytrading, there are many others out there.

#### #4: Action in the First Outside (Green) Band

The first outside level in your L2 window is important to follow, it's kind of a 'leading indicator' within the micro-world of the L2 box alone. Again, T&S and market / sector direction are the most important indicators, the L2 box is for closely timing your trade entries and exits only (not overall trend determination).

Think of the green band on the bid as your "escape hatch" for and the "wall of sellers to get through" on the ask.

What do the two different examples here (to the right and below) tell you about relative buying and selling in these two stocks, DELL and VRTY?

Can you exit a trade more safely in DELL or VRTY, based on what the L2 green bands alone are telling you?

Answer is DELL of course, you have 7 mms on the green bid, only an ISLD 2 green on VRTY.

DELL		Best Market		P		T		OK	
DELL - 53 9/16 b 53 9/16 a 53 5/8 20 x 30 36.1M 14:55									
MMID	Bid	B...	MMID	Ask	A...				
ISLD	53 9/16	20	ARCA	53 5/8	30	53 9/16	100		
INCA	53 9/16	14	ISLD	53 5/8	30	53 5/8	1.00K		
ARCA	53 9/16	10	NTRD	53 5/8	10	53 5/8	300		
BEST	53 9/16	10	INCA	53 11/16	10	53 9/16	100		
NITE	53 9/16	5	NFSC	53 11/16	10	53 5/8	700		
MWSE	53 1/2	54	NITE	53 11/16	5	53 9/16	300		
SBSH	53 1/2	10	REDI	53 11/16	2	53 9/16	100		
SHWD	53 1/2	10	PIPR	53 11/16	1	53 5/8	1.00K		
RAMS	53 1/2	10	BTRD	53 3/4	214				
DEAN	53 1/2	10	MLCO	53 3/4	22				
MSCO	53 1/2	10	SHWD	53 3/4	10				
MADF	53 1/2	2	WARR	53 3/4	10				
SLKC	53 7/16	10	SBSH	53 3/4	8				
DUP	53 2/8	10	PERT	53 3/4	7				

Daytrading Play w/Green Band on L2: Use it to help you with scalping. I use it to decide if I should stop out of a position if buyers aren't coming in like I thought they would. If the green band starts to evaporate, I'll sell at market bid 2-3 minutes before the stock price starts to drop. Likewise, if the green ask band starts to get thin, then I may enter a new long position in expectation that the price will bounce up 2-3 spreads before settling in, at which point I may scalp out (frequent) or use a trailing stop for a 30-minute to 2-hour trade (10-20% of my trades).



Hopefully, these tips will help you become more comfortable using Level 2 screens correctly. All of these subtleties are necessary to daytrade for a living, yet no website or book I've seen tells you these important tips.

They should all make sense, there is much more to tell you about, let's press on to the next lesson... >>

- Trading with the lead axes: MSCO, GSCO, MLCO, SBSH

● Main Points:

- Now that you've learned 4 ways to "spot the ax" on Level 2, let's look at how to make money daytrading by following the biggest and most powerful axes.
- Trading with the major market makers is a relatively safe way to daytrade, once you know what to look for and how to follow the signals.
- At a minimum, you do not want to be on the wrong side of a trade when up against any of these four mm's when they are selling (or buying) in size, and refresh their bid/ask.
- At best, you can be in front of their order flow and profit from a large order they are currently working.
- When they flip from the bid to the ask you should prepare to exit your trade if you're long.

As the old traders' saying goes, "Some days you're the dog and other days you're the hydrant". Let's try to be on the best side of that by learning how to trade with the right buying and selling pressure generated by the lead mm axes.

Examples:

Play #1: Follow the Lone Wolf

Let us say that you are watching this level 2 SBUX screen. Of the 4 major market makers we'll be shadowing, which one appears here on the inside bid or ask?

Ok answer is: GSCO, bid size 10 at 27 5/8. On the time and sales you see a lot of selling going on, and GSCO is buying.

How can you trade with this? First of all, consider all danger signals: eg there's a pretty high number of sellers on instinet (INCA size 44), it could be a number of players in that pool of 44, we need to watch the tape to see if the 44 shrinks to less than 10 quickly (bullish), or stays strong. Remember a mm like MLCO or SBSH or whoever could be routing a big sell order thru INCA. The tape tells us what we need to know, for now there is a larger ratio of sell orders to buy orders on the tape, and no big blocks (12

MMID	Bid	B.	MMID	Ask	A.		
SBUX	27 5/8	10	INCA	27 11/16	44	27 5/8	600
GSCO	27 5/8	10	ISLD	27 11/16	17	27 5/8	100
FBCO	27 5/8	6	NITE	27 11/16	1	27 5/8	600
BRUT	27 5/8	6	DBKS	27 3/4	10	27 11/16	500
STRK	27 5/8	5	SELZ	27 3/4	1	27 11/16	1,500
NITE	27 9/16	1	DEAN	27 3/4	1	27 5/8	100
SHWD	27 9/16	1	SHWD	27 3/4	1	27 5/8	800
FLTT	27 9/16	1	MONT	27 3/4	1	27 5/8	100
MADF	27 9/16	1	SBSH	27 13/16	10	27 5/8	200
INCA	27 1/2	10	MLCO	27 13/16	10	27 5/8	300
SBSH	27 1/2	5	LEHM	27 13/16	1	27 5/8	100
MONT	27 1/2	1	JPMS	27 13/16	1	27 11/16	500
JPMS	27 1/2	1	MWSE	27 7/8	14	27 11/16	100
CANT	27 7/16	1	OLDE	27 7/8	10	27 5/8	300
WBLR	27 7/16	1	MSCO	27 7/8	10	27 5/8	300
DBKS	27 3/8	10				27 11/16	1,000

**Daytraders' Play:** Let's assume you've been watching for awhile and you see GSCO has been at the inside bid (yellow) and is "holding up" the stock price at 27 1/2 to 27 5/8, giving it support.

Even when a wave of sellers comes in (that you can see on T&S), the price momentum doesn't weaken, and the stock is recovering (you see from Level 2 that the buyers aren't backing away, the color bands aren't getting thinner etc.). GSCO stays a buyer more than 70% of the time. He's not flipping over to the ask much at all, and seems to be holding the stock up. You also see here that GSCO's "trade box" is bullish, he isn't even posting an ask 3-4 spreads up (unless he's faking via an ecn). Also, you don't see any of the other 3 heavyweights selling openly at the ask: no MLCO SBSH MSCO.

selling at the bid, 5 paying the ask). Still, so what.

GSCO will not make his intentions overly obvious, but your "feel" of the situation is that he is a buyer of the stock today and is stronger than the sellers at this particular point in time. So, you would buy stock where GSCO is, say enter a limit buy 1100 shares at 27 5/8, or, if the sellers at 27 11/16 start to quickly disappear you enter a limit buy at the retail ask price of 27 11/16 to get some.

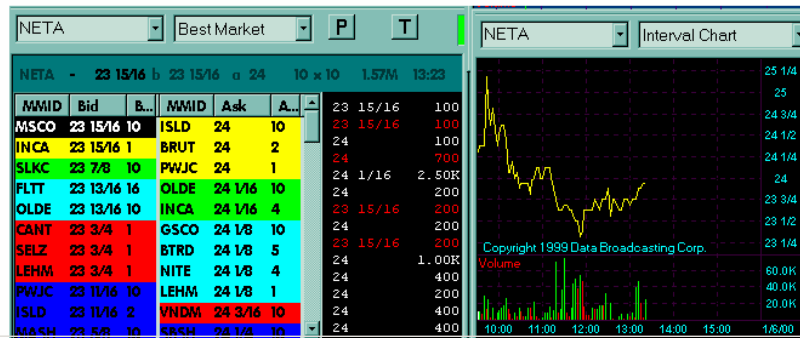
When the stock price rolls up a spread to read 27 11/16 x 27 3/4, watch GSCO. If he stays at 27 5/8 or better after the price goes up a spread, you're in a winning trade. Trail stops 1/4 point down to lock in profit, and sell when you see GSCO drop his bid by more than a spread, or when he flips over to the sell side.

## Play #2: Samson and Goliath: MM ax vs. weak hands

**Here's our NETA example with MSCO.** Now, lets just consider the 4 major mm's MSCO MLCO SBSH GSCO. Who is MSCO trading against? Nobody, unless someone's selling a bunch through ISLD (unlikely). BRUT and PWJC are small potatoes relative to MSCO.

The next "strong player" is GSCO at 24 1/8. So, your trade is relatively safe here, especially with volume reversal breakout confirmation on your 1-minute chart at right, and many trades going off at 24, the ask, in T&S.

What do you do to buy ahead of MSCO without paying up the spread? You can either enter a larger order than the best bid, eg bid 1100 23 15/16, or split the spread and bid 23 3 1/32 (though if you're only trading 500 shares that's just \$15, probably not worth haggling over).



**Daytraders' Play:** Anytime you see a battle between one of the "big 4": MSCO MLCO SBSH GSCO against an ECN order or chippies, you should probably start by assuming one of the big 4 will win, at least for a couple spreads' worth of price movement. Watch the T&S to confirm buying/selling direction, and be ready to exit if the mm flips over from bid to ask or vice versa. MLCO seems to flip the most, in the stocks I play. SBSH and GSCO seem to be the most consistent of the 4, they don't seem to flip around as often.

Make sure to define your entry and exit strategy before trading as always, eg for a "I'm going to follow MSCO trade at 23 15/16 buy the bounce play" you might say to yourself "I'll have to be careful as it gets over 24, the high of the day is 25ish so I'll plan on scalping it and selling when T&S starts to reverse, I'm expecting to exit somewhere around 24 1/2."

So, you buy 1100 shares at 23 15/16, immediately offer it out at 24 1/8 to frontrun GSCO if you're scalping, or, sit on it and sell as your T&S shows other sellers coming in strong. Again, based on what MSCO is doing, if he is holding it up and raises his bid as the price moves up I'd be less inclined to sell. If he immediately flips over to the ask, or if T&S shows lots of people hitting the current bid, then you should exit the trade as well. Easy, right?

## Play #3: Dueling Daytraders :o

Some stocks are heavily traded by daytraders, who have a stronger impact on the price momentum of the stock. Many internet stocks like DCLK and AMZN fall into this category, so you need to know how to play these as well.

Daytraders frequently route through ECNs like ISLD/INCA/ATTN/ARCA etc and so you see a ton of trades going on here. **You do not try to follow the ax in stocks that have most of their orders going through on ECNs**, nor through stocks that have very thin bid/ask levels (eg frequently only have 1-2 market participants at each level). Why not? Well, it's a pointless strategy to follow one of the big 4 if 80% of the trading is being routed through ECNs, right? In the example to the right, let's see, you've got MLCO offering 3 spreads up, MASH (an "almost-big" mm), with a 2 size two spreads down, nothing in other words you can follow in the area of a mm ax to trade with. It's an ECN play.

So, you need to follow trade using the crowd direction in these stocks even more so. Typically, these stocks sell off faster than others do, so are good "bottom bounce" play candidates or short candidates. They sell off faster because you have more panicked daytraders playing them, and we exit at the first hint of price weakness in our stocks.

M...	Bid	B...	M...	Ask	A...		
AMZN	91 7/8	10	92	10 x 27	10.5M	14:50	
INCA	91 7/8	10	ISLD	92	22	92	100
MWSE	91 7/8	1	ARCA	92	12	92	100
ISLD	91 13/16	6	MASH	92	10	92	100
MASH	91 3/4	2	BRUT	92	6	92	400
NFSC	91 3/4	1	INCA	92 1/16	10	92	900
MADF	91 3/4	1	DKNY	92 1/16	1	92	100
REDI	91 9/16	5	REDI	92 1/8	2	92	100
SELZ	91 9/16	1	MLCO	92 1/4	9	91 15/16	600
JPMS	91 1/2	1	MWSE	92 1/4	5	91 15/16	100
COWN	91 1/2	1	SLKC	92 1/4	1	92	100
SLKC	91 7/16	1	MONT	92 1/4	1	91 15/16	100
MSCO	91 1/8	10	NITE	92 1/2	20	92	100
STBK	91 1/8	5	MADF	92 1/2	11	91 63/64	600

**Daytraders' Play:** T&S looks bullish, L2 looks bearish (why, traders?). Indeterminate; I wouldn't know whether to buy or sell until I saw the tape in action and could see the day's chart and other market indicators (like the \$GIN first, then the naz \$COMPQ chart, then \$TRINQ/\$TICK etc).

For now, it's a "sit on the sidelines and watch" stock, based on what I see here. That's ok, I spend most of the time watching, waiting for an opportune moment, then bang I fire off the order, watch it go in my favor a spread or 2 or 5, then sell. Or, if it weakens then I'm outta there fast, and get ready to "try again".

#### NOTES on Following the big 4: MLCO SBSH MSCO GSCO

1. You are always looking for "lopsided" high-percentage situations to trade in. Many new traders overtrade, making for rich brokers and broke traders. Use a sensitive, practiced eye to see what the behavior of a major market maker is in the stock you are following.
2. All the same daytrading guidelines apply, eg dont go long during lunch, use small stops, try to stay ahead of the crowd by using your charts and T&S patterns to verify entry and exit points.
3. I have found it extremely helpful to identify the major market makers in my particular stock, using the [www.nasdaqtrader.com](http://www.nasdaqtrader.com) link (see front page [www.trainingaloha.com](http://www.trainingaloha.com) link for "Identify the naz ax").
4. Once I have narrowed it down to whichever one is playing my stock the most that day, I will look for high-opportunity profitable times to play the stock, such as the 10:30 naz bounce on a down day.
5. Recognizing net buying vs. selling is a fairly difficult skill to master, at least as hard as learning how to play Monopoly. So spend at least as much time, 3-4 concentrated hours on a single stock, to try and identify net buying and selling using your level 2 screen and t&s for the market maker you believe is the ax. It may take a few times to correctly identify who's moving the stock. In fact, it will probably take you a number of weeks to begin to get good at it. That's ok, it's not an easy skill to master. But master it you must if you are to do this for a living.

#### Notes On Daytrading:

I don't sugarcoat daytrading or spout vague warnings about risk management. I'm preparing you to succeed at this, by telling you the things other people do not. It is a job, and it takes work. The good thing about This particular job is that you can make a lot of wealth by doing it correctly.

But, it takes more work than most are willing to put in, so they "dabble", get lucky now and then, and end up leaving the casino broke. To succeed at daytrading, you must be willing to work exceptionally hard, and master many new skills. Look at it like a degree program, and prepare yourself as professionals do. Read the market maker info on the Workstation 2 page links (the pdf files).

Realize what you're into here. You set your own odds in this casino, and every one of the skills you master at DTU should help you become more effective at learning how to daytrade for a living. I am giving you more advanced information than any other daytrading seminar/book other resource provides (that I'm aware of), because it is what is needed to honestly, realistically succeed at this.

My role here is to be a coach and an armorer, giving you the defensive and offensive trading weapons, skills and signals you need to stay ahead in this game. It does take hard work, but at least you can really be free of a day job, live anywhere you want, and have what you want if you succeed at this.

- When to enter and exit trades based on Level 2 signals

● **Main Points:**

- In addition to providing insight regarding market maker activity in a stock, Level 2 should be used to help you time your "scalp" trade entries and exits.
- It is worth mentioning again that you should **Not use Level 2 alone** for your trading decisions, as it can give false impressions of support and resistance; use Level 2 along with Time & Sales, 1-minute charts and general market (or sector) direction to make trade decisions.
- Level 2 is **more useful for trading some stocks than it is for other stocks**. For example, I find Level 2 not useful at all for trading WCOM, AMZN and INTC, but very useful for stocks like CIEN CMCSK and NOVL. Factors to look at are: how 'transparent' are the lead mm's axes in the level 2 box for the specific stock; the ratio of how many mms vs ECN orders are represented on the Level 2 (eg the higher the ratio of ECN orders to mm orders the less useful L2 is; example: eg DCLK heavily traded on ECNs so L2 not as useful).
- This lesson is designed to help you develop two additional Level 2 daytrading skills: a) knowing **how to time** your trade entries in Level 2, and b) identifying "high-potential" trading opportunities that can only be seen in a Level 2 screen.

**Timing Your Trade Entries/Exits Using Level 2**

**Timing Your Trade Entries/Exits Using Level 2**

**Examples:**

**Situations to avoid buying into:**

As we mentioned previously, the "tape is king", not level 2 bands, however we can at least identify danger signs on Level 2 to avoid buying into.

#1) "Wall of Sellers at the Inside" - common sense, if you have many sellers to go through and you're buying long this is a no-no. Conversely, this is a terrific short opportunity (if you can get an uptick).

MMID	Bid	B..	MMID	Ask	A..	Volume
DLJP	21 7/16	10	MASH	21 1/2	107	1.00K
INCA	21 3/8	10	BRUT	21 1/2	53	2.00K
WETH	21 3/8	10	NITE	21 1/2	22	500
ARCA	21 3/8	10	INCA	21 1/2	15	1.00K
MASH	21 3/8	8	MADF	21 1/2	15	200
SHWD	21 3/8	5	WPCO	21 1/2	10	200
ISLD	21 3/8	2	HRZG	21 1/2	10	1.00K
BTRD	21 3/8	1	SBSH	21 1/2	10	100
WPCO	21 5/16	10	GSCO	21 1/2	10	100
REDI	21 1/4	25	PERT	21 1/2	8	700
NITE	21 1/4	22	MWSE	21 1/2	6	700
SBSH	21 1/4	10	PRUS	21 1/2	5	1.60K
BRUT	21 1/4	2	FLTT	21 1/2	3	400
SLKC	21 1/4	1	ISLD	21 1/2	2	300

#2) **Indeterminate/low-percentage level 2:** If your t&s and charts are not giving you a clear direction and L2 has an approximately equal number of buyers/sellers (or within 10% of being equal), avoid entering a trade.

Again, you only want to enter daytrades on "high-percentage opportunities", not guesses.

M..	Bid	B..	M..	Ask	A..	Volume
INCA	91 7/8	10	ISLD	92	22	200
MWSE	91 7/8	1	ARCA	92	12	100
ISLD	91 13/16	6	MASH	92	10	100
MASH	91 3/4	2	BRUT	92	6	100
NFSC	91 3/4	1	INCA	92 1/16	10	400
MADF	91 3/4	1	DKNY	92 1/16	1	900
REDI	91 9/16	5	REDI	92 1/8	2	100
SELZ	91 9/16	1	MLCO	92 1/4	9	100
JRMS	91 1/2	1	MWSE	92 1/4	5	600
COWN	91 1/2	1	SLKC	92 1/4	1	100
SLKC	91 7/16	1	MONT	92 1/4	1	100
MSCO	91 1/8	10	NITE	92 1/2	20	100
KTRK	91 1/8	5	MADF	92 1/2	11	200

**Keys to Success in Timing Level 2 Trades:**

**Daytrader Timing Plays:** Regular ho-hum trading with Level 2: let's look at the mechanics of using it correctly to time entries and exits

**Timing your Entries:** Again there's two times you want to buy: on breakouts and on strong bottom bounces. You see those two on your one-minute charts.

Timing entries with level 2 - here's some tips I've found helpful:

1. **The inside bid/ask ratio of market makers and ECNs is important for timing** when you buy or initiate a short. Having one or more of the 4 heavyweight mm's (MSCO MLCO SBSH GSCO) on the inside is a "strong hand" vs. ECNs only. In this example, you see both SBSH and GSCO on the bid with only ECNs (ISLD/INCA) and a weak mm bid (MONT at 1) on the ask. This is very bullish.

(Unless, of course, T&S is telling you differently due to mm's disquising orders via ecn routing; eg if you see 30 orders go through at 27 1/4 and INCA doesn't weaken, then there's a strong seller, another red flag).

**Timing your Exits:** When should you offer stock out at the ask, or even hit the bid to liquidate? Let's look at some timing indicators. The top L2 NOVL window would tell you to sell at 27 7/16 if you could, if you were in from earlier, as it's highly unlikely that all the sellers will liquidate their stock at 27 1/2, so the price may drop 1-3 spreads, shrinking your profit.

Again, use level 2 in moderately/ slow-paced stocks to buy at the offer, sell at the ask whenever possible, so you're not giving up 2 spreads of profit every time you buy and sell. Only pay retail when the stock is moving against you quickly, and the speed is most important. (in which case you might even want to preference an outside-of-the-market mm at a lower bid price so you may be able to exit).

In general, exit when T&S tells you that there's more sellers than buyers. Look for these confirmation signals on Level 2:

1) **The number of market participants** (both mms and ECNs) **starts to shrink** on a) the inside bid and b) the green band (first outside bid

MMID	Bid	B...	MMID	Ask	A...
SBSHc	27 3/16	10	INCAc	27 1/4	10
GSCOc	27 3/16	10	ISLDc	27 1/4	1
PACSc	27 3/16	1	MONTc	27 1/4	1
ISLDc	27 1/8	9	NITEc	27 5/16	1
SWCOc	27 1/8	1	MADFc	27 3/8	10
NITEc	27 1/8	1	PACSc	27 3/8	1
MASHc	27 1/8	1	DAINc	27 3/8	1
WBLRc	27 1/8	1	SELZc	27 3/8	1
SLKc	27 1/8	1	LEHMc	27 3/8	1
FBCOc	27 1/8	1	SLKc	27 3/8	1
BESTc	27	10	SHWDc	27 7/16	10
INCAc	27	4	GKMCc	27 7/16	1
MADFc	27	1	MLCOc	27 1/2	20
GKMCc	27	1	HRZGc	27 1/2	18

2. **Buying when the lead seller is done selling for now.** Let's say some traders are selling via INCA, and INCA now disappears off your inside ask, leaving just ISLD and MONT. This is a good time to buy stock, **but you must be fast**, as the ISLD and MONT sellers will try to pull their offers to sell as well. Here's an example of where a SOES buy to MONT would be a good way to take his stock before he can respond. haha, then the next thing you know the stock is trading 27 5/16 x 27 3/8 (the next major "hurdle" for buyers to overcome); and if SBSH/GSCO and others join the bid, making the yellow inside bid width look good, you've got a winner. Set your stop initially at where you bought in, and trail your stop up, exiting with 1/4 - 5/8 profit.

MMID	Bid	B...	MMID	Ask	A...		
GSCO	27 5/8	10	INCA	27 11/16	44	27 5/8	600
FBCO	27 5/8	10	ISLD	27 11/16	17	27 5/8	100
BRUT	27 5/8	6	NITE	27 11/16	1	27 5/8	600
STRK	27 5/8	5	DBKS	27 3/4	10	27 11/16	500
NITE	27 9/16	1	SELZ	27 3/4	1	27 11/16	1.50R
SHWD	27 9/16	1	DEAN	27 3/4	1	27 5/8	100
FLTT	27 9/16	1	SHWD	27 3/4	1	27 5/8	800
MADFc	27 9/16	1	MONT	27 3/4	1	27 5/8	100
INCA	27 1/2	10	SBSH	27 13/16	10	27 5/8	200
SBSH	27 1/2	5	MLCO	27 13/16	10	27 5/8	300
MONT	27 1/2	1	LEHM	27 13/16	1	27 5/8	100
JPMS	27 1/2	1	JPMS	27 13/16	1	27 11/16	500
CANT	27 7/16	1	MWSE	27 7/8	14	27 11/16	100
WBLR	27 7/16	1	OLDE	27 7/8	10	27 5/8	300
DBKS	27 3/8	10	MSCO	27 7/8	10	27 5/8	300
						27 11/16	1.00R

2) **The quantity of the lead bidders' size starts to shrink:** eg if GSCO's 10 turns into a 6 or a 1 then he's going to disappear; if he's really buying then his 10 would've stayed the same through multiple sellers as seen on t&s, as he refreshes for the tier size.

3) **A "wall of sellers" starts to build,** for example if you see either the number of mm's increase by 2-3 in either the yellow or green ask column, you should get out for now. Remember, you can always buy back in later when it looks safe.

level). Use the green band's # of participants as a leading indicator. Example: if (for the SBUX L2 window) both BRUT and STRK disappear and show up down at 27 1/2.



Always remember: **When in Doubt, Get OUT!** Shakes notwithstanding, you can always re-enter your position at maybe 1/16th or so higher if you were wrong and it was going your way. I frequently find myself getting out a "bit sooner" than the crowd does, before the stock drops 1/4 point or more...it's an instinct that says "nah, they're not buying anymore, it's "iffy", I'm outta there."

4) **You see the "ax" or other major mm flip from the bid to the ask.** Example: if GSCO jumps over to the yellow ask and 2 more people join him at the bid, you should hit the bid at 27 5/8 and get outta there now.

## Identifying High-Potential Daytrades using Level 2

Remember to use Level 2 as a **secondary** decision support tool to help you time exact entries and exits to within 1/16th; it's a "microscope".

Don't use Level 2 alone to decide whether or not to buy or sell stock, but rather **when** (within a 2-minute timeframe) to buy or sell, after making your initial decision using T&S, 1-minute chart and overall market (or sector) strength and direction. Many traders misuse level 2.

### Daytrader High-potential Play #1 - The "Rollup":

IF the stock is "breaking out" of a trading range, making a new high, trading actively in one direction, or making a bounce off a hard selloff.

It's usually safe to buy if t&s shows all buyers and you're one of the last ones to buy right before an ask price level disappears off the L2.

**How it Works:** Lets say this NETA used to have 4 sellers at 24 3/8, and now traders have bought so much that there's only the instinet (INCA) seller left, showing an ask size of one or so. If you're fast, you can "jump on board the last train at the spread" and buy from INCA before the L2 inside goes up a spread (to 24 3/8 bid, 24 7/16 ask). If you time these right, they are usually good for a fast 1-3 spreads profit. (For active traders with daytrading brokers only-type play.)

(As I mentioned before, for moderate or slow-paced stocks you always want to buy at the bid, sell at the ask, this tip is for fast moving stocks).

NETA - 24 1/4 b 2 Last seller on inside ask about to disappear, buy it and watch the price continue up 1-3 spreads.

MMID	Bid	B	MMID	Ask	A	Price	Quantity
BTRD	24 1/4	10	INCA	24 3/8	1	24 1/4	2,000
LEHM	24 1/4	1	RELI	24 7/16	1	24 3/8	100
MASH	24 1/4	1	MASH	24 7/16	10	24 3/8	800
SLKC	24 3/16	10	VNDM	24 7/16	10	24 7/16	200
MSCO	24 3/16	10	SBSH	24 1/2	10	24 3/8	100
MONT	24 3/16	1	MSCO	24 1/2	10	24 1/4	1,000
NITE	24 1/8	20	REDI	24 1/2	8	24 1/4	100
NFSC	24 1/8	10	BRUT	24 1/2	5	24 3/8	100
GSCO	24 1/8	10	ARCA	24 1/2	3	24 1/4	10,000
SBSH	24 1/8	10	PWJC	24 1/2	1	24 5/16	300
BRUT	24 1/8	5	FLTT	24 1/2	1	24 5/16	900



This usually works when you're buying ahead of a major support level (usually at 1/4 1/2 3/4 and whole numbers) that has a lot of people bidding for the stock.

In the QWST example to the right you see a wall of buyers at 34 1/2. Thus, making a bid at 34 9/16 (or 34 19/32 to frontrun DLJP haha) is probably smart.

*Secret to Scalping w/Support in Level 2 Daytrading:*

When I scalp, (most of my trades are scalps within a 20-minute roundtrip) I will use Level 2 walls of support at the first outside bid (green band) to set my stop.

For example, if I buy at 34 9/16, I would trade this as follows: my stop is at "I'll sell if the wall of buyers at 34 1/2 is almost gone". In other words, if I bought at 34 9/16 and it trades down, the inside now becomes 34 1/2 x 34 9/16 and then the green (now yellow) wall of bidders shrinks down to say 4-5 bidders from it's current 17 then I'll get nervous and probably hit the bid.

This is because the stock didn't do what I thought it would, namely bounce off the 34 1/2 support and climb higher, to a next resistance of 35. Make sense?

So, my downside is maybe 1/8th of a point. My target is 7/8, or about a 3/8 profit. I'll be smart enough to exit the trade into the buying strength, before it reaches 15/16 and fades back to 3/4.

So, my downside is maybe 1/8th of a point. My target is 7/8, or about a 3/8 profit. I'll be smart enough to exit the trade into the buying strength, before it reaches 15/16 and fades back to 3/4.

Of course, if volume picks up a lot then it may continue on strongly through whole number resistance, but I don't bet on it. Remember, you can always buy back in later. So, I'll buy here, sell up at 7/8, wait for a shake off 35, then buy back in at 35 1/8, if it goes up there. That's how to daytrade, folks.

Ok, time to practice: try papertrading with the above tips; perhaps print this page or summarize the main points and see how it works for the stocks you trade. Remember to keep an eye on the ratio of mm's to ECN's on the inside bid/ask as a key indicator, and that Level 2 is much less useful for stocks that do most of their trading through ECNs.

Level 2 is a secondary indicator to use for scalping and precision timing for entries and exits, not a major decision support tool as to whether you should be buying or selling the stock in the first place.

MMID	Bid	B...	MMID	Ask	A...
DLJP	34 9/16	10	INCA	34 5/8	89
REDI	34 1/2	136	BTRD	34 5/8	11
ISLD	34 1/2	61	SBSH	34 5/8	10
BTRD	34 1/2	50	MONT	34 5/8	10
BRUT	34 1/2	28	NITE	34 11/16	20
INCA	34 1/2	23	REDI	34 11/16	17
MADF	34 1/2	22	ARCA	34 11/16	10
MILCO	34 1/2	20	SLKC	34 3/4	1
VWSE	34 1/2	11	PRUS	34 13/16	1
NITE	34 1/2	10	PLTT	34 13/16	1
GSCO	34 1/2	10	MSCO	34 7/8	10
DEAN	34 1/2	8	GSCO	34 7/8	10
BEST	34 1/2	7	KCOM	34 7/8	1
HRZG	34 1/2	6	JRMS	34 7/8	1
PERT	34 1/2	2	FBCO	34 15/16	1
SHWD	34 1/2	1	PERT	35	20
PRUS	34 1/2	1	ISLD	35	11
WARR	34 1/2	1	HRZG	35	10



- Using TA and 3-minute charts with Level 2: the big picture

**Main Points:**

- Level 2 is critical for successfully timing precise trade entries and exits, and for following the ax for stocks that have an identifiable 'ax'.
- I have found that using a combination of level 2, 1-minute bar/close line and 5-day 13-minute charts gives me an effective edge in daytrading. As we've learned, you should take a "funnel" approach to daytrading, paying attention to the overall market/sector direction first, followed by the individual stock's intraday price action and technical indicators, saving level 2 for last to get your "within 3-minute" timing down for when exactly to fire off a buy/sell.
- This lesson will focus on how to use the powerful combination of multiple indicators to assist you in making your trade decisions. Note that for Scalping (under 3-10 minute roundtrips) the Level 2, especially T&S, becomes more important than the charts are; charts are important to determine breakouts and bottom bounces for daytrades that last from 10 minutes to an hour (or even longer). Remember that L2 alone is not sufficient (eg it's particularly useless for the most actives like WCOM, MSFT and INTC).
- New daytraders are advised to maintain positions for from 5 minutes to 2 hours max; intermediate/advanced daytraders should trade from 10 second - 20 minute roundtrip trades. Swing traders that are becoming daytraders are advised to start with overnight holds that are sold premarket or within the first 15-30 minutes of market open. This will help you tighten your trading range down to a faster style. Notice that many profitable opportunities can be had with overnight holds that are sold into the premarket gap up using level 2; the key is to sell on ISLD if it's within a spread or two of the best bid, but hold off for the actual open to sell if Level 2 shows ISLD 3 or more spreads away from the best bid, since you can sell to one of the mm's at their bid if they don't drop it immediately on open.

**Examples:**

**The DTU "Triple Play" Daytrading L2 Setup:**



**Level 2/T&S**

**1-minute  
Intraday**

**13-minute  
5 Day**

- And even then, I wouldn't be too sure about this particular stock continuing up...I'd wait and see what SBSH does. **Note that it's come up to half of its' trading range on the 1-minute chart, so don't buy when a stock is here. NEVER buy a stock that's bounced off the bottom and has come back up to half the range**, the play is probably over and it will just chop around here for awhile. Wait for either a bounce off the bottom again (2nd bottom), a breakthrough (above the day's high), or a breakdown to short (below the previous bottom.). Learn this.

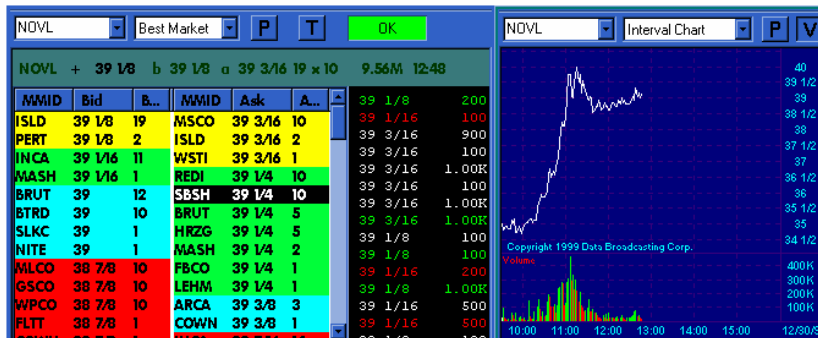
**Consider setting up a similar "triple play" for your stocks;** of the three parts the 5-day chart is the most "optional" part of it, as long as you know where the stocks' coming from and have made a note of the support/resistance levels you may leave this one out of the equation, if screen space is limited.

At a minimum, make sure you have this type of setup available to daytrade with: a level 2 window, time & sales, and a 1-minute intraday chart. The 5-day is used to help determine how strong the likelihood is of a bounce or a breakout, the 1-day chart doesn't give the perspective that I like to have.

For example, NOVL ran up from 20ish to 40 in a matter of days; it was a prime short candidate right here (Why? Making a lower high on lower volume after running up 5 points, plus SBSH, the usual ax on NOVL, is a seller, and there's a "wall of sellers" on the L2 ask. Good for 2 1/2 points in 40 minutes.

I wouldn't have known that if I didn't also have the 5-day chart available, if for instance NOVL had just dropped on bad earnings from 62 to 35 on the open then I would not be nearly as likely to short it. The 5-day perspective has been consistently profitable for me.

Knowing where your stock is coming from gives you a pretty good indicator of where it is likely to head over the next couple of days, in addition to intraday scalping and swing trades. This edge will help. It also helps you to set your stops; as I say I recommend 2-3 spread stops in general, at a maximum you would use decade support/resistance and 5-day support/resistance levels to help you with your trades.



**A Final Reminder;** Use Level 2 in conjunction with a "market snapshot" to help you nail your pivot points and trades effectively. Below (again) is a "market snapshot" I use to keep an eye on the direction of the overall market.

**I do not fight the market - the market is always right.** I don't care what Level 2 says, if the market is overall tanking I will not go long a stock, unless there is breaking news (almost never). If the market is "indeterminate" than I will not enter a trade. I enter if the market is ok, and the stock is making a pattern I recognize as a "high-potential" daytrade, as we have seen in the earlier lessons on bullish/bearish chart patterns.

Ok traders, lets take a look what are these indicators telling us?

Lunchtime is about over, overall trend of the market is down, we're under the opening, fairly choppy.

The bounce seems to be moderately strong here, as the composite trend has reversed above the previous high at around 4066.

**Pop Quiz:**

#1) Do you trade semis (\$SOX) or nets (\$GIN), based on their composite charts to the right? (answer: semis are stronger overall, because when they bounced in the morning at 10am they bounced higher than the nets did.)

#2) What does the last 5 minutes of the \$TRINQ chart at the right tell you?

a) it's bearish for stocks, stocks are dropping

b) it's bullish for stocks, stocks are rising

(answer: the \$TRINQ is an inverse indicator, I'd be ready to buy stocks since a drop in the \$TRINQ like this is b) a bullish indicator)



Answer to using 13-minute charts: Knowing that the majority of new traders use 15-minute charts, I can get a 2-minute head start on the competition to see subtle changes in pivots, reversals and breakouts faster by moving to a 13-minute chart.

# Reading the Tape: Using Time & Sales Successfully



## The Tape 101: What is time and sales? What's it used for?

Edison invented the original stock ticker a long time ago (his first big commercial success). Its' purpose remains unchanged to this day: it simply shows the transactions that occur whenever stock is bought or sold. Transactions are "printed" one after another in the order they happen, in realtime. The "tape" of yesteryear is replaced by realtime Time and Sales (T&S) electronic displays in that show us whenever a trade has occurred.

Using T&S, we see both the time that the trade occurred as well as how many shares changed hands. So, it might read 10:33 AMZN 500, telling us that someone bought 500 shares of Amazon at 10:33am. The next trade may be 10:34 AMZN 200, showing us the next trade in order was for 200 shares a minute later, at 10:34. And so on throughout the trading day.

We use it to see if trades occur repeatedly at the ask price (a bullish, uptrending sign showing buying) or the bid price (a bearish, downtrending sign showing selling). We also look for other indicators, like the **size of the trades occurring** (10K - 50K blocks of trades are more important than 100-share trades by individuals), as well as the **momentum, or pace** of how fast the trades occur in Time and Sales (this often speeds up when major pivots, or turning points, occur in the stock price).

## Bullish Time & Sales: Going Up!

MMID	Bid	B...	MMID	Ask	A...	
AMZN	73 13/16	b	73 13/16	a	73 7/8	10 x 3
MSCO	73 13/16	10	INCA	73 7/8	3	
PERT	73 13/16	8	REDI	73 7/8	1	
MLCO	73 13/16	1	ARCA	73 7/8	1	
HMQT	73 13/16	1	ISLD	73 15/16	5	
BRUT	73 13/16	1	NFSC	73 15/16	1	
ISLD	73 3/4	10	SLKC	73 15/16	1	
MWSE	73 3/4	5	BRUT	74	1	
SHWD	73 3/4	1	BTRD	74	1	
MONT	73 3/4	1	WEED	74	1	
BTRD	73 11/16	1	JPMS	74 1/8	1	
REDI	73 11/16	1	MWSE	74 1/4	1	
INCA	73 5/8	10	LEHM	74 1/4	1	

### Bullish T&S Signals:

- In this AMZN chart you can see a **string of trades going off at the ask**, 73 7/8. This tells you that other traders believe the price will go up and they want to "get on board" at 73 7/8 before it runs up higher.
- If the majority of trades occur at the inside ask, the "trading sentiment" for the stock is bullish for that particular moment.

## Bullish Time & Sales: Going Up!

MMID	Bid	B...	MMID	Ask	A...	
AMZN	73 13/16	b	73 13/16	a	73 7/8	10 x 3
MSCO	73 13/16	10	INCA	73 7/8	3	
PERT	73 13/16	8	REDI	73 7/8	1	
MLCO	73 13/16	1	ARCA	73 7/8	1	
HMQT	73 13/16	1	ISLD	73 15/16	5	
BRUT	73 13/16	1	NFSC	73 15/16	1	
ISLD	73 3/4	10	SLKC	73 15/16	1	
MWSE	73 3/4	5	BRUT	74	1	
SHWD	73 3/4	1	BTRD	74	1	
MONT	73 3/4	1	WEED	74	1	
BTRD	73 11/16	1	JPMS	74 1/8	1	
REDI	73 11/16	1	MWSE	74 1/4	1	
INCA	73 5/8	10	LEHM	74 1/4	1	

### Bullish T&S Signals:

- In this AMZN chart you can see a **string of trades going off at the ask**, 73 7/8. This tells you that other traders believe the price will go up and they want to "get on board" at 73 7/8 before it runs up higher.
- If the majority of trades occur at the inside ask, the "trading sentiment" for the stock is bullish for that particular moment.

- In this DBCC chart you can see a **string of trades going off at the bid**, 10 3/4. This tells you that other traders believe the price will go down and they want to dump it fast.
- Even though MWSE is showing a size 50 bid, pay attention to the T&S instead; everyone is selling, so MWSE will probably stop buying soon.
- Play this the same way you'd play any pattern once you see it, either enter a bid at 5/8 if you think that's where it will bottom (risky), or try to short it on an uptick if you think it'll continue down.

MMID	Bid	B...	MMID	Ask	A...		
MWSE	10 3/4	50	SHWD	10 13/16	15		10 3/4 1.00K
MASH	10 5/8	5	ISLD	10 13/16	10		10 3/4 800
INCA	10 5/8	2	FACT	10 13/16	1		10 3/4 100
ARCA	10 5/8	2	BRUT	10 7/8	12		10 3/4 800
FACT	10 9/16	9	FLTT	10 7/8	1		10 3/4 100
FLTT	10 9/16	1	SLKC	10 7/8	1		10 3/4 200
PRUS	10 1/2	10	HDLY	11	15		10 3/4 100
SHWD	10 1/2	5	JPMS	11	1		10 3/4 100
MLCO	10 1/2	2	HRZG	11	1		10 3/4 300
BEST	10 1/2	1	PWJC	11	1		10 3/4 200
							10 11/16 1.00K
							10 11/16 100

MMID	Bid	B...	MMID	Ask	A...		
STRK	90 1/4	5	ISLD	90 5/16	10		90 1/4 500
SBSH	90 1/4	4	BTRD	90 3/16	9		90 1/4 100
NEUB	90 1/8	20	MONT	90 3/8	1		90 1/4 400
GSCO	90 1/8	5	INCA	90 7/16	10		90 1/4 9.60K
MWSE	90 1/8	2	PERT	90 1/2	2		90 1/8 1.00K
ISLD	90 1/8	1	MASH	90 1/2	2		90 1/8 500
NITE	90 1/16	1	SLKC	90 1/2	1		90 1/4 900
SLKC	90 1/16	1	MLCO	90 1/2	1		90 1/4 1.10K
BRUT	90	11	HRZG	90 11/16	1		90 1/4 500
BEST	90	10	FBCO	90 3/4	1		90 1/4 500
MLCO	90	5	GSCO	90 7/8	5		90 1/4 400
PERT	90	4	ARCA	91	5		90 1/4 500
HRZG	90	3	BRUT	91	2		90 1/4 500
MASH	90	2	MWSE	91	1		90 1/8 500
CHIP	90	1	TWPT	91	1		90 1/8 100
LEHM	90	1	NITE	91 1/4	1		90 1/4 600
DBKS	90	1	DLJP	91 3/8	5		90 1/4 600
DLJP	89 7/8	5	NFSC	91 7/16	1		90 1/4 500
MONT	89 7/8	1	COWN	91 1/2	1		90 1/4 1.00K
MSCO	89 7/8	1	SBSH	91 3/4	1		90 1/4 400
FBCO	89 3/4	1	MSCO	91 7/8	1		90 1/4 500
NFSC	89 11/16	1	PRUS	92	1		90 1/4 500
SHWD	89 9/16	1	CHIP	92	1		90 1/4 500
NEED	89 1/4	1	NEUB	93	1		90 1/4 500
BTRD	89 3/16	1	FLTT	93	1		90 1/4 500
INCA	89 1/8	10	LEHM	93	1		90 1/4 500
LAZA	89 1/8	1	NEED	93 1/4	1		90 1/4 500
TWPT	89	10	JPMS	94	1		90 1/4 500
PRUS	89	1	PIPR	94 5/16	1		90 1/4 500
COWN	88 1/2	1	RSSF	95	1		90 1/4 500
							90 1/4 600

When you're reading the tape, you can always play around with different chart layouts, in this example I stretched it so you can see exactly how bearish the pattern of selling is.

Now, if everyone and their brother is selling to SBSH and STRK at 90 1/4, the current inside bid, will you try to buy the stock here? I hope not.

You may want to join the bidders a couple levels down if you are playing off a pivot point based on your charts (eg a whole number decade support level like 90 for DCLK here, risky though).

In this case I'd enter a bid at 90 and see if the price comes in; it looks like there's some support at 90 (9 bidders, including MLCO and BEST). If, on the way down, though, MLCO faded his bid lower and a couple other bidders canceled their bids, I'd also cancel my bid and wait to see a clear pattern of buying in T&S.

You're seeing a few larger trades, like the 9.6K one and a few 1K trade, along with some outside trades at 90 1/8. All fairly bearish. Don't enter a long position here, of course.

**Pop Quiz Question:** What type of order routing was responsible for the trades that happened "outside the market" at 90 1/8? SOES, Selectnet, ARCA, ISLD?

Answer: preferred selectnet order

## How to Trade Blocks and

## Volume Patterns in Time & Sales

Ok, now that you know the major, obvious trends in Time & Sales, we'll begin looking at specific daytrading strategies and tips you can use in this (and the next 2) lessons.

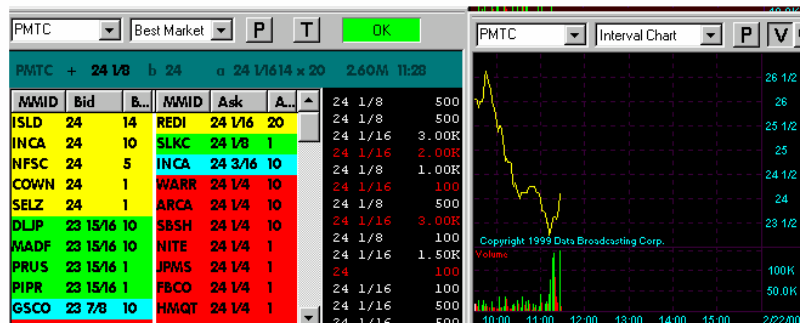
### Volume Buying on a Pivot Play:

This is the Best bullish type of pattern to play.

What's going on here?

- 1) Many block trades of 1K - 3K shares going off at the ask
- 2) Heavy support at a whole number and thin sellers.
- 3) Big volume spikes in the 1-minute chart.

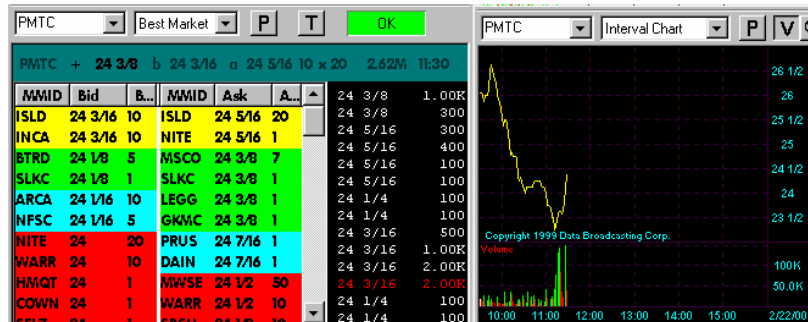
### Obvious Buy Here-Hurry!



Hopefully, you got in a bit earlier, on the first pivot, when the volume buying spike showed up in the 1-minute chart. If not, that's ok, there's still "juice" left in this trade. We see a lot of buyers at 24 1/16 on our time and sales, both a recent volume pattern in the chart and block trades in T&S.

Great, we nailed it! Now we're starting to see a mixed pattern on T&S, and it looks like we have a lot of sellers at 24 3/8.

Maybe I'll offer out the the 1K shares I just bought at 24 1/16 for 24 1/4. Ok, I get filled and make another \$187 in 2 minutes. Repeat many times a day and make a living daytrading.



**Daytrading Plays:** This is a classic textbook buy setup for a daytrader who scalps. It doesn't get any more obvious than this.

Hint: you see an INCA bid at 24 3/16, this might be some real support from a mm who's parked his bid here, wait to see how many shares whoever's anonymously buying via INCA wants to see if there's real support there. Of course, the same could be said about sellers on ISLD.

Remember, volume is your friend - it's the "vote" of the traders at that moment in time. Watch for blocks (trades of >5K shares, usually made by institutional traders) at the bid or ask prices to determine what the near term trend may be.

Your level 2, again, is a secondary tool to help you time the exact second to "pull the trigger" on your trades. Time and Sales is the "real story of the stock" you must pay attention to.





You want to exit before everyone else "heads for the door" too, so you sell into the buying momentum. This lesson shows what that means from a tape-reading perspective; the signals you want to look for in the tape to help you make trading decisions.

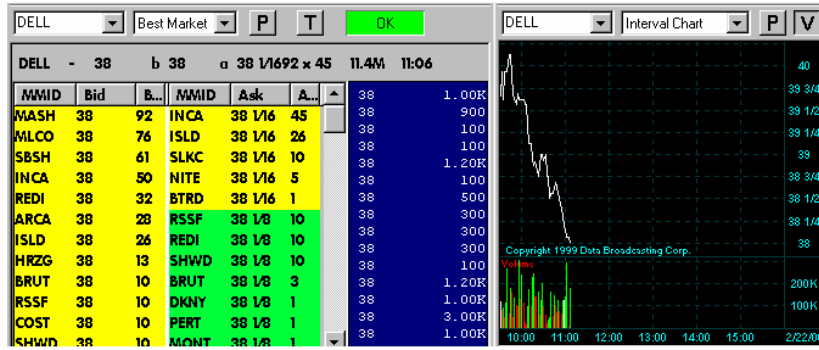
For pivots, you'll see a flurry of selling, some indecision, some in-between trades, then a flurry of buying, then a shake, then more buying etc. The speed slows down as indecision grips the traders worldwide you're trading with. What will happen next?-everyone is wondering. Waiting until you see a flurry of buys at the inside ask is a final indicator that the trade is headed up, in tape reading and scalping you need to be very fast on the trigger to capitalize on these moves.

**DELL SCALP Using Time & Sales:**

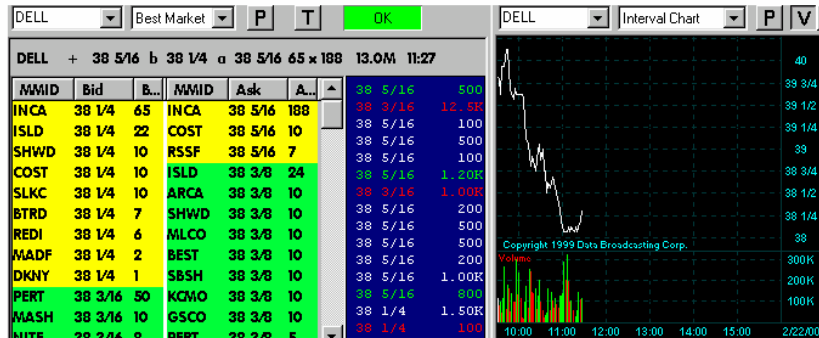
Let the Tape Speed Help You Decide When to Buy...

Let's look at an example of DELL from late Feb., 2000 -

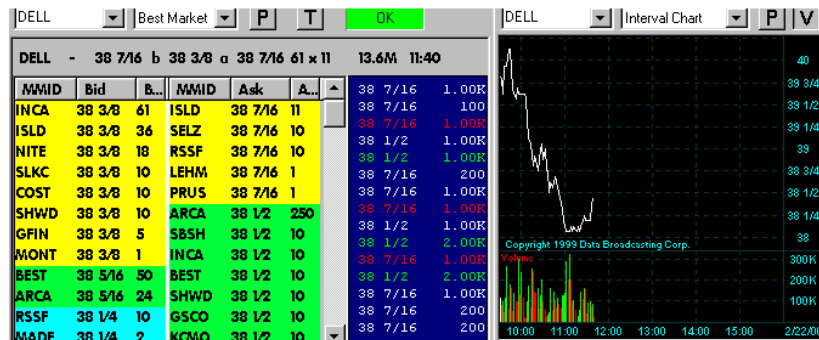
**Chart #1:** here we see a bearish pattern in T&S, trades all going off at the bid. But, it's at a whole number support level, so lets see where it goes from here. Waiting to see buyers before entering a trade.



**Chart #2:** DELL bought at buyers took out the 38 1/16 asks 20 mins later, we see most of the trades going off at the ask, 38 5/16, still bullish. As far as momentum goes, you can see by the volume bars at the bottom of the chart that the upturn is occurring on slightly less volume. The trade pace is still brisk in T&S, so we stay in long.

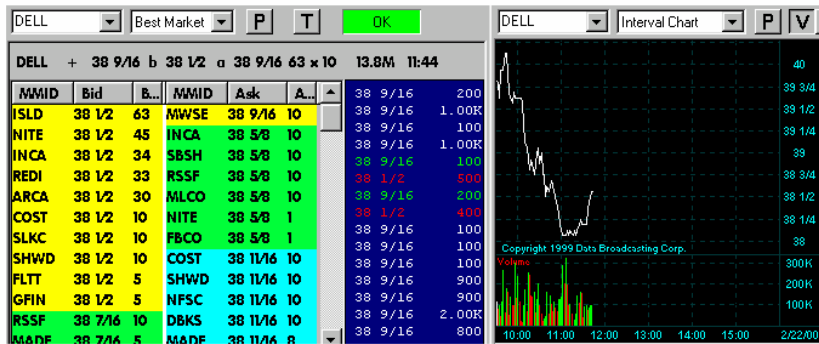


**Chart #3:** Here we see continued strength in time and sales - all of the trades went off at the ask price of 7/16 or better. Nobody's selling..we stay in long.



**Chart #4:** Now we see even more buying at 9/16...bullish, we stay in long. We end up closing the position at 38 11/16 for a 5/8 point gain on 500 shares, or \$360 in about 20 minutes. Not too bad. Why sell? Because the tape speed slowed down, and the retracement was fairly large for the timeframe and price.

Time and sales is our guidepost that shows us where the crowd is taking the stock at a given point in time. When trades go off faster and faster in time and sales, be sure you're on the side of the momentum you see.



Time	Exg	Price	Size	Flags	Bid	Exg	Ask	Exg	Sizes
2/22 11:35:58	NASD	101 5/8	700						
2/22 11:35:57	NASD	101 11/16	2000						
2/22 11:35:57	NASD	101 9/16	5000						
2/22 11:35:56	NASD	101 11/16	2000						
2/22 11:35:56	NASD	101 5/8	400						
2/22 11:35:55	NASD	101 5/8	400						
2/22 11:35:52	NASD	101 41/64	1000						
2/22 11:35:52	NASD	101 5/8	100						
2/22 11:35:51	NASD	101 9/16	1000						
2/22 11:35:51	NASD	101 9/16	3000						
2/22 11:35:51					101 5/8	NASD	101 11/16	NASD	10x36
2/22 11:35:48	NASD	101 11/16	1000						
2/22 11:35:45	NASD	101 5/8	100						
2/22 11:35:45					101 5/8	NASD	101 11/16	NASD	10x46
2/22 11:35:45	NASD	101 5/8	1000						
2/22 11:35:45	NASD	101 11/16	100						
2/22 11:35:43	NASD	101 5/8	200						
2/22 11:35:43	NASD	101 5/8	1000						
2/22 11:35:41	NASD	101 5/8	1000						
2/22 11:35:40	NASD	101 5/8	1000						
2/22 11:35:40	NASD	101 3/4	10000						
2/22 11:35:39	NASD	101 5/8	100						
2/22 11:35:38	NASD	101 5/8	300						
2/22 11:35:38	NASD	101 5/8	200						
2/22 11:35:38	NASD	101 11/16	200						
2/22 11:35:38	NASD	101 5/8	100						
2/22 11:35:38	NASD	101 5/8	100						
2/22 11:35:38	NASD	101 41/64	100						
2/22 11:35:37	NASD	101 5/8	100						
2/22 11:35:37	NASD	101 11/16	500						
2/22 11:35:37					101 5/8	NASD	101 11/16	NASD	10x23
2/22 11:35:35	NASD	101 5/8	100						
2/22 11:35:35	NASD	101 5/8	100						
2/22 11:35:34	NASD	101 5/8	300						
2/22 11:35:34	NASD	101 5/8	200						

### "Volume and Block Bear Signs" in time and sales:

Looking at INTC here, what warning flags do you see?

- 1) christmas tree, green and red mixed, so we're either at a pivot or a low-percentage place to trade, avoid it
- 2) See in the "Sizes" column where the bid/ask sizes are all bigger on the ask size? This is bearish too - eg 10x36 (bid x ask, 36 is bigger), 10x46 etc, means there is more stock to sell than there is to buy, a bearish sign.

Learn to monitor the sizes as well as the momentum and pace of the tape; when these traders are entering their tier buy/sell sizes you know which direction or sentiment they have towards the near-term direction of the stock price.

3 out of 3 bid/ask pairs are bearish, and there's not a steady string or majority of trades going off at the ask, so this is a stock to either short or stay out of for now.

### Daytraders Play: Using the Tape Speed to Enter and Exit Positions

24 7/16 100  
 24 7/16 200  
 24 7/16 1.00R  
 24 7/16 500  
 24 7/16 1.00R  
 24 7/16 200  
 24 7/16 200  
 24 1/2 200  
 24 1/2 500  
 24 1/2 100  
 24 1/2 500  
 24 1/2 100  
 24 1/2 200  
 24 1/2 500  
 24 1/2 100

Which of the two T&S displays is faster? If this is the same stock, but at different times during the trading day, how would you play it?

Well, if it was 9:50 and we see a time and sales like the one to the left, and all of a sudden it gets fast, like the one on the right, we know something's happening - either a breakout or a retracement will happen. You want to train your eye to see the different tape speeds, and to know how fast trades usually execute in T&S at different times during the day for the stocks you like to trade.

Learn it and prosper.

24 1/2 1.50R  
 24 1/2 500  
 24 7/16 100  
 24 7/16 200  
 24 7/16 1.00R  
 24 7/16 500  
 24 7/16 1.00R  
 24 7/16 200  
 24 7/16 200  
 24 1/2 200  
 24 1/2 500  
 24 1/2 100  
 24 1/2 200  
 24 1/2 500  
 24 1/2 100

**A Few More Professional Time & Sales Tape Speed Guidelines:**

1. If it speeds through a whole number in either direction, be prepared to play the pivot 1/16 to 1/4 point on through the whole number.
2. Pay close attention for blocks going off during tape speed-ups, this signals that institutional buyers/sellers "agree" with the crowd (important) and will likely maintain direction in the direction that they traded in (eg block going off at the bid, ask, in-between or outside).
3. Be aware that a mm fake play is to fire off a string of 100-200 share trades (vs a block) in the direction he wants the stock to go in to cover/buy a block once it starts consolidating. He makes it look like there's a string of buyers/sellers when in reality it's just him, trying to work the order flow to his advantage. No real counter-plays for this one.
4. Get to know the T&S action for 1-3 stocks like the back of your hand, know what's routine vs. price-moving.

## Module Two

### Comprehensive Level 2 Trading Techniques:

◀ PREVIOUS NEXT ▶

Back to  
MODULE 2

- [Time & Sales part 3: How to Read & Trade Tape Resistance and Support](#)

#### ● Main Points:

- Our final tape reading lesson for now looks at how to recognize and trade support and resistance patterns.
- Remember using TA with our charts we expect 'support' and 'resistance' levels at the tops and bottoms of key trading ranges, right? Using Time & Sales is another, more powerful tool you can use to confirm breakouts, breakdowns and pivots.
- Practice all three lessons' worth of Time and Sales lessons to become an effective daytrader. There's more to cover, yet mastering these three lessons alone should significantly boost your trading profits, if practiced over the course of weeks and traded with effectively.
- What do you do when the tape is showing resistance? Either sell off your entire position, scale down (eg sell 1/3 to 1/2 of it while waiting for confirmation of trend change), or enter a new short as buyers start to dry up.
- In tape reading, always remember that you're looking for momentum (covered in the previous lesson) as well as the ratio of buyers to sellers (both quantity and share size). Keeping this ratio in mind as you see transactions scroll down the screen helps you determine net buying or selling that's going on, and make a higher-probability trading decision. **The key is to recognize the difference between a minor retracement and a genuine change in the trend direction using Time and Sales.**

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Note: The higher-%age bottom or top you're playing, the more likelihood a pivot is about to occur (eg if WCOM sold off by >5% on no bad news that morning by 10:30am).

L2: Doesn't tell you much here, slightly weighted in favor of sellers; indeterminate.

T&S: Trades going off fairly mixed here, a few bearish blocks, need to watch tape for a trend to emerge.

## #2: Bottoming (or topping) out, about to pivot off a key support/resistance point.

After looking at the stocks' 2-day or 5-day chart to identify likely support/resistance levels, you watch T&S to see if, indeed, the traders respond to these "pivot points" where the stock either bounces off a bottom support level or breaks through a key resistance price.

These are most likely to occur at decade whole numbers, eg 30, 40, 50, 100 etc.; occur at 1/4 points for lower-priced (eg \$10-\$30) stocks. You hopefully already know this.

**Here's what's new for Time & Sales: Watch to see if stops (or new buy orders) are being executed at these key support/resistance lines.**

You'll likely see a flurry of orders occur at even numbers for stocks. Wait to see if the trading direction goes to the 15/16 or 1/16 (or 7/8...1/8) either above or below this key trading number, then buy or sell with the trend that emerges after stops.

Example: WCOM trades up to 46, you see trades go off faster in Time and Sales as a multitude of orders occur at this price; you see everything from 100-share trades to 10K blocks happen. Wait a second.

Now, lets see if the price strengthens or weakens at this key price level. If you see a bunch of trades begin to go off at 46 1/16th, then an occasional 46 1/8th etc, then go ahead and buy, with a stop set at 45 7/8.

If on the other hand it hits 46, then sellers pour in at 45 15/16, then you see 45 7/8, then up to 46, then back down to 45 7/8 etc (over a 3-5 minute period), then you know it may not have the momentum to break past 46. Look for a lower high/lower low pattern on the 1-minute chart. If it looks like it's weakening, fire off a short at 45 15/16. Your cover stop should be no more than 46 1/4. Maybe you set a cover target of 45 5/8, or even 45 1/4 if you're lucky. In and out, using your tape to guide your trading.

This is how we trade time and sales professionally.

MMID	Bid	B.	MMID	Ask	A.	Volume
MASH	77	214	INCA	77 1/16	17	77 1/16 100
SBSH	77	77	NFSC	77 1/16	7	77 1/16 2.50K
MMWSE	77	68	ISLD	77 1/16	7	77 1/16 300
ISLD	77	57	COST	77 1/8	10	77 1/16 300
MADF	77	52	MLCO	77 1/8	10	77 1/16 100
BRUT	77	46	PWJC	77 3/16	1	77 1/16 100
PERT	77	36	DLDE	77 1/4	10	77 1/16 300
LEGG	77	35	FBCO	77 1/4	10	77 1/16 100
MLCO	77	27	HRZG	77 1/4	2	77 1/16 100
HRZG	77	19	ARCA	77 5/16	22	77 1/16 200
PWJC	77	17	SLKC	77 3/8	10	77 1/16 100
GSCO	77	10	MSCO	77 3/8	10	77 1/16 100
NITE	77	10	JPMS	77 3/8	1	77 1/16 100
ARCA	77	10	SBSH	77 7/16	10	77 1/16 100
BTRD	77	10	DLJP	77 7/16	10	77 1/16 100
COWN	77	10	MASH	77 1/2	3	77 1/16 100
DLJP	77	10	NITE	77 9/16	10	77 1/16 100
SWCO	77	10	PRUS	77 9/16	1	77 1/16 100
PRUS	77	9	SHWD	77 9/16	1	77 1/16 100
FCAP	77	9	SALI	77 5/8	9	77 1/16 100
AGED	77	8	AANA	77 5/8	1	77 1/16 100

Here's WCOM from 12/8/99 - we've shown you this chart before; look at it again from a Time & Sales perspective. It's a "Christmas Tree", green and red, no clear direction identified.

But, since our L2 shows a wall of buyers at 77, it's kind of a no-brainer scalp to bid 77 1/32 (or pay up the 1/16th) and sell it back at 1/4 or higher.

This is bouncing off a key support level, identified not on a chart, but on your L2 window. Note: these setups occur infrequently, but when you do you're probably pretty safe buying here, as Long As your stop is "I'll sell if the wall of buyers at 77 dries up to 4-5 participants (from the current 21+). Your stop is Not under 77, because this is a support level. It may well drop to 76 5/8 or less if it loses support at 77, so use the 77 L2 wall as your scalping support level.

Time and Sales should show some interest at the inside ask for you to stay in the trade; if everyone starts piling onto the buyers at 77 then it may well sell down. Note that MASH is using a bid size of 214 because he wants to be first in line ahead of solly SBSH w/77 size. ISLD buyers are 4th in line; I'd pay up retail and give up a spread rather than risk losing out entirely on the scalp because I wanted to wait behind several big market makers to buy. Or, split the spread with a 77 1/32 bid like I said (preferred).

This CHR X pattern shows all buyers off 12 support in T&S, see everyone bid 12 1/16?. Somebody sold a block at 40K, very bearish, but since we're trading 10Million shares today I don't worry too much.

Oh, they didn't tell you about that in the books? heh. You need to evaluate the importance of blocks in relationship to the total share volume traded so far that day. Re-read that.

Of course, if our volume was at 769K so far I'd worry a lot more about that 40K block.

Since all but one trade is going off at the inside ask, I'd expect WARR to stop selling and the stock to trade up to 12 1/16th x 1/8th. The point is, where does it go after that? 1/16th, clearing the spread, is only your first step. You want at least 1/4 point right?

Look at the column in the right for some additional tips.

MMID	Bid	B...	MMID	Ask	A...	
ISLD	12	81	WARR	12 1/16	7	12 1/16 200
MASH	12	48	ISLD	12 1/8	33	12 1/16 1.00K
HRZG	12	43	INCA	12 1/8	30	12 1/16 400
SHWD	12	28	HRZG	12 1/8	20	12 1/16 500
INCA	12	15	SHWD	12 1/8	10	12 1/16 1.00K
REDI	12	11	LEGG	12 1/8	10	12 1/16 300
ARCA	12	5	REDI	12 1/8	6	12 1/16 300
HMQT	12	3	MASH	12 1/8	5	12 1/16 1.00K
SLKC	12	2	NITE	12 1/8	1	12 1/16 500
NITE	12	1	FBCO	12 1/8	1	12 1/16 40.00K
SELZ	11 15/16	10	SELZ	12 3/16	1	12 1/16 1.00K
JANY	11 15/16	1	SBSH	12 3/16	1	12 1/16 1.00K

Look at the second wave of action in Time and Sales to see if the support at 12 is going to hold. The L2 bands are really secondary, remember they are there to help you time when, exactly, you pull the trigger, and how to best route your order - will you try to preference one of the mm's, or will you just use a market or limit order? L2 is not for making trade entry decisions - it can fake you out.

The Time and Sales tells you when and if you should enter the trade, and when the best time to get out is.

Remember that, and you'll be ahead of 60% of the other daytraders out there.

#### Other tips about Tape Support and Resistance:

- If you see at least 3 out-of-market blocks going off within the space of 20 or so trades, watch to see if the crowd follows the direction, and be prepared to act. For example, if in the CHR X example above we see several 10K blocks going off at 12 1/8 or a 50K block at 12 3/16 we know an institutional trader is buying or selling ahead of the crowd.
- He may well be wrong, or, more likely, will continue to add to (or sell from) his position over the course of the trading day to work his order to the best price possible for his client. Watch the Time and Sales window to see what effect, if any, these block trades have on the response of the other traders.
- The ratio of trades going off at the bid vs. ask, when weighted with the size of shares and relative speed of the tape, is the barometer of the stocks' price direction. Learn to feel the ebb and flow of the trading waves by closely watching the trades go off in your T&S window, using a liquid (eg over 1.5Mshares/day-volume) stock.
- **Winning Hint** Many new daytraders cannot afford level 2 or time and sales, and tend to play under-\$20 stocks. You and the professional daytraders and market makers have a distinct advantage against them when using these trading tools. The play? You might want to add a relatively inexpensive stock (but still good-volume, for insurance) to your L2 watchlist and see if you can gain a spread or two advantage against the 'budget trader' crowd by using the techniques we've covered in Module 2 using L2 and T&S. Rookie daytraders tend to pay up both spreads, buying at the ask and selling at the bid; you can make a handsome profit by trading 500-1K shares of inexpensive stock like a market maker does, offering to buy at the inside bid then offering it back out a few spreads up a few minutes later. You'll have to learn which market maker is the axe, typically the heavyweights (SBSH MSCO MLCO GSCO) don't trade the cheaper stocks. You may see mms like PWJC etc.
- Look at a wide time and sales screen (like the INTC one in the previous lesson) to see the relative bid/ask sizes, and use that to help you determine the trading sentiment, whether bullish or bearish, at that point in time.
- Trading tape basics: remember to never fight the tape; the crowd sentiment is what you want to trade for a profit, hopefully ahead of the crowd, usually with it, but never against it. Don't short the skyrocketing stock, or buy the stock that's still tanking; use your T&S as a flashlight to see which path in the cave you should follow.

- Anticipating upticks in price movement using Level 2

● **Main Points:**

- One of Level 2's best advantages is in helping you identify the time "right before" the stock rolls up by a spread or so.
- **Know that for the most active/popular stocks L2 is generally not very useful** (eg INTC WCOM DELL) and for some net stocks (like DCLK); I rely on 1- and 3-minute tick charts much more for these stocks. Don't over-rely on L2; it can frequently **"fake you out"** for example if you see what seems to be a wall of buyers/sellers it can go against you in a hurry, as the mm's on the most actives don't show their hand on L2. For the most actives, the overall day's trend seems to be a more reliable indicator (eg is it above it's opening price at 11:00? if so it will probably carry its trend thru to the end of day).
- Remembering that T&S is your best indicator, you can also **see when sellers are done** with a stock and will let it run by a spread or two using your Level 2 window. This happens when the **ax backs away from the inside ask and/or you see a lead mm jump to the inside bid**.
- One of the skills you want to refine is how to **"jump in right before it upticks"**, using L2 properly can help you with this. Remember, when trying to catch a bottom your chances are much better when you're buying the first sign of strength in a stock that has just dropped sharply vs buying into a slow decline (and of course the reverse is true for shorting/selling tops; the market reacts to extremes fairly quickly vs. slow price erosion or growth).
- Notes: In general, I find **SBSH** is particularly obvious about making his **buying** known by holding the inside bid (eg in NOVL) and **MLCO** is somewhat obvious about making his **selling** known by holding the inside ask (eg in WCOM). This all depends on the particular stock etc. but these are two consistent trends I've seen over the last couple years for these two mms. This is an overgeneralization, of course, but it's one observation I've found that tends to hold true over time for nasdaq techs (like the "10:30 nasdaq bounce").

**Examples:**

## Anticipating Upticks using Level 2

What do you see happening in the two Level 2 windows below?

MMID	Bid	Q	MMID	Ask	A	Time	Price	Volume
ISLD	17 7/16	21	INCA	17 1/2	30	12:14	17 7/16	1,000
BRUT	17 7/16	10	ISLD	17 1/2	17	12:13	17 1/2	200
BTRD	17 7/16	10	BTRD	17 1/2	10	12:13	17 1/2	300
GSCO	17 7/16	10	MASH	17 1/2	1	12:13	17 7/16	100
MLCO	17 7/16	10	SLKC	17 9/16	1	12:13	17 7/16	500
FBCO	17 7/16	10	LEHM	17 9/16	1	12:13	17 1/2	200
BEST	17 7/16	10	MLCO	17 5/8	10	12:12	17 7/16	1,000
WEDB	17 7/16	10	SHWD	17 5/8	5	12:12	17 7/16	800
AGED	17 7/16	1	NITE	17 5/8	1	12:12	17 7/16	500
WSTI	17 7/16	1	SWST	17 5/8	1	12:12	17 7/16	400
DKNY	17 3/8	25	FCAP	17 5/8	1	12:12	17 9/16	1,000
REDI	17 3/8	20	JPMS	17 5/8	1	12:12	17 1/2	1,000
INCA	17 3/8	15	SSSH	17 11/16	10	12:12	17 1/2	2,000



MMID	Bid	Q	MMID	Ask	A	Time	Price	Volume
ISLD	17 7/16	21	INCA	17 1/2	10	12:14	17 1/2	200
BRUT	17 7/16	10	REDI	17 9/16	20	12:13	17 1/2	300
BTRD	17 7/16	10	INCA	17 1/2	15	12:13	17 1/2	200
GSCO	17 7/16	10	SLKC	17 9/16	1	12:13	17 1/2	300
MLCO	17 7/16	10	LEHM	17 9/16	1	12:13	17 1/2	200
FBCO	17 7/16	10	MLCO	17 5/8	10	12:13	17 7/16	100
BEST	17 7/16	10	SHWD	17 5/8	5	12:13	17 7/16	800
WEDB	17 7/16	10	NITE	17 5/8	1	12:13	17 7/16	500
AGED	17 7/16	1	SWST	17 5/8	1	12:12	17 7/16	800
WSTI	17 7/16	1	FCAP	17 5/8	1	12:12	17 7/16	500
DKNY	17 3/8	25	JPMS	17 5/8	1	12:12	17 7/16	800
REDI	17 3/8	20	JPMS	17 5/8	1	12:12	17 9/16	400
INCA	17 3/8	15	SSSH	17 11/16	10	12:12	17 9/16	400

Bullish trades going off at ask

It looks as though the sellers using INCA may be finished and the stock may go up by a spread. The real question is whether it will **continue** up past the 17 1/2 mark.

The **momentum** is telling you that **buyers are coming in**, both in the time & sales window as well as in the level 2 width of the sellers (yellow ask) getting narrow as their stock is sold.

(notice NOVL has more than doubled since these snaps were taken just last November!).

**Daytrader's Play/Quiz:** Well, depending on how fast the momentum is, which of these five things would you do?

1. Join the ISLD bidders at 17 7/16 and hope for a fill (unlikely)
2. Enter a new bid at 17 15/32, to try and split the spread
3. Pay up retail and enter a buy limit at 17 1/2 (last resort, only do this if you're sure the 17 1/2's gonna get taken out fast)
4. Do nothing
5. Short it

Well, which would you do? I'd try #2, unless the yellow ask band had collapsed in a hurry (under 5 seconds) and the 17 1/2 sellers are going to disappear, in which case #3 is ok.

It's a zero potential short, all the buyers at 17 7/16 would have to step off their bids for the price to drop from here.

Try to avoid watching if you see a high-potential trade; set narrow stops to protect your capital and play when the indicators line up, as in here.

**Where would you set your stop?** The way I daytrade is to keep it really tiny, the reason I entered was a "bounce off 17 7/16 play", if I'm wrong then so be it, I sell and re-enter when buying strength is truly there.

In this case, I'd buy it and stop out at 17 7/16 if the bidders are almost all gone. That is, if this wall of 11 bidders dropped to 2-3 and a steady stream of selling is going on in time & sales at 7/16 then I'd probably sell there as well, the stock may well lose a couple more spreads (or more) before bouncing, I don't want to be there until buyers are back.

Remember, daytrading is largely about stopping out quickly when you're wrong, and nurturing your winners for hopefully > 3-5 spreads (or more) per trade for round trips averaging 1 to 10-20 minutes or so. Confusing daytrading with swing and overnight holds and investing is a leading "cause of death" for daytraders who want to make a career out of it. If it's against me 2-3 spreads I'm outta there.

You should risk no more than 1-3% of your capital on each trade, I prefer to make it even tighter and stop out if it's against me by \$80-\$150, whatever that translates into in terms of share price and number of shares I'm holding.



Another example to study:



### High-percentage Level 2 uptick plays

should be capitalized on whenever possible. For the actives like WCOM L2 is generally not useful, particularly when there's no "directional bias" evident in the buyers and sellers.

A gift like this one to the right should not be overlooked, however. You know this stock will bounce to at least 77 1/8 in all likelihood based on what you see here, right?

Now I don't want to buy a \$77 stock for a fractional gain, I'd use the 1-minute chart support/resistance levels to confirm the upside potential of the trade before going in:

What does this chart tell you about WCOM's price action?

MMID	Bid	B.	MMID	Ask	A.			
MASH	77	214	INCA	77 1/16	17	77 1/16	100	
SBSH	77	77	NFSC	77 1/16	7	77 1/16	100	
MWSE	77	68	ISLD	77 1/16	7	77	2.50K	
ISLD	77	57	COST	77 1/8	10	77 1/16	300	
MADF	77	52	MLCO	77 1/8	10	77	100	
BRUT	77	46	PWJC	77 3/16	1	77	100	
PERT	77	36	OLDE	77 1/4	10	77 1/16	300	
LEGG	77	35	FBCO	77 1/4	10	77 1/16	100	
MLCO	77	27	HRZG	77 1/4	2	77	100	
HRZG	77	19	ARCA	77 5/16	22	77 1/16	200	
PWJC	77	17	SLKC	77 3/8	10	77 1/16	100	
GSCO	77	10	MSCO	77 3/8	10	77	100	
NITE	77	10	JPM	77 3/8	1	77	100	
ARCA	77	10	SBSH	77 7/16	10	77 1/16	100	
BTRD	77	10	DLJP	77 7/16	10	77 1/16	100	
COWN	77	10	MASH	77 1/2	3	77	100	
DLJP	77	10	NITE	77 9/16	10	77 1/16	100	
SWCO	77	10	PRUS	77 9/16	1	77 1/16	100	
PRUS	77	9	SHWD	77 9/16	1	77 1/16	100	
FCAP	77	9	SALI	77 5/8	9	77	100	
AGED	77	8	AANA	77 5/8	1	77	100	



Ok it's falling, do you buy? Actually I say yes because of the following:

- Heavy volume at 77 since stops are taken out. Possible reversal play off whole number support.
- My Level 2 shows a lot of buyers are willing to pay 77 for it, "the crowd" is lining up to pay 77.
- T&S isn't all red, we're about even money on buyers vs sellers.
- I've seen a lot of buying reversals in WCOM throughout the selling, telling me the stock *does* make frequent positive retracements as it sells off. (they don't have that in any books either)...example at every major fraction buyers come back in, at least for 1/4-1/2 point, so I have every reason to expect buyers will be here at 77, enough for a scalp at minimum.
- Looking back at the 5-day chart shows previous support at 77, eg it has bounced off 77 at least once or twice in the last 5 days.
- Last but not least, I will be prepared to sell at 76 15/16 or 7/8 if I'm wrong and all the 77 bidders get taken out (sold to).

In summary, Level 2 can be used on rare occasions by itself to identify good trade entries, but remember its role is a secondary one to help you time precise intra-spread trade entries and exits, using market/sector direction, T&S and 1-minute charts as primary decision support tools.

- Using Trailing Stops and the "3-Spread Stop Loss" Rule

● **Main Points:**

- **Trailing Stops** defined: Once you are in a profitable trade, you should raise your stop loss to "follow" the stocks' price as it moves up. This ensures that you will take a profit from the trade and not let a winner turn into a loser.
- **Example:** You buy WCOM at 44 3/8 (putting an initial stop in at 43 15/16 using your software, or a 'mental stop' if you are highly experienced - 1+ years or more fulltime daytrading). Now, let's say WCOM ticks up to 44 5/8. You would cancel your original stop, and enter a new "trailing stop" in at, say, the point you bought in at, at 44 3/8 (or perhaps 44 1/4). Eventually, WCOM breaks through 45 and ticks up to 45 1/16th. Now, you cancel the previous stop and enter a new stop at 44 15/16 (always place your trailing stops 1/16th under whole numbers/major fractions). WCOM starts to tick down, you see a ton of sell orders hitting the bid at 45, it starts to get thinner on Level 2, now it drops to 44 15/16 and your stock is sold. You lock in a profit of 9/16th, or \$56/hundred shares (so, if you were trading 500 shares your profit would be \$280.) This all happens in the space of 5-20 minutes.
- **3-Spread Stop Loss Rule:** we will also see how to set your stop losses for those times that you are wrong and the trade goes against you right after you buy in. At DTU we advocate a 2-3 spread maximum stop loss. I usually use the level 2 strength within 1 spread, as confirmed by T&S and 1-minute chart, to set even closer stops for the frequent times we scalp for 3/8 - 1/2 points.
- Most books say "take small stops" without explaining the mechanics of how this works when you're using level 2 in a live trade situation. This lesson will show you step-by-step, using screen snapshots, how to set and manage your stops and trailing stops using Level 2.

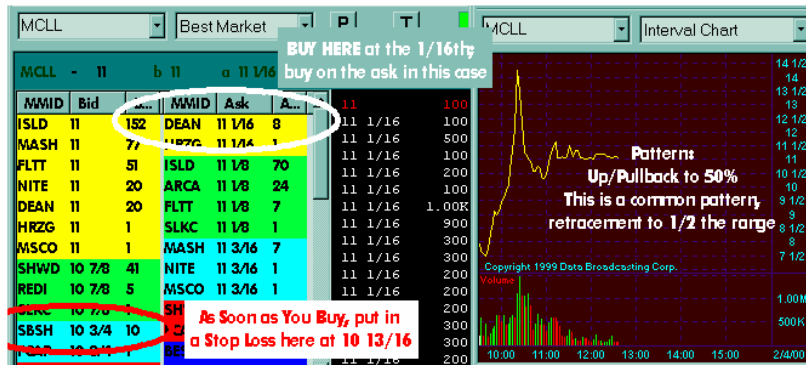
**Examples:**

### 3-Spread Maximum Stop Loss on Level 2

**3-Spread Stop Loss:** You should set a maximum stop of 2-3 spreads for all daytrades you do. I've illustrated how this looks in the level 2 window to the right.

You buy at 11 1/16, and immediately set a stop at 10 3/4 or 10 13/16. Why the 13/16? So that you get executed before it ticks down to 10 3/4.

Remember a lot of traders don't have level 2 yet (especially good tip for cheap stocks like this one; cheap stock players tend to be undercapitalized and can't afford pro L2 data feeds etc; our advantage).



Use Level 2 to help manage your timing for entries and exits, especially for stops and split-second timing for sell orders.

Never let a daytrade go more than 3 spreads against you. If you're that wrong about it, don't let it turn into an "investment", cut it short quickly and be prepared to re-enter the trade when buyers come back in.

Notes/Exceptions for this particular trade: Usually, I'd join the bidders at 11, but I'd be unlikely to get a fill, given the strong buying (see all the 11 1/16 buys on T&S) and thin number of weak mm's on the ask.

In fact, I would be likely to buy here at 1/16 and sell if the buyers at 11 thinned out down to 2-3 participants. If I'm wrong, I can always buy back in.

As a general note, you probably wouldn't want to buy this stock now anyways, it's lunch and it's already done its "run and retracement" for now. This trade might be good for only 1/8 point here, its a low percentage trade.

## Trailing Stops and Level 2

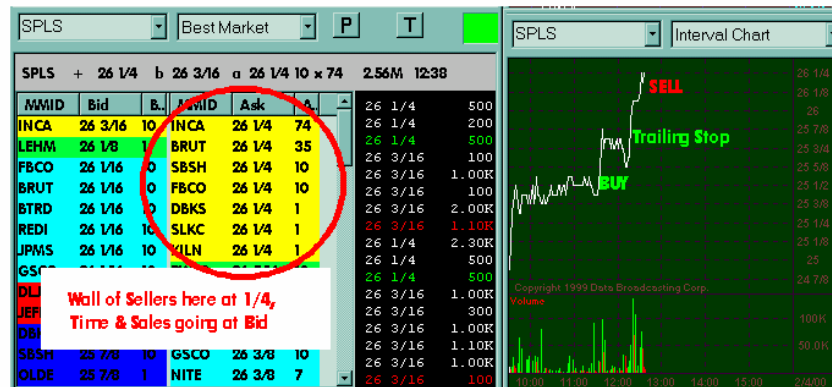
### Trail your stops roughly 3 spreads behind the current inside bid.

In this case, I'd probably sell right now, since there's a "wall of sellers" and it just ran up w/declining volume in the 1-minute chart.

If I was in the trade from earlier, my trailing stop would be around 25 15/16 (again, set it 1/16th under a whole number or major fraction).

Do Not neglect to use trailing stops; they lock in your profit and keep winners from turning into losers. It's better to consistently take 1/4s, 3/8ths and 1/2's off the table, keeping 1/16th-1/4point stops than to take large hits.

Another tip: You can also set your stops using a Dollar Amount, eg I never let a stock go more than \$200 against me (whatever that works out to in terms of



The trailing stop you use depends on three factors:

- 1) **Time of day:** use tighter stops if you are outside of "prime time", eg trading after 11:30 EST.
- 2) **Momentum:** If the stock is running up then ratchet up your stops faster and be prepared to sell quickly, before, the other sellers do. What goes up fast also drop fast as well.
- 3) **Price Levels Widths for Your Stock:** Some stocks have each level only 1-3 participants wide, others like SPLS will get as thick as 6-8 participants. In general, use a larger number of spreads (up to 5) for stocks that are trading with thinner numbers of participants at each level.

the number of stops etc.).  
Your stops should be "small cuts" you take on the way to successful, larger trades.

Get used to stopping out early, stopping out often. The extra commissions are a small percentage compared to loss of bigger chunks of your trading capital.

I used to get stopped out from 60-80% of the time; even on a great day I now seldom do better than 70% right on my trading calls; it's the money management piece of it that keeps it in the green and keeps it profitable.

Remember: You can make a living daytrading by being right only 20% of the time. Keeping tiny frequent stops and trailing your winners up to lock in profits is the key to success in daytrading.

Avoid the temptation to buy bottoms and short tops all the time; it's like fishing. Wait instead for Volume Reversals and pivots, using a stop at the previous low (for bottomfishing) or previous top (for shorting).

Stocks like WCOM and DELL are very difficult to daytrade since everyone's scalping them all the time for a living; try trading easier stocks at first.



Order Routing via ECNs, Selectnet, SOES; limit/market order routing

## **Nasdaq Order Routing: DTU's Guide for Daytraders**

### ● **Main Points:**

- Once you are with a daytrading broker, you will have many more **choices** as to how you wish to route your order (how you decide to place a buy or sell order to execute your trade). **Learning how to use these different order routing choices is important to your success.** *We've tried to make this the easiest-to-understand visual guide to Nasdaq order routing available.*
- Besides using market and limit orders, **you now have the added flexibility of Who you want to try and buy and sell stock with:** you can trade with specific market makers and use specific ECNs to trade with that you see on your Level 2 screen.
- **There are Two primary ways to route your order: Using the market systems (SOES & Selectnet) and using the ECNs (ISLD ARCA etc.).**
- Most market makers trade on Selectnet, many online trading firms (like Datek) represent buy/sell orders using the various ECNs, eg Datek uses ISLD.
- The major difference between the two: Because trading on the Nasdaq is computerized, **ECN orders get handled instantaneously, but when trading with the market market makers via Selectnet, the mms have a choice as to whether or not they want to trade with you** (and, SOES is mandatory for mms, but as with ecn orders you will be competing with other traders and may not get filled at the price level you want). Overall, trading on ISLD seems to be the fastest and safest way to go. We'll get into the details below.

*Notes on using daytrading vs. online discount brokers:*

- After learning the basics with a browser-based online broker like Datek, you should get a level 2 service (like esignal) and choose a direct-access daytrading broker like Cybercorp, MBTrading, or others. I would recommend using Datek or another Fast online browser-based broker for your first few months, then switch over to a daytrading broker.
- Many new daytraders go with daytrading brokers from the start, and the speed causes them to spend a fortune in commissions and bad trades, wiping out a lot of their trading capital. Think of it like racing, if you want to be a racer start by driving a sedan first, then migrate to the Formula One racer...if you start with the fastest thing out there you can accelerate your trading losses. During the first 3-6 months, use a reasonably fast online discount broker. If your online broker can't give your order confirmations and fills within 60 seconds on average, though, switch. I made a lot using Datek for well over a year, now I'm with Cyber.
- New traders might want to consider using longer trading timeframes (eg swing/overnight holds) or longer intraday trade times (eg buy at 9:50 sell at 11:30-type trades); you should use a direct-access daytrading broker if you like to scalp within under-20 minute roundtrip type trades (my favorite). If you don't need to have your order filled within a few minutes (because you buy it at 9:50, sell it at 11:30 etc. type trading), there's no reason to spend the extra commission load to get the faster fill time. Just be sure to *a/ways* use limit orders to buy.

## **Your Order Routing Choices:**

**MARKET SYSTEMS:**  
(trading directly w/mms)



OR

**ECNs (Electronic Communication Networks):**  
(trading with all traders in the market,  
including both mms and daytraders)



Let's look at the differences between these. I've organized a table below showing the rules, when to use, and costs.



	SelectNet	SOES	ECNs
<b>What Is It? How does it work?</b>	<p>SelectNet is the system that market makers use to trade with. You can also trade directly with mms using Selectnet orders. You cannot post bids/offers on Level 2 using Selectnet. There are 2 types of Selectnet orders you can make:</p> <p><b>BROADCAST:</b> Your order is sent to all market makers simultaneously; they can decide whether or not to trade. Low-priority for mms.</p> <p><b>PREFERENCE:</b> An order you send to a specific market maker, eg SBSH. Only he sees that bid/ask order you are making. Hi-priority for mms.</p>	<p>SOES is a system that lets traders trade in blocks of 200, 500 or 1000 shares (only), called tiers. SOES executes against mm's without their choice.</p> <p>SOES orders are automatically executed against the market maker; but the order is held in "queue" for 90 seconds. SOES is not used much by daytraders anymore because ECNs are more efficient.</p>	<p>ECNs pair up buy and sell orders and execute them in the order received. The ISLD ECN, used by Datek and many others, is the fastest and most efficient ECN available to trade on, allowing for instant executions.</p> <p>The ISLD book lets you see all the open orders at each price level. ECN's are the most popular way for daytraders to trade. You can trade odd lots easily on ECNs, and they are very liquid, allowing rapid trades. You can also get price improvements if the bid/ask price on the book is better than the one you enter.</p>
<b>Nasdaq's Trading Rules for This System</b>	<ul style="list-style-type: none"> <li>Once entered, you cannot cancel Selectnet orders for 10 seconds.</li> <li>For preferenced orders, the mm must respond with an Accept/Decline/Partial to you within 15-30 seconds.</li> </ul>	<ul style="list-style-type: none"> <li>5-minute rule: once you've entered a SOES order you cannot enter another order for the same stock in the same direction (buy or sell) for 5 minutes. But, it resets any time you reverse direction, eg you can buy/sell/buy again within 5 minutes.</li> <li>SOES can't execute against ECNs.</li> <li>All SOES orders are done at the inside market.</li> </ul>	<ul style="list-style-type: none"> <li>ATTN orders must be in the 100's.</li> <li>You can't send conditional Selectnet orders (eg all-or-none) to ECNs.</li> </ul>
<b>Advantages &amp; Disadvantages for Daytraders</b>	<p><b>ADVANTAGES:</b></p> <p>You can execute orders outside the market for fast-moving stocks, eg preference a mm who's 2-3 spreads away.</p>	<p><b>ADVANTAGES:</b></p> <p>As long as you're first in line, you can usually get a fill at the tier size advertised by the market</p>	<p><b>ADVANTAGES:</b></p> <p>Speed and instant executions. Price improvement possible. Liquidity is great. You can play market maker (especially pre- and post-</p>

You can try for price improvement, especially if you are trading in size, since the mm may want to buy without "showing his hand", preferred orders are silent to the market (though the trade will show on the t&s tape).

**DISADVANTAGES:**

For fast-moving stock the mm's reponse time (up to 30 seconds) can cause trading delays. Main disadvantages are speed and cost, you might get a faster fill at a better price using an ECN.

controlled by the market maker. It's "automatic", like the ECNs, where Selectnet is totally optional.

**DISADVANTAGES:**

SOES only works on the inside market; you may not get filled, the 5-minute rule.

market) by exploiting the wide spreads (buy at bid, sell at ask).

**DISADVANTAGES:**

The ECN's don't always have stock in their books at each price levels, where the market makers may have the price you want available. ECN participation varies by stock; some are more heavily traded on ECNs than others.

**Costs**

Selectnet broadcast: \$2.50

Selectnet preference: \$1.00

Cost: free

Cost: ISLD/NTRD direct: free;

REDI .002/share

BRUT/INCA: .015/share +\$1 if preferred thru Selectnet

ATTN/BTRD/TNTO: .005/share + \$1 if preferred thru Selectnet



**Pop Quiz on Order Routing:**

Ok here you are trading from the hood of your Mercedes, placing an order to buy 1000 DELL.

You see this level 2 screen, and decide you want to buy your DELL on ISLD.

MMID	Bid	B...	MMID	Ask	A...		
ISLD	53 9/16	20	ARCA	53 5/8	30	53 9/16	100
INCA	53 9/16	14	ISLD	53 5/8	30	53 5/8	1.00K
ARCA	53 9/16	10	NTRD	53 5/8	10	53 5/8	300
BEST	53 9/16	10	INCA	53 11/16	10	53 9/16	100
NITE	53 9/16	5	NFSC	53 11/16	10	53 9/16	700
NWSE	53 1/2	54	NITE	53 11/16	5	53 5/8	300
SBSH	53 1/2	10	REDI	53 11/16	2	53 9/16	100
SHWD	53 1/2	10	PIPR	53 11/16	1	53 5/8	1.00K
RAMS	53 1/2	10	BTRD	53 3/4	214		
DEAN	53 1/2	10	MLCO	53 3/4	22		
MSCO	53 1/2	10	SHWD	53 3/4	10		
MADF	53 1/2	2	WARR	53 3/4	10		
SLKC	53 7/16	10	SBSH	53 3/4			
DLIP	53 3/8	10	PERT	53 3/4	7		

Q1: Which of the following is the only real Market Maker on the inside bid/ask playing with all you ECN traders?

- a) INCA
- b) BEST
- c) ARCA
- d) ISLD

*Note: These pop quizzes are the result of a several traders asking "do you have quizzes and tests at DTU?"...so, I'll work them in as I have time.*

**Q2: Oops, a news story comes out saying DELL has been sued by a group of daytraders** because of faulty keyboards (they're not coffee-proof lol). You think all the ECN books will be traded too fast, so you want to preference a market maker to sell outside the market. **Who is the best out-of-the market maker you should try to sell to using a Selectnet preference order?**

- a) SBSH
- b) BTRD
- c) MADF
- d) ISLD

Answers below:

 Quiz answers:

Question 1: Answer is BEST, Bear-Stearns, the rest are ECNs

Question 2: Answer is SBSH, the outside bid market maker with the biggest size.



How to avoid getting shaken out/faked out on Level 2: using your charts to confirm trade entries and exits (stocks, MACD, RSI etc.)

● **Main Points:**

- Some market makers like HRZG MASH often show ridiculous bid sizes (eg 58, 104 etc) to give the false impression that there is buying strength in the stock. As soon as people start to hit their bid they often vanish (drop back a spread or two). You say "wow I thought there was a ton of buyers, where did they disappear to? These are common mm tricks to panic new daytraders out of their positions. Let's fight back, ok?"
- Other times, as we saw in earlier lessons, a mm will pretend to be a seller when he's really buying a boatload on ISLD or INCA. The way, as always, to tell the truth of the situation is to follow the momentum in Time and Sales - this tells you the genuine directional flow of the stock price.
- A general rule of thumb to repeat: stocks that are heavily traded primarily on ECN's (where you see a lot of ISLD INCA ARCA action in the inside bid/ask instead of the big mms MSCO GSCO SSSH MLCO) are not as easy to anticipate and follow using level 2; I find level 2 is more useful for stocks that have active participation by the big mms. For these ECN-traded stocks (eg DCLK) I find the one-minute chart is the most useful tool. I still watch L2 of course, but it does not play as big a role in helping me to decide whether to get in a trade or not.
- Some of the stocks for which L2 has been particularly worthless to me include WCOM, INTC and MSFT; yet another reason to avoid the "most actives" when it comes to daytrading. Why? In these stocks, the bid/ask columns are usually 5-12 participants wide and there is seldom any clear direction for net buying/selling. Of course, the T&S is still very useful here, as is the 1-minute chart.

## Avoiding Fake-Outs on Level 2

**Examples:**

**If you had made the common new trader's mistake of just relying on Level 2 in the example below, you'd have been wrong.** Look at the price action and time: in just 3 minutes (from 9:53 to 9:56) the 1/4 bid evaporated and the stock started selling off.

**Look at the Level 2 box on the left: it looks like the price may go up, right?** There's a lot of bidders compared to sellers. Now look at the Level 2 box on the right: just 3 minutes later and nothing but sellers. Fake-out!

How did this happen, you ask? Hopefully you didn't pay retail at 19 5/16 and sell back at 19 3/16 or lower once it started dropping; that's how professionals take your capital away.

**Quiz: There's TWO CLUES THAT SHOULD HAVE KEPT YOU OUT OF THIS TRADE. What are they?**

*(Answer below)*

MMID	Bid	B...	MMID	Ask	A...	Time	Price	Volume
MADF	19 1/4	80	ISLD	19 5/16	10	09:53	19 1/4	7.00K
ISLD	19 1/4	30	PRUS	19 5/16	10	09:53	19 1/4	200
INCA	19 1/4	30	MSCO	19 5/16	10	09:53	19 5/16	200
NFSC	19 1/4	21	BRUT	19 5/16	10	09:53	19 5/16	700
SBSH	19 1/4	10	PCAP	19 5/16	5	09:53	19 19/64	300
DBKS	19 1/4	10	WSTI	19 5/16	1	09:53	19 5/16	100
SHWD	19 1/4	5	MONT	19 5/16	1	09:53	19 1/4	300
NITE	19 1/4	2	NFSC	19 3/8	30	09:53	19 5/16	600
PERT	19 1/4	2	INCA	19 3/8	25	09:53	19 1/4	6.00K
FLTT	19 1/4	1	ANSR	19 3/8	10	09:53	19 19/64	900
COWN	19 1/4	1	INCA	19 3/8	25	09:53	19 5/16	500
HRZG	19 1/4	1	PWJC	19 3/8	10	09:53	19 1/4	300
MONT	19 1/4	1	DLJP	19 3/8	10	09:53	19 5/16	200
OLDE	19 1/4	1	FBCO	19 3/8	10	09:53	19 1/4	400
WPFO	19 3/16	10	LEHM	19 3/8	1	09:53	19 5/16	100
PRUS	19 3/16	10	HRZG	19 3/8	1	09:53	19 5/16	200
VNDM	19 3/16	10	DEAN	19 3/8	1	09:53	19 1/4	1.00K
WETH	19 3/16	10	SLKC	19 3/8	1	09:53	19 5/16	100

MMID	Bid	B...	MMID	Ask	A...	Time	Price	Volume
COWN	19 1/4	10	ISLD	19 5/16	225	09:56	19 1/4	100
DBKS	19 1/4	1	BTRD	19 5/16	100	09:56	19 1/4	100
ISLD	19 3/16	41	INCA	19 5/16	10	09:56	19 1/4	6.60K
INCA	19 3/16	25	REDI	19 5/16	10	09:56	19 17/64	1.00K
NFSC	19 3/16	10	MSCO	19 5/16	10	09:55	19 1/4	5.00K
WPFO	19 3/16	10	PCAP	19 5/16	5	09:55	19 17/64	1.00K
PRUS	19 3/16	10	ARCA	19 5/16	3	09:55	19 5/16	1.20K
VNDM	19 3/16	10	LEHM	19 5/16	1	09:55	19 1/4	200
WETH	19 3/16	10	WSTI	19 5/16	1	09:55	19 1/4	200
HRZG	19 3/16	1	MONT	19 5/16	1	09:55	19 1/4	400
BRUT	19 3/16	1	MWSE	19 3/8	20	09:55	19 1/4	600
CIBC	19 3/16	1	PWJC	19 3/8	10	09:55	19 1/4	2.90K
PERT	19 1/8	10	WETH	19 3/8	10	09:55	19 5/16	200
SNDV	19 1/8	10	DLJP	19 3/8	10	09:55	19 17/64	400
MLCO	19 1/8	10	FBCO	19 3/8	10	09:55	19 1/4	100
BEST	19 1/8	10	MADF	19 3/8	4	09:55	19 17/64	600
FLTT	19 1/8	8	NFSC	19 3/8	1	09:55	19 1/4	1.20K
MWSE	19 1/8	2	HRZG	19 3/8	1	09:55	19 1/4	100

Answer:

1) **Time and Sales** shows primarily selling action, a lot of trades going off at 19 1/4, including the block trades of 6K and 7K shares. Very bearish sign.

2) **Weak bidders vs sellers:** MADF (a small mm) and ISLD/ARCA bidders are weak. When you look at T&S you see that over 3K shares have been bought from ISLD at 19 5/16, yet the ISLD book is still strongly weighted to sellers, it didn't disappear, telling you that the depth of sellers on ISLD at 5/16 is heavy. Also, MSCO is right under the ISLD/PRUS asks, and he's a strong market maker.

**Daytraders' Play:** Keep your eye on the ball, which is Time and Sales, and the 1-minute chart. I'd look to buy this stock off 19 support, maybe put my bid in at 19 1/16 and have a stop at 18 15/16.

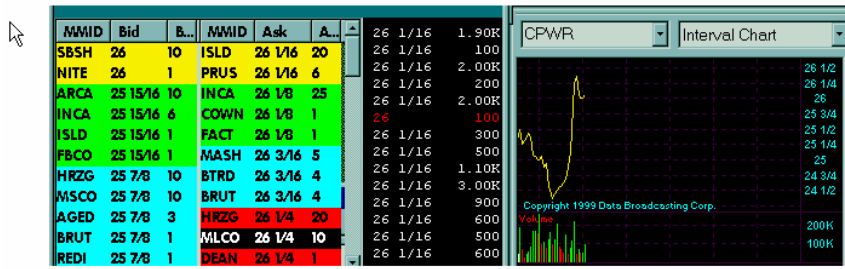
**Stops:** Again, mm's know that most traders set their stops at whole numbers and large fractions (1/4 3/8 1/2 5/8 3/4 etc). Use stops **1/16th under where the mm's drop the stock to** at these major whole numbers and fractions. For decade support/resistance, you might want to increase this to 3/16ths stops. Follow the major mm's closely for these plays.

**Example #2: In this CPWR L2 window and chart below, what do you see going on?**

A lot of buying at 26 1/16th, even though it's ran up 1 1/2 points off it's bottom, Time & Sales is telling us there's still plenty of buyers of this stock at 26 1/16. Also, since SBSH is on the bid (bullish) and only ISLD is on the ask (could be anyone, no direction indicated), it might be safe to enter a trade by bidding 26 1/32 or enter a buy 1100 CPWR at 26, frontrunning SBSH.

**At this point in the trade, you missed most of the major momentum**, and are looking for either incremental **scalps** (eg I'd scalp this to 3/16 - 1/4 max expectation), **or short** if it loses 26, for a short scalp down to the 5/8-3/4 support. Again, tempered by overall market direction - if it's a runaway bull market then I may stay in the trad a bit longer. If it's choppy or down, I'll be very cautious on any long positions and look to scalp only.

**Declining volume** that you see is also a bearish indicator, we may see some weakening of the stock, unless a major mm steps in to buy more. Note that sell volume was higher than the buy volume, and the buying ran up very quickly (weak high here), so again, cautious long even with a bullish tape; be prepared to fire off a sell (or short) if we drop back to 15/16.

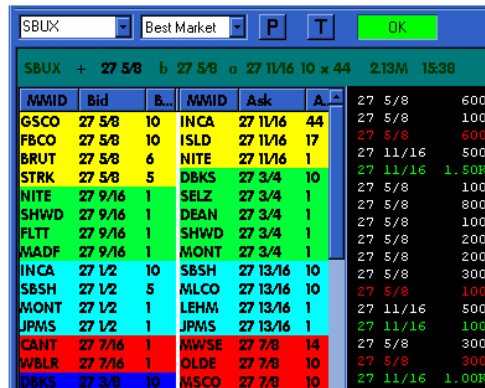


**Example #3:** The old "Trying to look like a buyer when you're really selling a boatload trick" (say that in your favorite Maxwell Smart voice). "Missed it by That Much".

Well, anyways, let's look at the L2 window below. What is MADF doing, buying or selling? Would you believe, "Selling"? No? Ok, how about "Looking like a buyer when he's really selling 50,000 shares on INCA"? (perhaps). It's hard to tell, all we know for sure is that GSCO is really buying since his bid is firm at 27 5/8 as seen by the tape action.

MADF, Even Though he's on the 2nd outside bid, he may be selling on INCA. So could FBCO and BRUT, for that matter. What we need to always monitor is the tape and the bid/ask size: are they staying the same? (indicating refreshed orders, impossible to tell the depth/order flow), or are they shrinking/getting bigger?

**Daytrader's Play:** Looks like they're selling it for now, you might want to put in a bid for the stock at 27 1/2 and wait for a bounce, or sit it out until the tape shows clear direction of selling resuming.



**In Summary, there are a few new points worth remembering about Level 2:**

- It should never be used as a primary direction/trend decision-making support tool
- It is useful to monitor your precise entry and exit timing, when used in combination with 1-min chart and T&S
- MMs will either a) flip from the bid to the ask or b) change the parameters of their "trade box", (eg where exactly they're bidding and offering the stock out at), when they believe the stock will change direction, you should be on the side of these major players when you see it happen.
- MMs will use Level 2 to advertise false and misleading bid/ask sizes to panic out and whipsaw the inexperienced trader
- L2 is useful as a trading tool only as a specific entry/exit indicator once T&S and TA has confirmed the direction or pivot point of the trade you want to enter. Eg, if both the major sellers of SBUX got taken out above (this time its ecns: ISLD/INCA) and NITE is alone on the ask, and T&S shows lots of trades going off at the ask, then you might want to pay up and buy retail at 27 11/16.

Additional insights into how & when to use Level 2

● **Main Points:**

- As with any tool, Level 2 takes time to master. Hopefully, you've learned how to integrate chart patterns and Time & Sales into your trading with Level 2 in Module Two. Level 2 is used to time the exact second that you buy or sell a Nasdaq stock, after using market/sector strength, chart TA and Time & Sales. It's a timing tool, not a trend direction tool.
- We will cover a few more techniques you should be aware of in this final page, and will add new strategies they are developed.
- From screen layout to trading decision-making, there is much room for experimentation in coming up with the best Level 2 setup for your particular trading style. Continually refine and try new setups until you come up with one that works well for you.
- The dramatic recent increase in the use of level 2 trading means that there are many unskilled traders who buy and sell based on perceived level 2 support/resistance alone, which is incorrect (watch WCOM some day on L2 to see what I mean). However, we can capitalize on these trends by staying a step ahead of the crowd using T&S and charts to anticipate what newer traders will do using L2.
- Realize that you can make or lose a fortune with or without L2, it's a timing tool for active scalp traders who look to make roundtrip trades in under 20 minutes. Time and Sales is important to have, so it may be worthwhile to have an L2 provider for T&S access.

**How and When to Use Level 2: More Tips**

**Examples:**

**TIP#1: Recognizing and acting on high-percentage vs. "indeterminate" market signals in Level 2**

We've already covered the high-percentage plays you need to be effective in using Nasdaq Level 2; for example knowing the difference between an L2 box that shows no trend vs. one that shows buying or selling direction.

**Pop Quiz:**

Which of the two Level 2 boxes on the right should you buy stock for, all else being equal?

- a) NETA
- b) WCOM
- c) Neither

MMID	Bid	B...	MMID	Ask	A...		
MLCO	23 1/2	10	ISLD	23 9/16	20	23 1/2	300
NITE	23 1/2	10	INCA	23 9/16	1	23 1/2	100
MADF	23 1/2	10	BTRD	23 11/16	5	23 9/16	1.00K
REDI	23 1/2	4	BRUT	23 11/16	5	23 1/2	400
MASH	23 1/2	3	MSCO	23 3/4	10	23 1/2	400
OLDE	23 7/16	10	LEHM	23 3/4	1	23 9/16	400
MSCO	23 7/16	10	GSCO	23 7/8	10	23 9/16	100
SLKC	23 7/16	10	NFSC	23 7/8	1	23 5/8	1.00K
BRUT	23 7/16	1	MONT	23 7/8	1	23 5/8	1.00K
ISLD	23 3/8	10	FBCO	23 7/8	1	23 3/4	2.50K
DEAN	23 3/8	5	HFZG	23 15/16	15	23 5/8	500

MM...	Bid	B...	MM...	Ask	A...		
REDI	45 3/4	33	INCA	45 13/16	40	45 13/16	100
ISLD	45 3/4	30	BTRD	45 13/16	30	45 3/4	600
INCA	45 3/4	20	MLCO	45 13/16	10	45 3/4	300
FCAP	45 3/4	8	MASH	45 13/16	10	45 3/4	9.00K
LEGG	45 3/4	5	DLIP	45 13/16	10	45 3/4	200
						45 13/16	100

- d) Both
- e) I don't know

FLTT	45 3/4	2	NITE	45 13/16	10	45 3/4	1.10K
MLCO	45 3/4	1	GSCO	45 13/16	10	45 3/4	200
DLJP	45 3/4	1	NFSC	45 13/16	7	45 3/4	1.00K
DBKS	45 3/4	1	AGED	45 13/16	5	45 13/16	100
SHWD	45 3/4	1	REDI	45 13/16	3	45 3/4	1.00K
JEFF	45 3/4	1	MONT	45 13/16	1	45 3/4	1.40K
MSCO	45 11/16	10	SLKC	45 7/8	10	45 13/16	200

answer: a) since there's not as many sellers as buyers And T&S is slightly biased to the buy side

The point is: don't buy or sell stock based on L2 alone, particularly if it shows an "indeterminate" pattern like the WCOM box to the right. Use T&S and chart TA to determine stock trend and entry/exit points, not L2.

In the WCOM example, now, if it had just tanked from 51 to 45 1/2, and was starting to get buyers back, then maybe I'd enter a long position for the bottom bounce. The L2 alone isn't enough. T&S is king, followed by 1-minute chart technical analysis patterns.

### Tip #2: Making the Market for a living Using Level 2

Chris Farrell's rather uninspired "daytrade online" book goes into this method for listed / NYSE stocks; I wouldn't try to make the market the way he describes - fortunately, our L2 does become much more valuable for this type of trading.

It's simple: find a stock that's trading in a channel (usually happens during lunchtime; though these are typically times where a stock weakens as well) - and enter a limit buy order at the current bid (either the inside bid or 1-2 levels outside), after you get filled then immediately offer it out at the ask.

This works only if you're trading 500-1K or more shares at a time; since your profit on teenies (1/16ths) is only \$62/1000. I try to scalp 1/8ths, which is \$125 per round turn per 1K shares. The key is to find a relatively liquid stock that's trading flat, using L2 and T&S to time your bids and asks.

This does Not work, of course, if you trade like new traders do, buying at the ask and selling at the bid, you're giving up 2 spreads this way, which is unprofitable. The only time you pay retail is if the stock is moving quickly and you want to exit fast - the retail exit is the fastest way to go.

Also play around with different order routing strategies in this type of trading, eg limit buy SOESing a mm or selectnet preferencing to see if you can get a price improvement. It's "fishing by selectnet" so to speak.

Most of the time, though, I'll just bid for stock at the inside bid (or 1/32nd higher if T&S is bullish), and then offer out at the ask immediately (or 1/32nd lower if T&S is bearish). These roundtrips should take no longer than 5-10 minutes maximum. Unless, of course, the stock is quickly headed up and you want to ride the momentum for a larger gain.

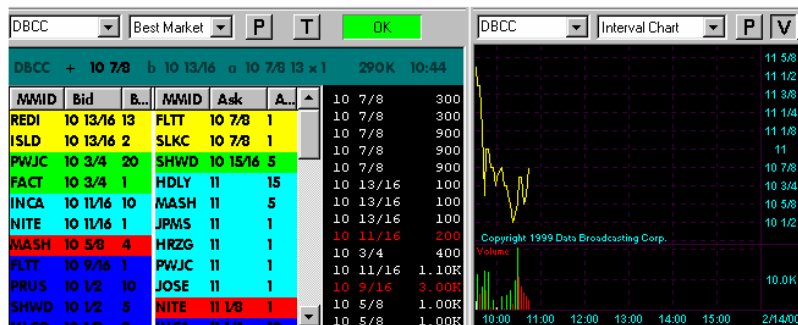
### Tip #3: Using L2 to trade Stocks in Motion

Stocks that are rapidly rebounding off a low (or making new highs via a breakout) are the two best plays to make.

Let's look at how L2 can help us recognize and make these trades successfully.

In this DBCC bounce, we see the low was at 10 1/2 (remember large fractions, the 1/4s, 1/2s and 3/4s) are typical pivot points for under-\$40 stocks in general.

We see lots of trades going off at 10 7/8, which is bullish. If I had entered at the 5/8 or so, I'd offer my stock out at 10 15/16.



Why? There's a lot of sellers at 11, so I want to be a teeny ahead of them, so I can exit my position. If the stock runs through 11, which is unlikely, I can always buy it again at 11 1/16th or so.

**This is an excellent "unknown tip" to follow: if you're long a position, sell right before it hits the whole number resistance.**

**If you're right and it falls back, great, you got the max profit out of the deal. If you're wrong and buyers continue, you can always buy the stock back at a teeny or an eighth over the whole number.** This is a great way to give yourself insurance in a trade. I seldom try to hold an under-\$40 stock through a whole number price level unless T&S is solid green and it's "running", I'll sell into the whole number buyers, and wait to see if the crowd pushes it higher. Sometimes they do, sometimes they don't. I want to "sit out" all low-percentage plays, and punching through whole numbers is low percentage. Particularly decade or fives, eg 20, 25, 30. Wall of bricks, since there's a lot of market stops/sell orders lined up at these whole number price levels.

**The reverse is true for entering a position on a bottom bounce, eg if it's tanking from 29 to 27 1/8, you might want to buy at 27 1/8 and use 26 15/16 as your stop. This is a high-percentage play that L2 can help you with.**

**Level 2 helps you to see these walls of support and resistance. Bounce scalps off them to profit.**

**More tips will be added in time; keep checking back as new momentum plays are developed and posted**

Worksheets

Module Two: Worksheet 1- Stops and Spreads in Level 2



- The Powerpoint worksheet below will help you learn how to set and keep track of your stops correctly using Level 2
- You should use both the 1-minute intraday chart support level And Level 2 to set your trading stops.
- Use Level 2 to determine the best stop by looking at the size of the bids at each price level:

1. It is usually best to set your initial stops no more than 3-4 spreads away from the current market.
2. Using the price spread on Level 2 that the "ax" trades at should give you an idea as to the trade potential. Eg, if SBSH is the ax trading AMZN and his Bid is 82 1/2 Ask 84 5/8 that tells you that your trade potential should be roughly 2 points, assuming you bought where the ax did on an uptrend.
3. If the bid levels start to shrink and T&S shows a string of trades going off at the bid, then sellers are in control and you should exit the position immediately.
4. If the trade is wiggling within a 2-3 spread range then watch T&S to see if a trend develops, if it doesn't then get out of the trade if the market (\$COMPQ, sector index) starts to go down.
5. If the trade goes your direction and more buyers come in, **set a trailing stop 2-3 spreads away from the inside market.**

**POP QUIZ Question #1:** Ok here's DELL, you just got filled on ISLD at 53 9/16 and SBSH is the ax. Where's your stop?

My stop is set at:

- A) I don't have one, DELL is a good company
- B) 53 9/16
- C) 53 3/4
- D) 53 3/8
- E) A and D above

Bonus Q: How wide is SBSH's "trade box"?

AMMID	Bid	B.	AMMID	Ask	A.	
ISLD	53 9/16	20	ARCA	53 5/8	30	53 9/16 100
INCA	53 9/16	14	ISLD	53 5/8	30	53 5/8 1,000
ARCA	53 9/16	10	NTRD	53 5/8	10	53 5/8 300
BEST	53 9/16	10	INCA	53 11/16	10	53 9/16 100
NITE	53 9/16	5	NFSC	53 11/16	10	53 5/8 700
MWSE	53 1/2	54	NITE	53 11/16	5	53 5/8 300
SBSH	53 1/2	10	REDI	53 11/16	2	53 9/16 100
SHWD	53 1/2	10	PIPR	53 11/16	1	53 5/8 1,000
RAMS	53 1/2	10	BTRD	53 3/4	214	
DEAN	53 1/2	10	MLCO	53 3/4	22	
MSCO	53 1/2	10	SHWD	53 3/4	10	
MADF	53 1/2	2	WARR	53 3/4	10	
SLKC	53 7/16	10	SBSH	53 3/4	8	
DLR	53 3/8	10	PRT	53 3/4	7	

**POP QUIZ Question #2:** Here's AMZN, you bought at 91 13/16 and MLCO's the ax. Where's your stop?

- A) 92 1/4
- B) 90
- C) 91 1/2
- D) I don't have one, I like AMZN

(Answers at bottom of this page)

M...	Bid	B...	M...	Ask	A...	
INCA	91 7/8	10	ISLD	92	22	91 7/8 200
MWSE	91 7/8	1	ARCA	92	12	92 100
ISLD	91 13/16	6	MASH	92	10	92 100
MASH	91 3/4	2	BRUT	92	6	92 400
NFSC	91 3/4	1	INCA	92 1/16	10	92 900
MADF	91 3/4	1	DKNY	92 1/16	1	92 100
REDI	91 9/16	5	REDI	92 1/8	2	92 100
SELZ	91 9/16	1	MLCO	92 1/4	9	91 15/16 600
JPM	91 1/2	1	MWSE	92 1/4	5	91 15/16 100
COWN	91 1/2	1	SLKC	92 1/4	1	92 100
SLKC	91 7/16	1	MONT	92 1/4	1	91 15/16 100
MSCO	91 1/8	10	NITE	92 1/2	20	92 100
STRK	91 1/8	5	MADF	92 1/2	11	91 13/16 200





**Pop Quiz answers:** For DELL, your initial stop should be set at D) 53 3/8 (or even a spread higher). DELL SSSH Trade Box is 53 1/2 x 53 3/4, only 1/4 point. For AMZN, your stop should be set at C) 91 1/2.

**Module  
Two**

Comprehensive Level 2 Trading Techniques:

Back to  
MODULE 2

Worksheets

Module Two: Worksheet 2- Market Maker Headfake Plays

- The Powerpoint worksheet below will help you learn how to avoid being taken advantage of by mm "headfake"-type trading



1. **I want you to develop an experienced, practiced eye for suspicious market maker activity** in this exercise. You will be examining your L2/T&S for the following

- Acting like a buyer when they're really selling
- Posting fake bid sizes to give the illusion of buying or selling support
- Flipping from the bid to the ask/vice-versa or fading back 2-3 spreads

2. Your primary guide will be "how strong and consistent is this trader's buying vs selling" as confirmed by a) the length of time he stays at the bid/ask in the face of buying/selling and b) the trades you see executed in the time and sales window.

3. Your objective is to learn to avoid getting suckered into "bull traps" and "bear traps" (making it look like there's buying/selling when there really isn't) and to better anticipate market maker direction

**You should use this worksheet (or a similar one you make yourself) to help develop your skills to correctly identify and avoid the most common and costly market maker headfakes that professional traders use:**





**Module Two: Worksheet 3 - Graphs, T & S and Level 2**

- The Powerpoint worksheet below will help you learn how to integrate all 3 sets of indicators: 1-minute graphs, T&S and Level 2 into your daytrading skill set.



1. Remember that you only want to risk your cash on "high-percentage daytrades", where several indicators line up, like the elevation and windage in a rifle scope, to give you an achievable target trade.
2. This worksheet will help you develop the discipline needed to complete a "mental checklist" of things to identify correctly before entering a trade.

**Use this worksheet (or a similar one you make yourself) to help develop your skills to integrate all 3 sets of indicators prior to buying (or shorting) a stock:**

**Directions:**

1. For one trading day, Choose 1 stock with good volume and volatility (over 1M/day volume and 5%+ intraday trading range) to follow intensely and look at the L2 window, T&S and 1-minute chart for.
2. You will be searching for when the technical indicators, L2 And T&S all tell you the stock is a buy.
3. Enter the details for Why each of these 3 indicators told you it was a buy, along with the actual price you would buy the stock at. (this is a papertrading activity)
4. Enter the stop you would set for the stock based on your 1-minute chart support level (or 3 spreads down from the buy price, whichever is smaller).
5. Finally, enter where you would have sold the stock at. NOTE: Your Exit criteria (when you sell/cover) can be based on something looking bad (an "early warning sign") in Any of the 3 indicators; your Buy criteria, however, should be when all 3 look good at the same time.

**Screensnap: Worksheet 3 - [Click here to d/l Powerpoint worksheet file \(43 K\)](#)**



Level 2 Combination Daytrading Worksheet		Goal: Improve my ability to identify when to buy based on all 3 indicators (L2, T&S, 1-min chart)
Stock Ticker: _____	What do you see Right Now that tells you it's a "Buy" using this indicator?	
The 3 Indicators:		Are All 3 Indicating It's a "Go"? <input type="checkbox"/> Yes <input type="checkbox"/> No Notes: _____
<b>1-Minute Chart:</b>		Price You Bought the Stock at: _____
<b>Time &amp; Sales:</b>		Price You'd Sell the Stock at: _____
<b>Level 2:</b>		Did you Sell <b>too Soon</b> or <b>too Late</b> ? (circle which one) (Note: you may nail the exact pivot 1 time out of 8 if you're lucky, don't worry about it for now.)



Worksheets

Module Two: Worksheet 4 - Shadowing the Ax - Recognizing and trading with the Market Maker Buyer



- The Powerpoint worksheet below will help you learn how to follow the lead market maker (ax) who is buying stock at a given point in time.
- This worksheet will help you figure out how to recognize net buying activity by a major market maker and to profit from this activity. You should buy a stock when you see a market maker buying in the face of weaker selling pressure, as the price will rise.

Use this worksheet (or a similar one you make yourself) to help develop your skills to "jump on board the train" and buy stock when a major player (mm ax) is also buying, so you can ride the momentum up for profit:

Directions:

1. **STOCK SELECTION:** Choose one stock you're familiar with and first determine if the stock is in a 5-day uptrend, downtrend, or flat and choppy (indeterminate) trend. You want to find a stock that's breaking above a key resistance level, not a stock that's in a downtrend (no bottom fishing for this technique, when you're first learning).
2. **MARKET MAKER AX RECOGNITION:** Next, Using your Level 2 window and Time & Sales, during the time period of 9:45 till 10:45, pick out "3 favorites" that you suspect may be the ax for the stock during that time period. Try and narrow it down to one market participant; learn how to spot who's buying it up.
3. What should you look for? See if, in T&S, you see either: trades going off at the bid and one mm is "holding the price up", or, preferably, you see the mm jumping up to the inside bid repeatedly as the price moves up several points, eg you see a major market maker "**chasing the stock**" on the inside bid.
4. **DAYTRADE PLAY & TRADE MANAGEMENT:** Ok, you think you know who is a buyer of the stock; let's now use that to profit. In the worksheet below, your papertrade exercise here is to see "how right you would have been", had you followed that ax in the trade. Mimic the mm ax's behavior, eg buy as he's buying, sell when he either drops away from the inside bid by a couple of levels or flips to the ask. How would you trade the stock based on what you're seeing?

## “Shadowing the Ax: When is he Buying?”

Goal: Improve my ability to identify when a market maker is buying stock so I can duplicate his trading for personal profit

Stock Ticker: \_\_\_\_\_

Which of the following market makers do you think is doing the most buying of this stock during a given 10-20 minute timeframe (one of the 'waves' in trading activity from 9:45-10:45)?

- \_\_\_ SBSH
- \_\_\_ GSCO
- \_\_\_ MLCO
- \_\_\_ MSCO
- \_\_\_ MASH
- \_\_\_ DEAN
- \_\_\_ HRZG
- \_\_\_ SHWD
- \_\_\_ PWJC
- \_\_\_ SLKC
- \_\_\_ DEAN
- \_\_\_ MADF
- \_\_\_ BEST
- \_\_\_ Other: \_\_\_\_\_

Notes: Remember, this works best for stocks that aren't as heavily traded on ECNs (eg ISLD, ARCA INCA). Also, pick a moderate-volume stock (600K-2M/day) priced from \$15-\$80 that's breaking thru a key resistance level or is in a steady uptrend.

At what Price did you see the mm **start to buy more** of the stock at? When?

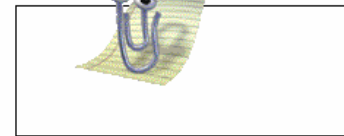
### Your Daytrading Activity:

How would you trade the stock based on this "buy pattern"? Would you join him at the bid, bid a teeny or 32nd more, or pay retail (inside ask) for it?

How many shares of the stock would you buy? 100? 200? 300? 500? 1000? 2K or more?

At what Price did you see the mm **stop buying** the stock at? When?

Once you see the market maker stop buying, how do you trade it? Do you exit the entire position immediately, do you wait, or do you scale out of the position (eg sell half now and wait)?



Did you Sell **too Soon** or **too Late**? (circle which one)

What's your Net Profit/Loss from the trade?

Activities

Module Two: Activity 1 - "Name That Ax"



- Being Able to Spot the Market Maker who has the most Buying/Selling Activity at a Given Point in Time on Level 2 Is an Important Daytrading Skill
- Following the ax is a relatively safe way to play stocks.
- This activity is designed to help you with your "ax recognition" and daytrading skills.

The GOAL for this activity is for you to be able to correctly identify who the "ax" market maker is in a given stock using your Level 2 screen.

**Directions:**

1. Choose 1 stock to watch all day in a Level 2 window that has an average daily volume >3million shares. Do not pick a DELL/CSCO/INTC etc. that has ask/bid columns 5-10 market makers wide; instead Choose a stock who's level 2 inside bid ask averages from 1-4 market makers wide with volume over 3Mil shares and an intraday trading range of at least 5% (eg \$1 on a \$20 stock).
2. Carefully watch the level 2 action: premarket, of the two, is it market makers or chippies on ARCA/INCA/SLD etc. the main player premarket? Which one is moving the price?
3. After the market opens, watch the stock for a half hour or so and see if you can determine which market maker is frequently on the inside bid or ask. Make sure to follow a major market maker like SBSH MLCO MSCO GSCO (not hrzg/silk etc).
4. Write down the following:
  - stock's closing price from yesterday,
  - today's opening price,
  - the name of the market maker you think is the "ax" for the time period you're watching,
  - number of times this market maker is at the "best bid" or "best ask" in a 2-hour timeframe (use a simple checksheet to keep track of this)
  - Which of the following important trading signals do you observe? A) The Market Maker is **Buying in Size** (he keeps refreshing his bid, and you see him buying more than 10K shares (or more than 12-15 transactions) in time and sales at the same price level); B) The Market Maker is **Selling In Size**; you see him stay at the inside ask and sell more than 10K shares at a given price level, **Headfakes and Switching** from the bid to the ask repeatedly (he's probably not the ax if he doesnt buy or sell a lot, jumping around).
  - Finally, develop a trading strategy based on your observations and consider buying or selling in response to the "ax's" buying and selling. Try to shadow the market makers' movement. Examples of axes I follow: SBSH for NOVL price movement, MSCO for SPLS.
  - Note that the ax may frequently change throughout the day, or from day to day. Look for whoever's buying or selling a lot of stock in a given timeframe, and follow that traders' lead.
  - Practice trading small sizes of 100-300 shares by following the ax after papertrading for several days with this ax. See how it works for you. Good trading.

**Examples:**

Looking at this Level 2 chart doesn't tell you much without seeing it "in action", but for now let's assume that GSCO is the ax on SBUX and is buying a lot of stock here. How would you trade it? Join his bid at the ask, use a larger size (or increment the bid by 1/32) to frontrun him? Wait? Check Time and Sales? It all depends on the price action and technical signals on your 1-minute SBUX chart.

Looking at this Level 2 chart doesn't tell you much without seeing it "in action", but for now let's assume that GSCO is the ax on SBUX and is buying a lot of stock here. How would you trade it? Join his bid at the ask, use a larger size (or increment the bid by 1/32) to frontrun him? Wait? Check Time and Sales? It all depends on the price action and technical signals on your 1-minute SBUX chart.

The immediate "battle" is between GSCO and whoever's selling on INCA (Instinet). The players line up under these two for the moment, no real strong mm's next to this action; SBSH and MLCO are each a couple of levels down. It's an indeterminate L2 window until we see a pattern of buying or selling in the time & sales window.

If INCA fades and we just have ISLD/NITE left, with GSCO staying strong you might BID SBUX 27 5/8 1100 shares or 27 21/32 500 shares etc. to frontrun. The battle goes on.

SBUX		Best Market		P	T	OK	
SBUX	+	27 5/8	b	27 5/8	a	27 11/16 10 x 44	2:13M 15:38
MMID	Bid	B...	MMID	Ask	A...		
GSCO	27 5/8	10	INCA	27 11/16	44	27 5/8	600
FBCO	27 5/8	10	ISLD	27 11/16	17	27 5/8	100
BRUT	27 5/8	6	NITE	27 11/16	1	27 11/16	500
STRK	27 5/8	5	DBKS	27 3/4	10	27 11/16	1,500K
NITE	27 9/16	1	SELZ	27 3/4	1	27 5/8	100
SHWD	27 9/16	1	DEAN	27 3/4	1	27 5/8	800
FLTT	27 9/16	1	SHWD	27 3/4	1	27 5/8	100
MADF	27 9/16	1	MONT	27 3/4	1	27 5/8	200
INCA	27 1/2	10	SBSH	27 13/16	10	27 5/8	200
SBSH	27 1/2	5	MLCO	27 13/16	10	27 5/8	300
MONT	27 1/2	1	LEHAM	27 13/16	1	27 11/16	100
JPMS	27 1/2	1	JPMS	27 13/16	1	27 11/16	500
CANT	27 7/16	1	MWSE	27 7/8	14	27 11/16	100
WBLR	27 7/16	1	OLDE	27 7/8	10	27 5/8	300
DBKS	27 3/8	10	MSCO	27 7/8	10	27 11/16	1,000K

## Module Two

### Comprehensive Level 2 Trading Techniques:

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## Activities

### Module Two: Activity 2 - "Finding T&S Support and Resistance"



- Next to "Being Able to Keep Small Stops", this has my vote for the Most Important Daytrading Skill to Develop
- Reading the trend of the sales going off in T&S is the best way to see what's really going with the stock's price movement.
- The **pace** (how many trades are going off, is it faster than it was 20 minutes ago?) as well as the **ratio & size** of trades going off at the bid vs. ask is important to keep an eye on.

24 1/2	500
24 7/16	100
24 7/16	200
24 7/16	1,000K
24 7/16	500
24 7/16	1,000K
24 7/16	200
24 7/16	200
24 7/16	200
24 1/2	200
24 1/2	500
24 1/2	100
24 1/2	100
24 1/2	200
24 1/2	500
24 1/2	100

The GOAL for this activity is to help you become skilled at determining when a stock's price is about to "pivot", or change and go in the other direction based on your watching trades go off in the time and sales window.

#### Directions:

1. Choose a stock to watch from 9:30 am til 11:00 am in a time and sales window. (By the way, I'd disable the "time" part of time & sales if I was you, there is no reason to see the time that a trade goes off at, it is distracting data that you don't want to have).
2. Keep an eye on the 1-minute tick chart as well, especially from 10:00am til 11:00am
3. At first, I want to encourage you to **just get a feel for the rhythm of the stock** during the different 10-20 minute cycles that it buys, sells, buys and sells. The rhythm means the pace of the trades, how fast are they going off? Are there big blocks in there (over 5K shares), or are they mostly 100-1K size trades? How fast is the tape printing?

24 1/2	500
24 7/16	100
24 7/16	200
24 7/16	1,000K
24 7/16	500
24 7/16	1,000K
24 7/16	200
24 7/16	200
24 7/16	200
24 1/2	200
24 1/2	500
24 1/2	100
24 1/2	100
24 1/2	200
24 1/2	500
24 1/2	100

4. Next, I want you to **look for directional trends** in the t&s display. How long does each "run" in one direction or the other last? Do you see "in-between" trades going off at a price in between the bid and ask, and is it signaling a pivot in the price?
5. The most important skill to develop here is to find the difference between a **"Real Directional Change"** in buying vs selling versus the **"noise"** of individual trades, or small flurries of 5-7 trades, that are part of the trading patter.
6. **As the stock gains momentum and you see more and more buyers (or sellers) coming in, try to estimate how long, and for how many spreads, the directional change will last in the time and sales window.**
7. Write down the following:
  - **specific times that you believe the stock is about to change direction as you watch the t&s window** (e.g. its 9:50 and, watching the t&s you think to yourself "ok I think it's going to head down now", so you write 9:50 NOVL going down on a pad of paper).
  - the **actual times** that it really did change direction that morning
  - **how far you think the direction change may be good for**, maximum (eg "ok NOVL's going down, based on chart support, L2 and t&s momentum I think it may be good for 3/8 point change maximum")
  - the **actual amount of price change** the stock went in the direction after the "pivot"

Over time, by practicing this way, you should gain a feel for the directional support and resistance using time and sales. "Reading the tape" is the most important observational skill you can develop as a trader; the "small stops" is the most important trade management skill you can develop.

Again, I would strongly recommend that you choose 2-3 stocks that you want to make a living daytrading from; you need a core of stocks that you know like the back of your hand. Some stocks are more difficult to trade than others, definitely avoid the most actives, as these tend to attract the best traders and have low-%aqe volatility. [See my latest 4-monitor esignal and cyberx setup](#) for a look at the stocks I was following in January 2000 (note: ARIA/TIVO were just plays for setup for a look at the stocks I was following in January 2000 (note: ARIA/TIVO were just plays for that day, some of the others like CIEN NOVL DCLK are my core trading stocks).

Your success at "tape-reading" is determined by your ability to correctly identify when the "tide is about to turn" in the opposite direction, so that you can a) buy bottoms and b) sell/short tops. Invest a lot of time in watching the tape for a couple of stocks you want to trade for a living, from 9:30am-11:00am and perhaps 2:30pm til 4:pm. Don't burn yourself out by watching the tape all day. Best wishes!

## Module Two

### Comprehensive Level 2 Trading Techniques:

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MODULE 2

#### Activities

#### Module Two: Activity 3 - "Reading the Outside Bid and Ask"



- As a leading indicator, it's useful to learn how to trade in response to the strength or weakness you see in the outside bid and ask bands in your Level 2 window. There's 2 patterns to watch for:
  1. **Seeing movement of mm's from the 1st outside level (green band) to the inside (yellow band) indicates that they want to lock in their buys/sells at this price level.**
  2. **The other pattern to look for is the width of the green band (number of market participants) either increasing or decreasing in response to a breakthrough or breakdown past a key support/resistance level.**

**The GOAL for this activity is to help you become familiar with how to look at the entire Level 2 window as a system, including the outside bid/ask bands. Of course, T&S is still the most important indicator. Use the activity of mms in the outside L2 bands as a secondary leading (early warning)- type trade direction indicator.**

#### Directions:

1. **Choose a stock to watch from 9:30 am til 11:00 am in a level 2 window**
2. Identify the "most important market makers" for this stock based on who's buying and selling on the inside (yellow) bands initially (with first preference given to MLCO MSCO SBSH GSCO, as usual).

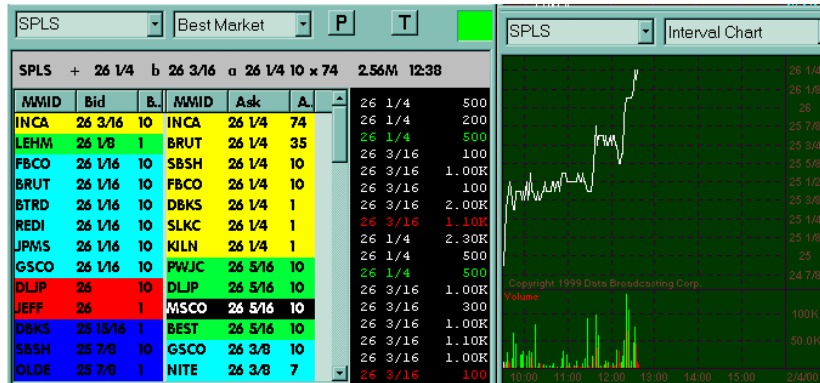
24	7/16	200
24	7/16	1,000
24	7/16	500
24	7/16	1,000
24	7/16	200
24	7/16	200
24	1/2	200
24	1/2	500
24	1/2	100
24	1/2	200
24	1/2	500
24	1/2	100
24	1/2	200
24	1/2	500
24	1/2	100



- The most important skill to develop here is to see how the activity of the market makers and ECN's in the green (1st outside) band affect the the short-term momentum trend of the stock price.
- This is yet another tool that you should add to your bag of trading tricks, it is yet another Level 2 trading indicator an experienced trader watches to help assess the momentum of the stock.

**Quick L2 trading example:** here you see a bearish setup as far as the 1st outside (green) band goes: LEHM bid 1 vs 4 market makers each offering 10 at the ask means I'd think this stock would go down to 26 1/16 before it will go up to 26 3/8.

Remember, it's dynamic, so respond with your trades in accordance with the patterns of buying and selling strength & weakness using charts, T&S and L2.



Of course, the selling pressure in the inside ask is also bearish, and T&S is mixed, so it's pretty obvious in this example that the stock will retrace a bit. For your stock, check the pattern in the green band to see where the other traders are lining up their bids and offers, using it to help time your trade entries and exits.

## Module Two

### Comprehensive Level 2 Trading Techniques:

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#### Activities

#### Module Two: Activity 4 - "When the Market Maker Flips Over"



- Often times you'll see a market maker flip from the inside bid to an outside ask level, or vice versa. This indicates he's "through" with the stock in the direction he was playing it, for the time being (maybe a few minutes or so), and gives you an indicator that you might want to bail out of the trade at that time.
- Once a market maker has finished selling (or buying) for the moment, you can mimic his trade direction, again with confirmations from T&S and your 1-minute charts, to gain a momentum edge on other traders.
- As always, be careful to watch the tape, as he may be fooling around with posted bids/asks to give the appearance of buying or selling when his true direction is routed through an ECN, however this isn't as likely for the 4 major mms we've discussed: MSCO MLCO GSCO SBHS.
- Below is a rough animation of the pattern to watch for: MLCO was on the ask (looking like a buyer), then he flips over the ask (now he's a seller); if you're in long then you might want to consider selling as well, if the T&S confirms net selling.

Notice how MLCO flips over to the ask in this rough animation we constructed. If a major mm like MLCO and both major ECNs (ISLD/INCA) are selling, I wouldn't be holding long here.

NETA		Best Market		P	T
NETA - 23 1/2 b 23 1/2 a 23 9/16 10 x 20 1.38M 12:35					
MMID	Bid	B...	MMID	Ask	A...
MLCO	23 1/2	10	ISLD	23 9/16	20
NITE	23 1/2	10	INCA	23 9/16	1
MADF	23 1/2	10	BTRD	23 11/16	5
REDI	23 1/2	4	BRUT	23 11/16	5
MASH	23 1/2	3	MSCO	23 3/4	10
OLDE	23 7/16	10	LEHM	23 3/4	1
MSCO	23 7/16	10	GSCO	23 7/8	10
SLKC	23 7/16	10	NFSC	23 7/8	1
BRUT	23 7/16	1	MONT	23 7/8	1
ISLD	23 3/8	10	FBCO	23 7/8	1
DEAN	23 3/8	5	HRZG	23 15/16	15

The GOAL for this activity is to help you learn to spot reversals (or pivots) in price direction based on what you see a major market maker doing when he flips from being a buyer to a seller (or vice versa) on the inside bid/ask of a level 2 window.

#### Directions:

1. Choose several stocks to watch from 9:30 am til 11:00 am in level 2 windows.
2. Identify the "most important market maker" for these stocks based on who's buying and selling on the inside (yellow) bands initially (with first preference given to MLCO MSCO SBSH GSCO).
3. See if you can detect any reversals in market makers' bias towards buying or selling, based on their "flipping" back and forth from the inside bid and ask.
4. As we saw earlier, you can also look for trends in where they are playing their trade box, eg if they drop their bids or raise their asks etc. This activity is to help you see abrupt pivots, or directional changes, in their buying or selling activity.
5. One more of the market makers' behaviors exposed for our DTU traders!
6. After seeing a reversal, follow the T&S to see if it holds, and to see if the market maker himself stays true to his reversed position for any length of time. Sometimes, they are indecisive and may flip back and forth, but they will usually hold through at least a spread or two of direction before changing from being a buyer to a seller or vice versa.
7. Once you've identified a pivot that holds true, see if you could papertrade it accurately, would you join the market maker in his now-changed position in the stock, and if so, will it hold long enough for you to make at least a few spreads' profit by it?

- Seeing pivots and momentum pauses in Level 2

● **Main Points:**

- In addition to charts, your Level 2 window can also be helpful in **identifying where the price trend is about to change**, either with new buyers coming in for a bottom bounce or selling at a top occurring, before the price drops.
- **Pivots:** occur when the sellers are finished and new buyers come in to buy a stock that looks oversold; or, conversely, when buyers are finished and everyone wants to take profits, where the stock looks overbought.
- **Momentum Pauses:** occurs right before a price trend pivot, where the buying and selling pressure is about equal. Uncertainty before the run (either up or down) is a good time to enter your trades, if you can read the tape correctly.
- Momentum Pause price action is sometimes seen in time & sales as **"in-between" trades** going off between the current bid and ask, for example if the inside looks like 41 1/4 x 41 3/8, you may see people splitting the bid at 41 5/16. This is one possible indicator of a pending change in direction of the price trend.
- One thing worth noting is that these plays are for bounces and tops that are **extreme**, eg usually characterized by a **change of at least +/- 5% for the stocks' price action**...when you have your portfolio tracker open these are the plays for the stocks at the ends of the spectrum, who have either gained or lost quite a bit on the day (eg shorting a top of a stock that's up +14%, or attempting to bottom-fish a stock that's down -7.2% etc). These pivot and momentum pause plays are **not for stocks that are in a trading range**, rather it's how to identify the "turning points" with a fair degree of accuracy on the extremes. As always, use small stops.

## Level 2 Pivots and Momentum Pauses

**Examples:**

Buying bottoms and selling tops is almost impossible; however, you can use Level 2, Time & Sales, and risk/stop management to profit off of these corrections in stock prices. It takes practice and attention to your L2 windows.



Don't even try to nail the tops and bottoms exactly, the best I've done on average is 10-15% of the time for nailing it within 1/16th. The main thing is to take a piece of the action consistently, using small stops, eg if you buy what you think is the bottom, make sure to sell if back if you're wrong and the stock goes against you another 1/8th or more. DELL on Feb. 8th 2000(above right chart) is a good example; it kept selling off to around -6% before rebounding later in the day.

Let's look at how to use Level 2 to help identify where these pivots and momentum pauses occur:

**Pivots:** When you see one side (bid or ask) stacked heavily in one direction a pivot may be about to happen. Note that in this PAGE L2 box the inside (yellow) buyers are stronger than the inside sellers and the majority of the trades going off in T&S are at the ask, a bullish sign.

I would be careful with this one, however, since the 1st outside (green) band is much stronger with sellers.

**Identifying the pivot:** using t&s and the relative speed and price momentum of the trades is helpful, as is the mm movement within the bands. For example, you can see MLCO and MASH are buying here, but are making the market at 3 7/8 offered. Daytrader sentiment seems bullish, as we have 179 bid ISLD vs 10 ask. And, as I've mentioned numerous times, HRZG's large sizes are almost always fake, so ignore them.

MM...	Bid	B..	MM...	Ask	A..		
ISLD	3 13/16	179	ISLD	3 27/32	10	3 27/32	100
HRZG	3 13/16	117	BRUT	3 27/32	9	3 13/16	1.00K
MLCO	3 13/16	20	SBSH	3 27/32	9	3 27/32	500
ARCA	3 13/16	15	HRZG	3 7/8	193	3 27/32	800
MASH	3 13/16	10	MASH	3 7/8	50	3 27/32	1.50K
PRUS	3 13/16	10	STRD	3 7/8	50	3 27/32	900
BRUT	3 13/16	9	SHWD	3 7/8	43	3 13/16	400
SLKC	3 13/16	1	INCA	3 7/8	30	3 27/32	1.00K
SHWD	3 25/32	1	MLCO	3 7/8	20	3 27/32	1.00K
MADF	3 3/4	23	MADF	3 7/8	17	3 27/32	1.00K
PWJC	3 3/4	10	REDI	3 7/8	15	3 27/32	1.50K
						3 27/32	1.50K

**Daytrader's Play:** Watching the price action in T&S as we've learned in earlier lessons, keep an eye on where, within the yellow and green bands, the major market makers are placing their bids and offers.

They are experienced traders and are always fading in and out of positions at different sizes. (eg MLCO may have been a buyer at 3 3/4 through 3 13/16, and wants to sell several hundred thousand shares from 3 13/16 up through 3 15/16, for a sizable profit. In terms of pivots and L2, watch for clues by seeing the width of the 1st outside (green) bands as a leading indicator, and watch to see if the major mm's are flipping from one side to the other.

You may be relatively safe joining the ISLD bidders here at 3 13/16, or even paying up 3 27/32; with a stock like this I'd sell it if we got down to 3-4 market makers at 3 13/16, though. Losing traders would hold the position down to 3 5/8 or something and hope for a turnaround. Get out fast in fast-moving high-volume stocks on pivots like this one.

**Momentum Pauses:** Again, these are where buying and selling pressure is about equal, right before the pivot occurs.

In this T&S box for DELL you can see that the inside bid and ask depth is about the same, with 7 players on each side. More importantly, you can see a number of "in-between" trades going off inside the spread, at 37 3/32, 37 5/64 etc. If this keeps up, you will slowly start to see the trend slip in one direction or the other.

If, for example, we see trades going off at the ask, 37 1/8, and the number of players on the inside ask start to drop you might want to jump on board and hit the ask before it rolls up to 37 1/8 x 3/16. Even better, just try bidding with the "in-between" bids at 37 3/32 to get a fill for any last-minute sellers.

Watch also in T&S for a relative slowdown in the pace of trades going off, and watch your 1-minute chart to see what's going on with the volume. Fading volume tends to precede a change after a big directional move (either up or down), as 'that crowd'/sentiment wears down, before the direction change occurs.

M..	Bid	B..	M..	Ask	A..		
ISLD	37 1/16	69	ISLD	37 1/8	33	37 1/8	100
INCA	37 1/16	39	NITE	37 1/8	10	37 1/8	800
REDI	37 1/16	20	NFSC	37 1/8	10	37 1/8	100
COST	37 1/16	10	MADF	37 1/8	8	37 1/8	1.00K
SBSH	37 1/16	10	MWSE	37 1/8	1	37 1/16	100
FLTT	37 1/16	5	PRUS	37 1/8	1	37 1/16	1.00K
RSSF	37 1/16	5	ATTN	37 1/8	1	37 1/16	100
MASH	37	19	RSSF	37 3/16	10	37 1/8	200
ARCA	37	10	ARCA	37 3/16	10	37 1/8	100
MWSE	37	10	MASH	37 3/16	4	37 1/16	200
GSCO	37	10	INCA	37 1/4	20	37 1/8	300
SLKC	37	10	REDI	37 1/4	5	37 3/32	100
						37 1/8	1.80K

**Daytrader's Play:** Pivots are dangerous to play, as the trend is 'usually but not always' your friend; the stock may pivot for 1-2 spreads and then reverse back to continue it's original direction.

Keep especially tight stops when you're going against the trend waiting for a reversal, as these are tougher to play than other types of daytrades. When done well, you feel great, and they can be highly profitable. You may need to take several small stops "on the way down" before finding the real bottom; that's fine, just remember that your odds are better when you're playing pivots on extreme moves.

Of course the best pivots are to short huge gaps up on open and buy huge gaps down on the open (huge meaning over 11-15%); again they are dangerous though.



How long it takes you to get from the "land of confusion" through the learning curve and into your personal "trade zone" varies by individual, aptitude, effort and skill. Many people will never succeed at daytrading, looking at it like gambling and not willing to put in the hard work, determination, patience and practice it takes to be consistently successful.

A fair number will do okay, and a handful of dedicated people will be able to make a living at it. The ones who can daytrade for a living will be those who look at it like a career change, recognizing the need for training, patience with themselves, and a curiosity to learn new techniques. It is not easy to daytrade for a living. It can be done, but you have to be willing to work very hard at it. Reading the popular books is maybe 15% of what you need to do to succeed.

Most of it is market-watching, learning financials, doing daily research (IBD, Clearstation, Bigcharts, CBSMarketwatch), learning the technical aspect of intraday trading the financial markets, learning how to short stocks, and other skills we continue to cover here at DTU. I want you folks to make it, just realize the learning curve is much much harder than the books make it out to be.



## Eliminating Your Barriers to Successful Daytrading

### Identifying and Getting Rid of Common Barriers Is an Ongoing Key to Trading Success:

- **Barrier #1: Lack of Disciplined Trading Attitude and Mindset of a Trader:** To win at this game, you need to follow the rules (such as keeping tight stops) and see yourself as a trader. When I first got started, I put clippings from guys like Serge Milman around the office. A photo of the ferengi trader from star trek. Anything it took to get myself thinking like a trader: to buy at one price and sell at another price for profits is what I must learn to do for a living. My success is measured by my P&L at the end of each day.
- **Barrier #2: Not investing the time and resources to do the job right.** Get at least 2 monitors, a good broker and quotefeed etc. etc. It's much cheaper in the long run. Having 4 monitors is great.
- **Barrier #3: Not being serious enough about daytrading as a profession.** Some losing traders are more like gamblers, playing \$5 low-volume stocks and trying to make a fast buck. They lose. You must take this game very seriously if you are to take money off wall street. You're in competition with professionals; you must think like and trade against other professionals to make a living at this.
- **Barrier #4: Having no trading plan or entry/exit strategy for your trades.** Make sure you have predetermined entries/exits etc...common sense but when was the last time You updated your trading journal? See the ones I developed for you in Module 1 as a starting point; develop your own.
- **Barrier #5: Physical daytrading environment not conducive for success:** We'll look at this in detail in another lesson, for now, make sure to have a quiet, well-lit uncluttered trading area to work from. Use an ergonomic keyboard, change your cursor/mouse pointer icons, experiment. Keep CNBC (and the wife/girlfriend) muted when you're in a trade, or setting up for a trade.
- **Barrier #6: Hesitancy to get in a good trade & staying in bad trades too long:** My average trade time decreased from 30 minutes-2 weeks when I started to around 10-15 minutes now. I miss on big runs up, but I like to scalp for 3/8s to 1 1/2 points profit many times a day now. If a trade is saying "buy me" then follow that signal. It's much better to miss a good trade then to force low-percentage trades, though. Marketwatching is what I do 98% of the time, 2% of the time I'm trading. Be a sniper looking for targets of opportunity.
- **Barrier #7: Not managing your physical readiness for daytrading:** No I don't just mean drink a pot of coffee, even though I guess that's ok too. Daytrading is highly demanding physically and mentally. Take breaks frequently during the day (especially during the lunch deadzone, look for stock picks then), refocus your eyes on something far away to relieve eyestrain, splash water on your face now and then, stretch, drink lots of water/take vitamins, have some carbohydrates prior to the day's trading (I always eat a microwaved baked potato or have some rice and eggs etc.), keep yourself fit by walking around the block or something

a couple of times a week, whatever works for you. Daytrading is like being an air traffic controller, always monitoring gauges and looking for signals, then responding. Refresh yourself. And, take a day off now and then. Sit out flat/choppy days. The market will be there tomorrow. Keep fit.



## Getting Into Your "Trade Zone"

Successful daytraders have several things in common. Let's look at the actions you can take to get into a profitable "trade zone":

1. **Learn how to filter information quickly:** you need to develop an experienced eye for what is worth paying attention to (eg shorting the gaps up on open, playing the days gainers/losers correctly, news plays, chart & level 2 signals etc.). There is way too much financial information available; learning to quickly identify what is potentially profitable from a daytrading standpoint is an important skill to develop.
2. **Keep tiny small stops:** although I say it way too much it's the number one daytrading skill to master: taking a few small scratches so you can profit from large runs is critical. It builds confidence; eg I may take 3 1/16th point stops while trying to find a bottom before it rebounds 1/2 to 1 1/2 points; that's great. I walk away a winner. Stops should be no more than 2-3 spreads max (I usually use 2 spreads w/a micro look at the 1st outside bid/ask).
3. **Post your winning trades around your trade area:** when I got started, I'd always print out an intraday chart of my winning trades and use a green felt market to circle where I bought, where I sold and how much I made circled, such as +262 for the # dollars I made. It's important to keep visual reminders of your successes. Document your bad trades in your trading journal and look for common threads (like the types of stocks you played, the time of day and number of shares you traded etc.). Standardize what is winning for you.
4. **Develop daytrading goals and a trading plan you believe in:** having goals that you believe in is a powerful motivator (read Tony Robbins' stuff); now when I asked you for your daily average profit target I mean how much do you want to earn on an average day, not a mandatory daily target. Some days you shouldn't trade at all. On other monster days you should trade very aggressively, as your net risk is lower. It's important to identify your goals though, starting with a profit target, so you can budget for living expenses etc. Also develop **daytrading process goals**, such as "I will try to make between 1 and 2 trades per day for each day of the next trading week if I see a high-probability daytrade in front of me", or "I will keep a 2-spread stop maximum on my next 10 trades" or "I will update my trading journal each Saturday morning" or "I will not make a trade unless both the \$TRINQ and \$COMPQ confirm that market direction is headed my way for the next 5 trades.
5. **Share your daytrading progress with family and friends:** tell people about what you've learned, or at least that you're learning new things each day. Share your trading progress, for example you could say "I've lost some, but I'm getting better, I averaged \$160 profit on each of my last 3 trades" etc. Find supportive friends/family to share your trading activity with. Avoid toxic people.
6. **Know when to hold and when to fold and when not to trade in the first place:** some days aren't good for you to trade on, even if the market's great. Maybe you're not in a good mood. Or you have a hangover. Or you had a fight with your wife/friend/boss etc. Don't trade on those days; just watch, learn, or take a break. Regroup, perhaps take a few days off. For learning, I find going to the beach, park or library is a nice change of scenery; you may be re-reading a daytrading book but somehow reading it in a different place causes you to pay attention better. Try it.
7. **Read daytrading books often:** My favorite book for getting encouragement is Friedfertig's "Secrets of Successful Daytraders", followed by Schwager's "New Market Wizards" and Patels' "Mind of a Trader". For the mechanics of daytrading successfully, I like Tony Oz's "Stock Trading Wizard". Find books that you believe can help you, highlight them with a college-type highlighter, and translate the concepts into specific trading strategies in your personal daytrading plan.
8. **Find other daytraders in your area to network with.** A great example is "Daytraders of Orange County", now [www.worldwidetraders.com](http://www.worldwidetraders.com); they have emails of other traders in your area of each state (or call a local broker and see who they might know). Attend occasional meetings for energy, ideas, sympathy, and learning. Daytrading can be the world's most lonely profession, so it's important for you to connect with other traders. The chatrooms are an okay social substitute, but most do not post good calls.
9. **Commit to your personal success at daytrading.** Say to yourself out loud, right now, "I am a trader". There now that wasn't so hard was it? If you laughed when you said it you need to keep saying it til ya believe it. Now say "I trade for a living. I'm serious about it". Finally, say out loud "I will be persistent and keep at it until I learn how to daytrade for a living. It might take awhile, but I will get there in time. As I improve my trading skills, I will expect to make higher profits, which I will spend on (your choice)." Clearly identify personal benefits to daytrading.
10. **Make a list of helpful daytrading behaviors for your trading style:** jot down what you do and how you feel when you're in common daytrading situations: doing research, looking for a trade, when you're in a trade, how it feels when you exit with a nice profit, how you feel when you take a stop. See what thoughts are going through your mind in each of these situations and what you can do to deal with it the best you can. It helps.



These tips should help your trading results, let me know how they work for you.

- Developing the Skill, Patience, Discipline and Attitude to Succeed at Daytrading

● **Main Points:**

- A combination of "Successful Trader Characteristics" exists that all of us need to continually work towards improving.
- If you want to succeed at trading, you have to make a personal commitment to look at things from a different perspective, and to change some of your habits and viewpoints. "If you always do what you've always done you'll always get what you've always gotten". I assume you want to gain financial independence, or at least healthy profits for all the learning and work and dues you've paid, right?
- It is not easy to change and improve one's skills, in any endeavor. A particularly challenging field like "becoming a surgeon" or "trading the financial markets" or "getting into a great marriage" takes a lot of sacrifice and hard work.
- Professionals, those of us who do this to pay the rent, have invested hundreds of hours of our time and many months of intensive effort to prepare and learn how to do this right. Months of determination and expectation of success is needed. Few will have the energy or patience to make this part of how you make your living. Again, look at it as a regular college program, but tougher. You have to commit the time and energy to it.
- This lesson will ask you to do a **self-assessment** (which you might want to re-take in a few months) to help you identify your temperament and current progress for being an effective trader. Identifying areas for improvement can help you focus your energy more effectively on those things you should strengthen. It's a journey, we're always striving to improve all of these.



How Can Each of These Help You Make Profitable Trades?

**Patience:**

- To not chase stock or enter bad trades out of boredom
- To let a good trade mature, not taking profit too soon, too small.

**Discipline:**

- To get out of bad trades quickly instead of riding them into the ground, losing or tying up your capital.
- To take healthy, regular profits out of your winning trades.

**Trading Skills:**





## Trading Skills

**#7.** I am a good technical analyst, and can describe to others when and how to use chart patterns, and at least 3 indicators (RSI, Stochastics, MACD).

**#8.** I know how to scale up and fade out of positions regularly, I add to and sell off partial positions according to market momentum.

**#9.** My trade execution and routing skills are solid, I can enter and exit round trip positions quickly and via the right ECN/Selectnet routes.


## Personal Attitude

**#10.** I realize that to become successful at trading, I need to take a stone cold professional non-emotional approach to the markets and am continuously working to refine my professionalism in trading skills.

**#11.** I fully expect to be consistently profitable at trading, given time and practice, and am not treating this like a gambling-type activity. I have committed to not repeating my mistakes.

**#12.** I know that it is critical for me to develop the ability to take small stops, and I am able and willing to not ride positions down "hoping they'll come back someday", or committing other basic trading errors. I expect to win.


**My Score (120 Max Points Possible): \_\_\_\_\_**

### Traders' Self-Assessment Scoring Key:

**120-100: You have all the right stuff** (or at least you say you do!), you should be consistently profitable and making a healthy income from your trading activities. Be sure to maintain your successful habits so that you don't "backslide"

**80-100: You're a solid trader with some useful skills that you've developed.** While you seem to have excellent skills in some areas, other areas need improvement. Spend some time focusing on how to build those areas that you gave yourself low marks in. Frequently, traders will tell me that they're good in several categories but may be weak in the "Patience" department, which costs opportunity (eg taking profits too soon, while they're only 20-30% of the max available). Slowly build up the skills.

**50-80: You've got a good basic start** on some of the skills that are needed; however it takes awhile to get highly successful. Be sure to practice with small shares (eg 100-share lots) so that you learn the mechanics of how to trade, and you become aware of how to manage your emotions and build trading discipline over time. All is not lost - this is a good place to start from.

**12-50: Have you considered a nice mutual fund?** I hear Vanguard and Fidelity have some good ones, you can let them manage your money for you without worrying about all this trading stuff! Of course, I'll make more %age in a week than they they do in a year, but hey! That's their job right?

I hope this is a useful assessment for you; keep working on those areas you feel are limiting your trading profits, place reminders around your trading area, and good trading!

- What you should be doing first thing in the morning before the market opens

● **Main Points:**

- In addition to all the information we have from the original Module 1 page on "[A Day in The Life](#)", which you should take a minute to review now, there are a few other things we should consider prior to the market's open.
- The focus of this lesson will be on the mental preparation that I encourage you to get in the habit of doing prior to each new trading day.



**We've already said you should do the following:**

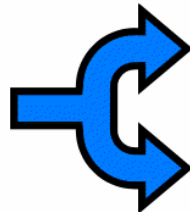
- turn on CNBC to see what the futures are doing and listen to the talking heads
- you've scanned the headlines at <http://www.cbs.marketwatch.com>, I also look at [jagnotes.com](http://jagnotes.com) to see what the latest up/downgrades and commentaries are
- you've got your computer on and all your quote/broker software is set up correctly.
- you've put potential "daily picks" in your watch portfolio to keep an eye on
- you've looked for premarket gaps on volume of at least 20K shares.
- you've already eaten something for energy and maybe have some coffee. You definitely need a large (16 oz) glass of water by your side throughout the trading day, the brain works hard and stimulates thirst during trading, water is better than coffee, though I drink both.

**What's next?**

- Your game. The mental frame of mind that you should put yourself in prior to trading. Let's see how it should work

The first thing you should be asking yourself is:

**Am I Really Ready to Trade this morning?**



OR



If you're not in the mental frame of mind to be an active trader on one particular day, don't push yourself. Take a rest, take a break. Do not feel pressured to trade.

**Trade only when you can devote 100% of your mind and body to the trade;** anything less will usually result in losses.

Ask yourself each morning: Have you done your research, do you have 3-5 likely picks in mind, and you're alert and ready to trade? If the answer is no, then go for a walk,

come back and do some research, and decide again whether you are going to trade that day. It's fine to take an occasional day off, in fact I recommend it.

### **Premarket Checklist of "Mental Things to Do" To Get Ready for Daytrading:**

*Here's a few 'mental reminder'-type favorites that I find helpful, hopefully some of them will benefit you as well.*

1. Tell yourself that your [trading is your business opportunity](#) to provide for your family and yourself. It is not a casino. You should fully expect (not hope) to make money in my trades. For myself, I am running a small SOHO (small office/home office) business here, and I take it seriously. [I trade to pay the rent.](#)
2. Reviewing the market and sector indexes for the past 10 days, while listening to the CNBC commentary, I [start to put together a "mental map" of likely trade opportunities](#) before the market opens. I develop several "IF- THEN" scenarios.
3. [I'm watching my L2 and Time & Sales tickers for the sector lead stocks](#) to see if I can gauge the market sentiment in each sector....are they buying, chopping around, or selling?
4. I try to [find calm](#) in the frenzy of market activity. It is easy to get overwhelmed by the data out there, the key is to assess it professionally and focus on high-percentage likely trades.

Calm used to be difficult, after trading profitably and consistently the calm comes, it's more a matter of "not being surprised by anything the market does"...you look at the charts, the momentum, and in a relaxed way say to yourself, "nah - still waiting" or "almost ready" or "this is a good trade, I should pull the trigger here"....

After a while you get that sense of when the trade is a correct one, you don't think you're guessing. And if you're wrong, [your small stops save you](#) and you look for a better entry. Or a better trade somewhere else.

5. I fully realize that [my success depends on my ability to get in and get out fast](#), with small stops and larger profits. This ratio, adjusted for brokerage costs, must be maintained for me to be able to do this for a living. Tightening up the trades for the day is important. For my occasional [swing trades](#), like VISX HRL DBCC CCL T LU HET SPLS etc, I realize that my success depends on my [ability to be a decent chartist](#), and to roughly know where the market will take a stock based on oversold/overbought/volume and other technical indicators.
6. [I use analogies that are familiar and comforting to me, like golf.](#) I will see a trade like winding up to drive the ball down the fairway. What do I need to do to avoid missing my target? What bad golf and trading habits cause me to miss out? I focus on the 'zone' I need to be in, those moments of clarity and understanding that can only be reached by knowing the stocks you trade like the back of your hand.

For example, I am writing this at 3:50EST, right before the close, on Monday March 27th, 2000...I saw SPLS drop to 20 x 20 1/16th with a wall of L2 support at 20. I just bought a truckload of SPLS at 20 1/16th and fully expect to swing trade it to sell at 21 1/2 or better sometime within 10 trading days. I did this nonchalantly and am back writing this 2 minutes later. I am calm. I know I will profit. Because I trade this stock for a living, I fully expect to make lots of money. It's easy, when you know what you're doing. Notice that from a chart/TA standpoint the last thing you should do is buy a downtrending stock with no volume reversal. But, like AT&T anywhere under 50, I know that SPLS at 20 is always always a buy. So, I'm glad I'll be adding some more profit to my p&l.



### Premarket Game Activity: Ready - Set - Trade!

In the fast-paced, high-stakes world of online trading, your ability to think and act fast is an asset. Before the market opens, you might want to consider using a stopwatch to 'time' various things you are doing, to get in the habit of click-on click-off time-based activities. It's a fun way to get yourself in the right frame of mind to do things quickly, and will train you to think in terms of faster paced action that is needed to daytrade.

### Premarket Stop Setting:

Pick 4 stocks you will watch carefully throughout the morning trading session. For each stock, take a minute to write out it's closing price, the 5-day support and resistance levels, and the maximum stop that you will take - for example if you are trading AOL and decide to buy on strength at 67, you might want to have a 3/8 point stop.

Write this out ahead of the day's trading for the stocks you will most likely be trading, so that you will take small stops more automatically, without thinking about it during a live trade situation. You've already mapped out your trade plan and have identified your stop loss.

Also identify where you will sell it at if the trade goes your way - I like to use previous 5-day resistance areas as places I look to exit a position at. If it breaks through the resistance line, I may buy it back after it consolidates and holds.

## Module Three

### The Mental Game of Daytrading:

◀ PREVIOUS   NEXT ▶

Back to  
MODULE 3

- **Creating a Successful Trading Environment: What to Put Near Your Monitors"**

#### • **Main Points:**

- From my previous consulting work with over 137 companies worldwide (sales training, management & quality consulting etc.), I can say with certainty that your work environment, in this case your trading environment, can have a significant impact on your likelihood of success.
- In general, successful people surround themselves with a successful place to work. This includes not only the physical layout and organization of your workspace, but perhaps more importantly the people & other support resources you have around you.
- For successful trading, your tradestation and work environment could probably use some minor enhancements that will encourage and motivate you to make more effective trades.
- Some traders enjoy being in a room with 5-30 other daytraders. Personally, I like trading from a quiet living room workspace at home with plenty of space around me.
- This lesson will help you look at ergonomics, layout and other things to place around your personal computer to help you improve your trading results.

## A Successful Daytrader's Work Area:



### Your Personal Daytrading Workstation Area: **ERGONOMICS**

- **Multiple Monitors:** definitely get at least 2. I have 4, but you can do fine with 2 or 3. Get the largest ones you can afford, 17" minimum. Get a fast CPU (>P2350).
- Get an **Ergonomic keyboard** (non-microsoft) and **wrist rest** for your mouse pad: makes a big difference. I use a legal pad for a mousepad with gel wrist rest.
- **Chair:** get a swivel one with arm rests. Do Not get a \$20 swivel chair with no arm rests, these are bad for extended sitting times.
- Make sure to **angle the monitors** so there's no glare or reflection from outside light or internal lights, and angle the monitor faces so your neck is comfortable.
- Be sure to have adequate **ventilation** and that the room is not too hot or cold.

### Your Personal Daytrading Workstation Area: **SUPPORT & ENCOURAGEMENT**

- We all know that hope, greed and fear are what causes trading losses (be like Spock, completely logical, following predetermined rules, stop losses and techniques. For fun, go to a casino. Daytrading is hard work, we're in this as a business). Here's how to keep things successful for you in terms of your mental preparation and what to have near your trade station:
- First, make sure to have something like "Tight Stops - No Exceptions" taped to at least one monitor.
- Second, use encouraging success & motivational products, posters and other reminders on the walls of your house/apartment where you can see them. See [www.successories.com](http://www.successories.com) for ideas. Rotate these things every few months.
- Third, **make copies of intraday charts that you made successful trades in** (or screensnaps of your winning trade confirmations) and tape these to a board on your wall. I use the 3/16th inch thick 3' x 4' foam presentation boards available at office supply stores to mount things to at my home office.
- Fourth, by **analyzing your trade journal**, find out what is helping you and what is hurting you and **put reminders of these things near your monitors**. Examples: "Don't trade from 12 - 1" "Don't trade more than 500 shares". "Wait til the momentum starts to turn, then sell" "Small stops keep me trading - no more than 3/8 against me" etc.

### Your Personal Daytrading Workstation Area: ORGANIZATION

- "A Cluttered Desk is..." well, messy and mentally frustrating. Keep your desk area as **clean** as possible. Hint for the chronically untidy (like me): at least keep your primary trading area clean of all clutter, and put all your papers on another coffee table or the floor; anywhere out of your line of sight. While trading, make sure your monitors, keyboard, clock and mouse are all that you are seeing. **Daytrading requires a lot of mental focus and concentration, make it easy on yourself by putting unnecessary papers and the like out of the way where you can't see them.**
- **Put the TV behind you** (or off to a side behind you); do not distract yourself with too much CNBC. I like watching it too, but it's silent whenever I'm about to trade (which means it's muted 80% of the time, from 9:30am til 11:30am). Putting the tv out of your line of sight helps you concentrate on your charts, L2 and trading rig like you should, not CNBC. I rarely find CNBC a useful source of realtime trading information; I may put one of their mentions (mostly Joe K's) on my watchlist for further action on a different day, but by the time CNBC talks about a stock it's usually far too late for daytrading. It used to be that a CNBC mention would move a stock 1/2 point or so, now I find the time it takes listening to CNBC vs. the payoff of a play is extremely low. It's more for watching during lunch or on choppy trading days.
- **Start over now and then:** move your desk to an adjacent wall, put mirrors on the walls, try new layouts and combinations to get one that you feel personally most comfortable with. Experimentation is useful.

### Your Personal Daytrading Workstation Area: RUNNING IT LIKE A BUSINESS

- Sure, trading for a living is fun; but it's also work. Make sure to keep your daily P&L (profit and loss; how much you made or lost each day) posted on a graph near your work area.
- Remember that, like all new businesses, you may be in the red for your first year or so. That's normal; what's bad is to have steep trading losses in the thousands of dollars that turn into "investments" because the stop wasn't taken soon enough. This ties up your capital and costs you money. Look at many companies, eg Sears, S, whose stock price has been slowly cut in half over the last year. Or QCOM, which has been selling off all year in early 2000. Don't make the mistake of buying and holding for a long time if the trade violates one of your rules. Don't let winners turn into losers, waiting and hoping for a comeback or turnaround. That's not how we make our living at this; we dart in and out of positions.
- I put notes like "High-percentage daytrading for daily profits is Required, Ken! Continue to Succeed". Your mental frame of mind is so important to success as a trader; risk management and trading techniques are critical to add to your skill set over time.
- **See trading as though you just hired yourself for a job** - how would you look over your shoulder as the boss? If you're a small business owner like I've been it's automatic, you do it or nobody else does... **What measurable expectations do you have of yourself?** How will you take it seriously enough to succeed vs hoping to make it rich on lucky trades (the "lotto" approach hah). Make no mistake, this is a shark pool you're swimming in, we're all here to take food from it. To win, you must nibble more adeptly than the the others do.
- "Internal vs external locus of control"; psych 101, do you see yourself in charge of your fate, or do you blame the market, your broker, the company whose stock your trading, everything but yourself? Winners see themselves in charge of the situation, losses are temporary. Losers see themselves as victims and enjoy feeling bad, generating sympathy and blaming others. I sincerely hope you're disciplined and successful. Tony Robbins and other authors have excellent books on the topic.
- Step 1: Remove all non-trading/non business like artifacts from your trading area and workspace (or at least most of them). Perhaps keep a family photo, or a photo of a tropical place you'd like to live, or other incentive, in view as a reminder as to why you're doing this.
- Step 2: Do an ergonomic check: make sure everything is well-done. Educate yourself on the topic; if you're going to be spending hours in front of the computer like I do it's important to take care of eye and wrist strain-related products and equipment layout for your health.
- Step 3: Add the encouraging reminders and trading metrics/graphs to keep track of your activity as a trader.
- Step 4: If you want, submit a photo scan and we'll post it on the message board (or on this page) for others to see how you've arranged it. I'll do mine when time permits...

- Dealing with Trading Losses (also [see the worksheet](#) on this topic)

● **Main Points:**

- A string of trading losses, or a "red portfolio", can have a serious damaging effect on your ability and confidence as a trader. Let's look at how to deal with losses in a constructive way.
- LOSS PREVENTION: As we've said all along, having small predetermined stops and sticking with them is a prerequisite for your trading success.
- LOSS RECOVERY: Many good traders can trade their way back up out of trading losses, particularly with all the profitable trade opportunities that exist daily in the market. Poor traders who do not resolve to change their trading habits lose.
- EMOTIONS OF LOSS: Dealing with losses in a professional way, as a business person, helps you to avoid major problems. Small losses are a routine part of trading. Inexperienced traders take moderate to large losses, giving their money to other traders and institutions.
- EMOTIONS OF VICTORY: Celebrating small stops taken well should be a "new thing" you add to your trading system. Saying, "ok, I lost \$125 on a 1/4 point stop of 500 shares" is great. Saying "aagh I'm down \$850 on that EL0T tank, now I'm an investor" is terrible. Savor your wins, don't take losses personally.
- Let's look at a few examples and illustrations here to help out:

**Small Losses = A Cost of Doing Business**

**You Should See Small Stops as a  
NORMAL & ROUTINE Event**

- Do not try to be a perfectionist and expect perfect trades; it is an imperfect game. You will not buy the exact bottoms and sell the exact tops; you just want a piece of the action.
- Every trader takes trading losses. The size of losses taken is what separates good from poor traders. Resolve to take small stops, using TA, T&S and L2 indicators.
- Small losses should be seen as the "lights and water" bill of operating your store. If you're losing a lot vs. winning you will not be able to trade for very long. Papertrade until you are good at real trades, or at least trade small shares (100-200) until you're good at it.
- You should look at the big picture, nobody likes losses, even if they're small. They are better than large losses though, it's your daily (or weekly) P&L that counts. You can do fine just making 20%-30% winning trades if your win:loss ratio is correct. Eg for every 3 1/8th point losses you take you also get 1 5/8 point win etc. (at a minimum).
- Small "cuts" are better than broken arms - learn how to take small stops quickly and re-enter the trade at a better time and price until you get it right. Maybe its a short not a long - reverse your trading style if you think you are following the right trend.

**Large Losses = Trading Mistakes**

**Look at Moderate/Large Losses  
as a Failure to Trade with Discipline**



- A large loss is a mistake, no doubt about it, no sugarcoating it. Sure, the key is "did you learn from it", but let's not let that happen in the first place, okay?
- A large loss means that the trader was not fast enough, did not hold their stop, was impacted by a gap (for overnight/swing traders), or other trading event.
- The benefit of daytrading is that you can control your trades 100%, and are not impacted by overnight news; the tradeoff being that you don't benefit from gaps that go in your direction as well. Large intraday losses are nobody's fault but the trader's.
- It helps to remember that a good trader responds, a bad trader predicts. Intraday movements are completely unpredictable, you must be early to respond to buy signals and technical indicators, the tape/T&S and other things that tell you there's more buying than selling going on in the stock for the timeframe you're trading it.
- Everyone makes mistakes, small mistakes are easier to deal with than big ones. Example: **look at your stock like you're on a date**. Going on a first date that turns out badly and then never going out with the person again is a smart "small stop". Going on a bad first date and continuing to see a person who isn't good for you and then end up marrying them hoping you can change them etc. and then divorcing two years later is a "big loss" that should've been prevented early on. Same thing with stocks - don't marry them unless their technicals are showing buying strength. speaking from an early personal experience there :-]
- Commit yourself to changing your trading habits and swallowing a small loss is much better than riding it into the ground, or a margin call, or a long-term hold, tying up valuable trading capital. Get out early, get out fast if you're not right.

### Knowing when Not to Buy:

Let's look at this NOVL chart. At no time in this trading day do you see any buy signals of any kind.

Yet, people were buying and selling this stock all day long. The intraday buyers were wrong, the intraday sellers were right.

The stock opened on a downtrend, consolidating in a tight range at 20 5/16 x 3/8 for a couple of hours. Eventually, sellers win out as the price starts to drop. As soon as we made lower highs during the range at 20 1/4 x 5/16 over lunch you knew the price was going down, and could have entered a good short. Shorts covered awhile later, causing a minor bounce to 20 1/8... which was unsustainable, as the price dropped back to the low of the day. Don't buy charts like this.

If you had bought on the open for some reason, where should your stop have been placed? As soon as it traded in the 20 1/4x5/16 range.



Remember our page on only going after "high-percentage" plays, ones that look like they're winners early enough to get some play out of it. Avoid "indeterminate/can't tell" and "low-percentage" plays vs overtrading. An important part of trading for a living.



## Module Three

### The Mental Game of Daytrading:

Click on each link for a new daytrading lesson. Be sure to complete the trading worksheets and activities for each module.

[Back to  
DTU CAMPUS MAP](#)

Click on each line for daytrading lessons from the list below. Keep checking back every couple of days for new lessons, activities and worksheets. An underlined link means the content is now available. **Note: set your browser to refresh "Each Session" you reload a page...Enjoy!**



Trading Lessons

 = Updated pages w/in last 48 hours.

DTU Module Three Lessons:



- [Mental preparation and focus: Tips for How to get into your "trade zone"](#)
- [Developing the Skill, Patience, Discipline and Attitude to Succeed at Daytrading](#)
- [What you should be doing first thing in the morning before the market opens](#)
- [Creating a Successful Trading Environment: What to Put Near Your Monitors](#)
- [Dealing with Trading Losses: Or, How to Lose \*without\* saying "#@\\$% I just lost another \\$300"](#)
- [Maintaining a profitable risk:reward ratio in your trading](#)
- [Disciplined Trading: 10 Practical Tips to Stay Ahead of Trading Losses](#)
- [Setting Daily Profit and Loss Targets: How to Know When to Hold, When to Fold](#)
- [Becoming a Better Trader: Having Patience with Yourself](#)
- [Knowing the Rules of The Game and Following Them - Daytrading Discipline Tips](#)
- [Minimizing Losses and How to "Turn the Corner": \*\*Trader's "Turnaround Wheel"\*\*](#)
- [Celebrating Victory: Trading Rewards and the Daytrading Lifestyle](#)

Worksheets



[Click here for Powerpoint viewer program](#)

[Click here for MSWord view program  
\(3.5Megs\)](#)

- [What to Do When You Lose](#)
- [Finding Your Daytrading Discipline](#)
- [Developing a Daily Trading Matrix](#)
- [Increasing & Decreasing Trade Sizes](#)

## Activities

- [Thinking Like a Professional Trader](#)
- [Becoming Focused on the Trade](#)
- [Using Your "Lessons Learned" in Trading](#)
- [When All Else Fails...](#)



**JOIN DTU'S 'TRADER FRIENDS' REFERRAL PROGRAM** 

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Successful Online Daytrading Training Resources

- Maintaining a profitable risk:reward ratio in your trading

• **Main Points:**

- Let's face it, **daytrading is hard work, and you have to run it like a business** if you are to profit and/or make a living at it. To help migrate from "gambling/playing now and then before work/having fun" into SUCCESS that's Consistently Profitable, enabling you to do this full time from wherever you want to live, you've got to make more than you lose, right?
- It's very true that I can have 70% losing trades but be highly profitable at the end of each day, and at the end of each month. Tiny stops and larger profits is the key. Hey maybe I have to take 3 1/16th-point stops before I get a 5/8 point score...that's profitable for me. Or, maybe I want to scalp a slow mover for consistent 1/4s all day, that's fine too. I have much more often been happy that I sold too soon.
- **Here you will develop your risk:reward trading ratio needed to be effective.** Remember that they are defined by each trader, depending on your trading style and objectives, and must be such that your net wins are bigger than your losses. It's that simple, yet that difficult.
- Think of it as though you're running a casino: you want to set the overall odds slightly (hopefully largely!) in your favor over the long run of trade after trade. This means **you must have defined measures** and a trading plan that you stick to no matter what trade after trade. For every time you stop out and then watch the stock reverse and run up you'll get 2 or more times that it doesn't. **That's what knocks traders out of the game** - all it takes is the "2 or more times it doesn't" to eat away your trading capital. Play a slot machine with a 93% payout and you'll lose capital at the rate of 7% of your stake, nibbling it down to zero. Don't be a gambler in stocks.
- Instead, we'll take a highly disciplined approach that enables you to succeed at this. Note: if you're not a highly disciplined person who can't make rapid decisions with computer-like precision then daytrading is not for you - try swing trading/buying mutual funds instead. :o [Try playing games like Tetris](#) that force you to make rapid decisions one after another, it's been my favorite for years.

**Examples:**

Your Risk:Reward ratio is simply the ratio of the average amount you win per trade vs. lose per trade (or per trading day, or week etc.). If you're losing 1/2 points and winning 1/8ths you probably won't be trading for very long, right?

You have to adjust all of this by the number of shares traded, the stock price and the width of the spreads for the stock being played of course.

Let's look at the example on the chart to the right here, for NEON. So let's say you bought is at 57, thinking it sold off "enough" and wouldn't keep going down. Wrong! It keeps plummeting.



**Optimal Day:**

### Quiz time! Do you:

- a) pray for it to bounce
- b) watch like a deer caught in the headlights of a car, frozen as the price drops out from under you
- c) quickly limit your loss by taking 1/4 point stop on the trade, admitting defeat quickly
- d) decide "I'll hold on to this stock for a few days or weeks, it'll come back sometime, it's a good company, nice analysts ratings, and they just got into a deal with XYX company..."

I hope you're a DTU trader who answers with the correct choice c, we want to trade against all the losers who trade like a, b and d. We take their money.

**Daytraders' Play:** For NEON, as soon as the market proved you wrong you should've exited the position. Why let a 1/4 point loss turn into a 1-point loss?

After letting the sellers finish, we caught a mini-double bottom at 56, and bought the bottom 3 consecutive times for scalps up to 57 resistance, before it broke through at the end of the day. Very predictable stock pattern.

See, our risk reward ratio in this case (1/4 point loss to 1 point win, on average), is 1:4...**we win 4x as much for every time we lose.**

**Think of it like this: if you have a 1:4 loss:win ratio, every "win" you get "buys you 4 chances" to get it right the next time.**

**Bonus Quiz question:** Where else could we have traded the above chart Long based on a key technical indicator you see? (answer: after the last buy/sell cycle where you see a volume breakout indicated right before it goes thru 57 again).

### Setting Your Own Risk:Reward Ratio for your Daytrades -

You must, for your own trading style, determine the following:

**Once you're in a trade, where is your predetermined stop point at?** Use either a key support/resistance level, or a "trading standard" that you use. My stops are always no more than 2 spreads away from where I bought the stock at. **Also determine "where's my trailing stop at"?** (For example, you buy NOVL at 35 1/8, it goes up to 35 1/2 (now you should have a trailing stop at 35 1/4 etc.)

Why? Because **for me to make money I need to have at least an absolute minimum 3:2 win/loss ratio**, meaning that every time I lose 2 spreads I need to make an equivalent trade (volume of shares etc) that gets me a profit of 3 or more spreads. With commissions, trade slippage and other factors I prefer to shoot for a 3:1 or 4:1 target).



Like Serge Milman says in Electronic Daytraders' Secrets (Friedfertig/West), "these guys are killing themselves losing points and making quarters".

**The first cut is the cheapest one;** you have to determine for yourself how far to let a trade go against you before bailing out. I am almost never disappointed in myself for stopping out with -1/8 or -3/16 or -1/16 stops all the time. My broker likes this of course; I try to maneuver for high-percentage trades, and don't mind "trying for the win" a few times, even if I take a few small cuts before I nail a 1/2point+ trade w/500 shares.

Of course if you're playing JDSU DISH QCOM DCLK etc then adjust these for the 3/8-point spreads these stocks can trade in. The main thing is to set a stop at no more than 2 spreads away from where you bought in (or at least 2 spreads down from the inside bid). If I'm that wrong about a trade it'll probably get uglier before it gets better.

**"The best trades are usually right from the start". eg. I bought the bottom of WCOM on Friday 1/21/2000, nailed it exactly for 500 shares and made \$187 in 7 minutes. Boom.**

But, I kept fishing for bottoms for the rest of the day in WCOM and gave back most of my \$187 in commissions :( Should've taken the money and run, waiting for a breakout above resistance. However, I traded the bottomfishing correctly in that I kept 1/16th point stops. WCOM never did run more than that first successful trade I made.

To make a long story short, I made \$187 on the winner, and lost from \$30-\$45 a couple of times on the times I wasn't right. A breakeven afternoon in WCOM, but at least I managed the trades correctly. Just goes to show you we all make common trading errors, mine was in violating the "don't overtrade" rule. At least it was fun. And wow look at those 1-second order executions.

```
[13:23:56] <Confirmed> Buy 500 Shares of WCOM at 41 1/8 using CyBerX
[13:23:57] <Executed> Buy 100 Shares of WCOM at 41 1/16 from ISLD-
[13:23:57] <Executed> Buy 400 Shares of WCOM at 41 1/16 from ISLD+
[13:31:14] <Confirmed> Sell 500 Shares of WCOM at market using CyBerX
[13:31:15] <Executed> Sell 500 Shares of WCOM at 41 7/16 from ISLD-
```

Buy using limit orders,  
sell using market orders  
in fast-moving stocks.



Ok, your turn. Pick any 3 stocks you trade regularly, and write out on a piece of paper **where the key 5- and 10-day support and resistance levels are at.**

Now, **write down what your stop will be** if you bought a breakout above a key resistance level.

Finally, **write down how far you want to trail your stops at** (I generally use 2 spreads, maybe 1 if I'm trading in size, eg over 500 shares).

As always, papertrade it for a few days to get the hang of it, then trade with small 100-300 share size trades just for practice.

**Remember that you can always get back in a stock** if you stop out, it climbs down some more, and starts to rebound on volume. Or, if you sell with a profit in an uptrend and it breaks through some key resistance level after pausing for a bit, doing a "shake".

One of the key things I had to learn was to not think in absolutes, saying to myself "well I tried to buy WCOM and I missed it so now I won't trade it anymore today". Instead, be a fighter and if you still have the initial reason to enter the trade in motion in the market for that stock at that time, then try again.

Think of it like "chipping away" at a large gold nugget, waiting for a big piece to break loose and fall into your trading minecar. You'll get some scrapes and dust in your eyes (small stops) along the way, but keep trying. If your reason for entering the trade remains intact (eg a breakout on volume). Wait to buy the dip in an uptrend vs. buying the top and having it fade back. Keep at it. Learn the psychology and behavior of the traders in that stock on that particular day.

Best wishes!

## Module Three

### The Mental Game of Daytrading;

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MODULE 3

#### Disciplined Trading: 10 Practical Tips to Stay Ahead of Trading Losses

#### ● Main Points:



Ken  
Calhoun

- Aside from reading the book, The Disciplined Trader, I've found a number of basic disciplined ideas that help me to stay profitable consistently in the long run.
- Here's 10 quick tips to help you; hopefully you're already using a few of them in your trading.
- If you are and you're still behind, don't worry; just refocus on trying to use 1 to 2 of them differently each day until you're able to say "I'm doing all of these consistently". If you are, you can begin to minimize your losses and start the path to turning around and becoming a more successful, disciplined trader.
- (note: if the spinning rings bug ya, type Alt-V, A to stop animations; View/Stop Animations)



#### **Tip #1:** Define your stop and exit target before buying or shorting.

This means to have a predetermined trade plan for the stock before you do anything related to buying, selling or shorting the stock. As targets of opportunity come up on your trading charts and level 2 screens, quickly consider the risk and expected profit before entering the trade.



**Tip #2:** Prepare for each day you intend to trade both mentally and physically.

You have to take a bit of time to get yourself geared up to trade. Trading scared, trading tired or trading with anything less than your full concentration will lead to losses. You may want to start by trading only several days out of each week instead of trying to play daily.

Physically, you should take care of yourself: eat some carbohydrates in the morning, not just coffee, eg toast, a microwave baked potato or rice for energy. Take a few deep breaths, stretch your body a bit. Go for a walk during the lunch hour.

Mentally, you should do your DD (due diligence) and prepare a watchlist for the day prior to the open; once the market has opened also keep an eye on the % gainers/losers/most actives for shorting and bounce opportunities. Get your mind in shape to trade by practicing with a trading simulator or other paper-trade device. I find playing tetris-type games keeps my mind alert to develop the rapid decision-making ability needed to daytrade effectively. Get "Tower of the Ancients" at [www.fiendishgames.com](http://www.fiendishgames.com), for example.

Finally, if you're not up to trading on one particular day, then don't. Take the day off. The market will still be there tomorrow.



**Tip #3:** Scale back your trade sizes if you're losing consistently.

Nothing can be more mentally devastating than a string of losses. Things seem frustrating, and you're worried about losing even more capital. You want to "get out of the hole and at least break even".

To get there, you need to: 1) review why you lost in the first place: eg was it the stocks you played (like cheap \$5 chatroom pump n dump specials), was it lack of discipline to keep small stops, lack of knowledge of level 2 or chart patterns...etc? 2) papertrade til you are at least 40% successful with your choice of trade entries and exits 3) start back in the game by trading just 100-200 shares (or less, for expensive stocks) 4) work up your share sizes back to 500-1K shares after you are effective for at least a few weeks using 100-200 share size trades.



**Tip #4:** Gain more knowledge, regroup and resolve to re-educate and re-train yourself.

Learning from others who've made it can be a big confidence-builder. I find if I've lost and I'm feeling down I re-read the "Secrets of Successful Daytraders" by Friedfertig/West; I enjoy reading the attitudes and intensity that these guys have in the stories they share. Everyone has different books they like; make a commitment to building a library of "defensive resources" to help encourage you to examine your errors and commit to more successful trading habits.

Much of what you need to be successful is in the subtleties that are not included in many of the books; I'm attempting to bridge that "intermediate/advanced practical gap" with the DTU content. But, the trading basics and friendly authors' voices in many of the books out there are helpful for encouragement and to help you get back on track. Buy a bunch of daytrading books from Amazon.com and return the ones you don't like. Also, get some of the tapes from last year's daytrading expo at <http://www.onlinetradingexpo.com/recordings.html> and the recordings at [www.worldwidetraders.com](http://www.worldwidetraders.com) in the members' area. I find listening to other traders as well as reading their words is helpful. Tell them I sent you.



**Tip #5:** Get in touch with other daytraders in your area.

If there is no group, consider starting one to meet and share trading strategies. Tim of "Daytraders of Orange County" started the big chapter down there, see if you can get an informal monthly meeting at a local restaurant started to swap daytrading strategies and techniques with others. I plan to start up a chapter here in Hawaii if I have time (hah), you may have luck by contacting others in your area.

The worldwidetraders.com has geographic contact info. for other traders in each state/country, start by emailing others, perhaps phoning a few local brokers to see if they know of anyone who daytraders that would like to meet every now and then. Daytrading can be a lonely job; it's good to share and get encouragement from others.

### **Tip #6:** Change the stocks you trade, and narrow your focus.

An ongoing personal trading challenge I have is to keep my list down to under 20 stocks I watch each day, it's entirely true that you can make a living daytrading a single stock (or a small group of 1-5 stocks).

There's so many to choose from it's tough to limit yourself! It's kind of like going to a nightclub or bar with a lot of women to dance with; you have to choose carefully or you might get a bad one (ok I'm stretching, but you get the analogy). (^\_^)

It's easy to get in the habit of following a few "favorite stocks"; but you must exercise discipline and ask yourself questions like "ok, of the last 5 trades I did with this stock how many were winners, and what's my profit and loss trading that stock?". Since you now know to run your trading like a business, you must cut that stock loose and not trade it anymore if you aren't successful with it. Many stocks are very difficult to daytrade consistently (like INTC MSFT for me, at least); remember to pick stocks that meet our [trading criteria](#).

Change the stocks you trade, no matter how much you "like them", if they aren't making money for you. Some stocks are difficult, low-percentage stocks to daytrade. Recognize this and move on. For daytrading I like CIEN NOVL DCLK AMZN SPLS, for example. Your mileage may vary, e.g. try stocks you tend to do well with.

### **Tip #7:** Experiment with different trading styles; e.g. go to swing trading for awhile.

If your daytrades are losing you money; you might want to try a different trading style for a couple of months, eg fade back to swing trading (buying and holding from 2 days to a week or more, depending on when a good profit is reached).

Many traders are more effective at swing trading and investing than they are at daytrading. Make sure you do not mix the two trading styles, however! Your stops are generally looser for swing trades, and your profit expectation is also higher. In swing trades, you will carefully use the 5- and 10-day charts, along with standard longer term indicators like the 50- 100- and 200-day MA lines for support and resistance. You will be keenly aware of earnings dates for not only your stock but those of major customers for the stock you are buying that might impact your stock.

The key is to not mix the two and treat your swing trade like a daytrade. Sure, if your swing trade runs up and you make a good profit then take it (eg I recently swing traded DBCC from 8 1/2 to over 9 and took profit when it looked good).

### **Tip #8:** Don't "average down" (adding to losers) or use other bad trader habits.

"But it worked for me the last time I did it", you exclaim. Well sure, and Tennessee got to the playoffs this year too, but over time it will not work. It's ok to add to your winners in a small pyramid (eg buy 500 at 44 1/8, add another 200 at 44 1/4, sell them all at

44 15/16). Do Not average down (bought 200 at 33 1/2, bought another 200 at 33 'cuz it looks cheap, bought 500 more at 31 because I know it can't possibly go any lower than this, then capitulate and sell them all for a loss at your 30 stop. After which, of course, it rebounds.). Sound familiar?

Don't do it, just say no to "averaging down", a loser's way of playing the market. buy strong stocks, sell weak stocks. It's like golf, you need to get rid of bad swing habits that cause slicing, in your daytrading you have to eliminate losers' trading habits like averaging down, even if it did work for you on a couple of occasions. Also avoid trading on choppy, low percentage days, or during the lunchhour (in general).

### **Tip #9:** Change your trading environment drastically.

Go buy a better chair (I use a leather execs chair w/built in massage that swivels, very comfortable and effective), get ergonomic keyboard and mouse (I use a legal pad for a mouse pad, best idea I've ever had, I write my day's trades on it w/notes etc).

Change your monitor and computer setup: perhaps change from one wall of the room you're in to another wall, reconfigure the tables and chair. Above all, make it comfortable and clean. A cluttered trading environment is bad for you.

Add motivational posters and sayings to your trade area. I use a coffee mug from Successories that says "Expect to Win". I do. Also, have reminders posted to your monitors (I have "Tight Stops - No Exceptions" posted and it still helps me to remember to get out fast when I'm wrong). Read Tony Robbins' books over and over again. If you really get into it, you'll start to believe, and make it happen. Expect success of yourself, and be willing to "do it right" to achieve your goals.

### **Tip #10:** Ok I'll say it again: Resolve to Keep Small Stops, and Use Trailing Stops to Lock in Profits on the Way Up. Discipline, discipline, and more discipline.

Anyone teaching about daytrading can't say this enough, because more people say they'll do it but waffle when they're in a trade and lose their money than I can keep track of. your trading should be highly mechanical, not emotional. System-based.

This is a game that requires absolute discipline, concentration, and rapid decision-making abilities. If you cannot do this, then put your money in a mutual fund and go work for another man for a living.

Personally, the thought of putting up with the bs that goes on at most companies (and the horrific loss of personal time that goes with a 8-10 hour day job) is a tremendous motivator for me to abide by the rules of this game. Life is too short to spend any amount of it working in someone else's office. Being your own boss is exhilarating. Ran my own training business here in Hawaii for a few years, over 130 clients, now daytrading full time. It's great.

Having time to golf, spend with my new baby and wife, and enjoy shopping and fine dining here in Honolulu is a "dream life" that I do not want to sacrifice. Daytrading enables this lifestyle, the price is intense study, continuous learning and commitment to follow the rules.

Expect success from your efforts. Commit to changing your life. It can happen, if you're strong enough. Most people aren't. Good luck with it.



- **Setting Daily Profit and Loss Targets: How to Know When to Hold, When to Fold**

● **Main Points:**

- Developing the skills to know the best price to **take a stop loss** or **take profits at** takes plenty of practice. Nobody ever gets the exact top and bottom consistently, your goal should be to take a piece of the price movement off the table as profit for good trades and/or exit the trade at a minimal loss if you're wrong.
- One of your best tools in this area, besides knowing the 10-day support and resistance levels, and intraday volume and range, is your own sense of when the stock is overextended or oversold and **"looks good" to you** for a buy or sell. In daytrading, we look for the extremes and play retracements off the extremes. The obvious example is an opening gap up or gap down; eg if the futures are -15 or worse on the open (a rare occurrence) you'd expect some buying, with a retracement into the single digits, as stock prices "look cheap" to traders and institutional investors.  
**Remember, what "looks good" to a professional is typically more of an extreme than what "looks good" to a beginner.** If my stock is up over 12% on the day, I'll look to sell. If a stock is down over 5% on the day around 10:30 on no news, I may be looking to buy.
- Many people say you should not have profit targets and to 'let the stock tell you' when it's time to sell. Rubbish. If your stock trade is over 5-10% in your favor then take a profit, eg you bought at 20 and it's now at 21 3/4 or 22 1/2....I'd look to take the profit, or at least sell half your position to lock in the profit and 'wait and see' for the rest of your position, using a trailing stop.
- If the loss is over 1-2% against you, eg you bought at 20 and now it's 19 3/4 and dropping, look to stop out and wait for a lower entry price. You can always buy the stock back...the commission is an insignificant percentage of your total potential gain or loss....get in the habit of buying, stopping out small, taking profits healthy, and you'll be a successful trader.
- Taking small stops continues to be the #1 challenge for virtually all traders; we need to put trading rules in place to help us have the discipline to exit a losing trade quickly, and re-enter when the price has stabilized and is back on the upswing (it may not be til another trading day).
- Each trading day is it's own "world", spend a lot more time than you currently do looking at the daily composite charts (\$COMPQ, \$SPX, \$TRINQ/\$TICK) as well as sector charts like \$RLX \$SOX \$GIN. This tells you you if there's more net buying or selling, along with the trend, for the group of stocks that you are trading. They are major indicators that you should use to determine money flow direction; far too many traders ignore the sector and market indexes, focusing only on their stocks' intraday charts. The major indexes can help you see the overall direction of the market, which you should pay a lot of attention to.
- Determining support and resistance levels will help you decide where your stops and profit targets should be, remember to stay at least 1/4 point ahead of the market in your timing so that you can sell into buying strength and buy on panic dips and buys.

**PROFIT AND LOSS TARGET GUIDELINES for TRADERS:**



**Deciding When You're Going to SELL is MUCH More Important than When you're going to Buy**

- Unlike conventional trading, you should spend 80% of your time and energy figuring out where you will sell and 20% of the time on where to buy. Most traders have it wrong and put a ton of energy into figuring out where to buy, with little energy being spent on managing the more important Sell side of the transaction.
- Try setting sell targets at slightly under where you bought (for stop losses) and use trailing stops to lock in profits. Stay a spread or two under the average "wiggle" in the stock price, eg if it wiggles in 16ths in a 1/4-point wide band on the way up, use a trailing stop right under the 'wiggle/shake' area.
- **Managing the sell side of your stock trades is much more important to your success as a trader than managing the buy side.** Most traders fail at this

## Set Your Targets BEFORE You Trade

- Most traders do a haphazard job at best in this critical area - impulsively buying near the top of a stock, getting shaken out or taking a loss.
- By "set your targets before you trade" I mean WRITE THEM DOWN IN FRONT OF YOU on a piece of paper: where is your stop loss, where will you sell to lock in profit?
- If you are trading in size, over 500 shares, jot down a quick note of how you will scale out of the position as the price goes up. What's your strategy? Make sure to have one.

## If You Can't Keep Your Targets, Make Your Software/Broker Do It For You

- Most software platforms, including Cyberx, Datek and others, let you set stop losses and sell prices to automatically trigger for you.
- Many people like to go with "mental stops". This is fine if you're experienced and scalping teenies or flipping 1/4s and 1/8ths, but if you're new/intermediate you really should **use mechanical stops at first**. At least for some of your trades.
- Experiment with the software, I get frequent trader questions from people who need to know the basics of what a sell limit order vs market order etc. is. Please see the help resources available at your broker and call them to ask them to explain how their particular software platform works to help you set stop limit orders. Use them.

## Scale In and Out of Positions Using Targets

- When you're trading more than 500 shares or so, you should scale in and out of positions, unless an unusually large move warrants immediate action on the entire lot.
- **SCALING IN:** When you buy a stock that's going up and you add more stock/buy more as the price keeps going up. This is for those rare occasions when you've "caught a runner early in a breakout" and there's still a lot of upside left, in your opinion. You might also scale in as an "Average down" on very rare occasions for swing trades, but remember your pyramid must be built with larger positions at successively lower prices, vs incremental adds on the way down (more on this strategy in a later lesson).
- **SCALING OUT:** This is when you are gradually selling off your position a bit at a time, lets say you have 1000 DELL at 52 1/16th and the price is up to 52 5/8 from your buy point, you might want to sell 500 at the 5/8 and wait to see where the price goes before selling the rest of your position. If the level 2 shows thin support at 1/2 and the price starts to drop, then you might close out the balance of your position at the 1/2, locking in profit before the price drops. Or, if the price keeps running up you might sell at 7/8, taking profits of 500 shares at 5/8 and 500 shares at 7/8.

- Use targets to determine ahead of time how you will manage your scale-in and scale-out trades. This is particularly important in the case of stock going against you, you might scale out most of your position at the initial stop, say 800/1000 shares, keeping 200 to see if you get a bounce .... if it doesn't bounce where you thought it would, then sell off the remaining 200 and wait for a consolidation before buying back in again.

## The Mental Game of Trading and the Successful Use of Trading Targets



- Does trading occasionally cause stress for you and get on your nerves?
- I have found that it brings much calm and order when I have designed the borders for my trades ahead of time: the borders being my stops and exit targets.
- It's also a useful trading development tool, as you can look back over the charts and trade stops/profits to see where you stopped out too soon or too late and where you took profits too soon or too late.
- To trade consistently for a living and have a net profit at trading absolutely requires a long string of base hits vs. home runs. Your trading stops and targets will help you decide when to take profits and when to stay in the trade.
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### When to Hold and When to Fold?

Although I'm not a big Kenny Rogers fan, his song captures the essence of successful trading in some ways.

You have to decide, ahead of time, when you will let the ante go to the other fellow (your small 1/4 point stop), and when to hold your trade for more profit.

If the cards are against you in a trade after you've ante'd up then give up the trade, take a small hit,

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- **Becoming a Better Trader: Having Patience with Yourself**

● **Main Points:**

- **After discipline, patience is the second-most important personal skill to develop to help improve your trading profits.**
- One of the challenges we all face in trying new trading styles is that we can, for example, be too impatient with our swing trades and use a daytrading-type profit target (recent example (Mar 2000) I bought ROST at 13 and sold 3 days later at 15, but holding another week would've given me 22. I took a 15% profit but could've had 80% if I'd been more patient with that swing trade. Could've would've should've have no place in our trading self-talk, though!).
- Entry, exit and profit targets all help build patience, let's look at a few new ideas, though.
- In daytrading, much of our impatience comes from a sense of "not knowing what to do". This can be the 90% of the time you're watching a stock looking for a good place to buy, it can be from feeling frustrated that you haven't made a lot of good trades lately, or it may come from the greed to take quick profits when you should let the trade sit longer so you can book a bigger profit.
- Determining support and resistance levels, along with patterns, such as cup and handles, breakouts from trading ranges, trading channels and trends, are all key in helping you decide if you're being too hasty or too slow in terms of your patience with a trade.
- **Patience should not be confused with taking large losses or letting a trade get away from you with a stop that's inappropriate for the trade timeframe (scalp/day/swing/position) and number of shares you're trading, however.**
- **Don't "be patient" with a stock whose price is falling, for example.** Sell at a tiny stop and patiently wait for a better time to enter the trade, if opportunity presents itself.
- **Be patient with a stock whose price is rising,** locking in profits with a trailing stop.

- **Personal patience** can be enhanced by a number of simple activities, such as slowly counting to 20, or slowly reading off the day's closing price for each of the last 20 trading days in one of your favorite stocks, for example.
- Why is patience important to the trader? We need it for several reasons:
- to avoid selling too soon and taking overly-small profits
- to avoid overtrading and commission churn
- to avoid entering bad trades
- to to use more professional trading techniques, like buying at the bid and selling at the ask
- Why is patience important to helping you develop your personal trading style? Can you think of several benefits, or reasons, why you need to personally devote some time and energy to trading patience?

Exceptions for taking fast profits: when a stock jumps up over 15% or more you should set a stop right under the peak, or sell into buyers.... but those are rare occurrences. Below is an example from March 29, 2000 on how selling a spike is fine, and patience is not called for (compelling immediate profits are always good to take!):

Stock	Bought	Shar...	Sold	+/-	P&L
HRL	15 3/8	200	16 11/16	+1 5/16	262.50

**\$262 profit taken on small HRL swing trade March 29 2000.**

**Sell signal: 16% price spike on no news, time to sell and rebuy on pullback.**

Defining your time horizon and profit/sell targets prior to entering the trade will let you know if you're being "patient enough" as well. If you're buying a stock that's just been cut in half on bad earnings, for example, I'd set a 15%-25% retracement sell target, eg it goes from 60 to 30, you buy at 30 1/4, the sell target might be 34-36 or so for a swing trade and maybe 31-32 on a day trade.

**Trading Areas to Develop Patience In:**

## Personal Learning

- Almost all traders I work with underestimate how much there is to learn about trading stocks for profits - have patience with yourself.
- You should read at least 15 books on stock trading, highlight them, make notes and develop your own set of trading tips. Most of the books are too basic, but they do offer a starting place.
- Going up against the stock market unarmed with detailed trading skills leads to financial losses - the success is in the details of learning how to trade.
- To help develop patience in this area, try making a commitment for how many hours each week you will set aside to learn our DTU content and content from other sources.



## When to Buy

- Avoiding choppy or low-percentage trades is an important success skill. Most of the time, you will be watching the charts, not actively trading. Figuring out when a breakthrough or reversal is about to occur is the skill to work on.
- When to buy? It's always better to avoid questionable entries and wait a bit before plunging into a trade because you're bored or because of a CNBC or chatroom call.
- Since it's your money, be very careful before you hit the 'buy' button. Enter your positions in small increments, eg start with 100-300 shares and build the position up from there, don't just jump in to buy 1K unless it's really on fire, a rarity.
- Try calling the intraday tops and bottoms of your stocks by papertrading, based on the 3-5 day support and resistance, as a skill-building activity.



## Stock Research/TAVDD

- Many traders want chat room and site picks vs. doing their own stock research. This is a mistake. You need to be an independent, strong trader, not using a crutch of other people's stock picks, many of which are incorrect anyways.
- Learning Technical Analysis is a core trading requirement and takes months of study. We provide patterns and training here at the site to help out, it will take you many hours of practice and market watching before you can correctly identify overbought/oversold/trending stocks that you can trade profitably.
- To develop patience here, use our worksheets and other materials you develop yourself to help you decide what the buy and sell signals are for stocks that you are watching or trading.

## When to Sell

- Traders' success depends largely on their sell decisions. Sometimes it is difficult to hold a stock that is showing a decent profit. Other times it is difficult to sell a stock that is showing a small loss. You must learn to do both consistently, and professionally.
- Depending on your trade time horizon, you should look at support and resistance levels, trends and volatility to help you determine when you have gotten enough profit out of your trades, or when to cut a loss.
- I have found that selling when the stock is up over 12% for the day, or when it fails to make a higher top after 10:10 am for overnight holds etc. are good times to sell. Selling fast with profits in your pocket is an effective strategy.
- I have lose when I've held on "just a bit longer" for intraday trade selling decisions. The time to sell is on a minor shake after the stock has run up in your favor a fair amount. Example, you buy DCLK at 81 and it's up to 88 1/2, you might set a trailing stop at 88 or 87 1/2 and close the position before it turns against you and trades down to 83.

## Trade Time Horizon vs # Shares

- FIRST QUESTION TO ANSWER: If I buy this stock, how long am I willing to hold it to show a profit? What are my stop and profit targets?
- SECOND QUESTION: Is this the best price level I'm likely to get for this stock on this trading day, or can I get a better price by entering after lunch selling is done?
- THIRD QUESTION: How many technical and momentum indicators are lined up to support my decision to trade this stock?
- FOURTH QUESTION: How many shares will I buy? Should I "scale in" to the position by buying a few hundred here and adding, or should I buy the whole position at once?
- These are the types of questions you should be asking yourself, and yes they require patience, plenty of it!
- To help develop patience in this areas, think of the market like a professional does: we don't get excited over much of anything, we know the ranges and behaviors of a handful of stocks we trade regularly, and we are on the casual lookout for high-percentage opportunities.
- Example: I'm a SPLS trader and buy from 18-20 and sell from 21-23, on swing trades. If I'm daytrading it, I look for MSCO on the inside bid and know that it gets it's first peak around 10am, so I look to buy on open or wait til after lunch if it's still showing strength. That's about it. No magic, no uncertainty, I know this stock and profit from it 90% of the time I trade it. It's not exciting. It's a job. I know how to produce money trading this stock.
- For yourself, focus on just a handful of stocks you want to trade that have nice volatility (but not too much, like SPYG MSTR GENE etc, unless you're an experienced trader). Put the hard work, discipline and patience needed into understanding what these stocks do MOST OF THE TIME. That way, you're not surprised by the stock, and can reliably choose good buy and sell price levels.
- That's how you trade, folks - realize when there's a good price level to be had, and buy it. Or, realize when there's a lot of trading excitement in the stock AND THERE'S STILL LIKELY TO BE ENOUGH FOR YOU TO PROFIT FROM IN THE NEXT 15 MINUTES. A big mistake I see far too many amateur chatroom traders make is to enter WAY too LATE. You should skeptically look at a chart and say to yourself things like "yes the PMTC entry Would Have Been Good, way back at 11 3/4, now it's at 12 7/8 and most of the momentum is out of the stock, I Should Not buy here." Don't buy stock at 10:00am, in general, that's when I sell most of my stock, I like to buy on down days around 10:30 for the bounce, if we started off on a down day, or play the afternoon short cover rallies and bounces.
- Patience to NOT TRADE is the most important one to develop. Study all the examples at DTU and try to see things from a pros standpoint: why do we care about a stock, how closely do we have to fine-tune our trades to make them profitable?
- Patience to Let Your Winners Run (for Swing trades only) is the second-most important.
- Nibble at the market consistently, don't wait for home run \$1000 trades all the time. I am happy to exit a trade of 100-300 shares with a \$180 - \$350 profit. With 1K shares I want \$600-\$800 or more. (unless I am tick scalping, in which case the \$125s 1/8th point on 1K shares is fine).
- Do Not Be Patient when it Comes to Small Stops, however!!!! Don't stay in a losing trade and say to yourself "I need to be patient with it". If it's a daytrade, take the small loss and wait for a better entry. Like I said, you can try to enter the position 2-3 times on the way down waiting for a bottom, with 1/16th - 1/8th point stops. No big deal. Or, buy breakouts and set the stop right under the support line.

- **Knowing the Rules of The Game and Following Them - Daytrading Discipline Tips**

● **Main Points:**

- Becoming a "disciplined trader" is the biggest challenge you will have to overcome if you are to succeed. You can learn all the tools and strategies, but if you lack the discipline to enter and exit trades mechanically based on the signals we teach, all is lost.
- What do we do about it? People are remarkably slow to change, and so I find it takes more than just telling people to be disciplined. It is helpful to include "systems"-type changes in your trading environment to make disciplined trading more natural for you, more automatic. For the fellow trekkers out there, in trading you have to be Spock, not Kirk. Be Kirk when you're spending the money, be Spock to earn it. Sound right?
- Like any business, using and acting on metrics (measurements), are critical to success here. Know when to hold and when to fold, know when to sweep profits off the table, know when to cut a loss small and try again. You can always buy the stock again, just "sit out" downtrends and buy on strength. Nassar said it well in his *How to Get Started in Electronic Daytrading* book that "stops are like fences to help the trader know when to enter and exit positions".
- I find that using "**Visual Reminders**" on the wall is a big help for me to maintain my discipline and focus for trading. Trading for consistent profits requires you to be businesslike and professional, not like a gambler walking into a casino (even pro gamblers have predefined win and loss limits they follow, which is more than most new traders have).
- Develop these in Powerpoint or Word, print them out and **tape them to the edges of your monitors**. My personal favorites are:
  - "Tight Stops - NO EXCEPTIONS",
  - "Critical to Your Success: Sell at SMALL STOPS"
  - "Do You Buy or Sell stocks Today? Is the Nasdaq/S&P Green or Red?"
  - "High-Percentage Daytrading for Daily Profits is Required"
  - "Discipline --> Success"
  - "Become Wealthy. Just Do It"
- Also **keep some of your trade records posted to the walls**, both winners and losers, so you can see what happened "by chance" vs. what happened because of a system you followed. Make your losses count for something, learn from the losses and develop countermeasures where possible to avoid repeating the mistake in the future. Over time, you should **develop a set of disciplined trading skills that serves you well**, based on previous winners and losers.
- All good traders will tell you discipline is the key to success; this lesson will share other tips on **how** you can develop the mindset of a disciplined trader. There's a good book out by the same title, Schwagers "Intro to Technical Analysis" also has a superb chapter on 82 trading rules...a 'must buy' book. Look at these resources, they can help your trading.
- Setting **trade alerts** is also useful, have your software flag you when your stock has met a profit target or a stop point. Also using time of day patterns to your advantage will help (eg knowing that the market usually weakens from 11:30-1:30, or our 10-10:30 nasdaq bounce etc).

**Examples:**



**First: Define your own personal specific "disciplined trading" areas for improvement** - Check all that apply:

*As a trader, I know based on my losses I need to work on improving these specific skills:*

\_\_\_ **Due Diligence (DD)**: I need to do a better job of my own stock research, vs relying on chatrooms or stock picking services to pick my stocks. I need to learn how to pick high-percentage stocks.

\_\_\_ **Basic Technical Analysis (TA)** : Being able to correctly identify support/resistance levels & trendlines

\_\_\_ **Advanced TA**: Knowing how to interpret and use RSI, stochastics, MACD and sector indexes

\_\_\_ **Entering Trades Effectively - Buying Tops and Bottoms**: I need to do a better job of not buying 'false bottoms' or buying the high of the day for my trades

\_\_\_ **Exiting Trades Effectively - Using Stop Losses**: I need to predetermine stop loss limits with more discipline and stop letting stocks go too far against me.

\_\_\_ **Exiting Trades Effectively - Selling Too Soon**: I need to develop disciplined patience to let my winners run, so I do not take a small profit instead of a large profit

\_\_\_ **Learning from My Successes and Failures**: The only bad failure is one that's repeated over and over again. I learn how to improve my trading based on my experiences, refining my trading approach over time until it becomes more systematic and less emotional and hunch-based.

In looking at the list, to this day I still check "all of the above" (except for DD); it's a career process.

**Second: Make a personal commitment to yourself to change into a highly disciplined, efficient trader.** At least for 80% of your trades.

**You need to make a decision to run this like a business.** It's not "fun, hey look my stock went up"; in the long run only those of us who take it seriously are still doing it 5 years later. Plan on trading for the next 5 years, profitably.

**What do you need to do differently to run your personal "daytrading business" so that it is successful?** Like any business, it involves hard work. Lots of self-study, practice, papertrading and small-share (100-200) trades to get the hang of mastering your emotions without it costing you a lot if you're wrong.

Add a **brief trading log** (journal) to your weekly trading habits, make it very brief and easy to follow, there are numerous downloadable powerpoint example logs in Modules 1 and 2 you can use to start with. **Look for patterns in your winning vs losing trades**, identify and eliminate bad trading behaviors (like learning how to golf, it's tough to break bad habits sometimes).

**Discipline: Avoid most chatrooms.** Beware of bad "idiot traders" out there, hucksters and professional market makers. Take the time to learn how to trade correctly.

Please **do not log into chat rooms** to follow sheep into bad low-percentage trades. If you must use chat rooms, learn from the few good educationally-oriented rooms, the "why was that a good trade, what were the indicators we used?" type of rooms. If they play cheap under-\$20 stocks then beware. If nobody says things like "semi's are strong today, the \$SOX is up, the trin is 1.4 and the \$tick is..." etc... then beware. If they're saying "ELOT is running, everyone jump on board...ELOT to 10" then press Alt-F4 immediately. :o

If you check into those rooms year over year you see a lot of new sheep, a few wolves, very few are still there for the long term, because they lost all their capital and now they're back at a day job talking about "gee the stock market is tough". Dont get whupped. Avoid bad chat rooms. I've spent many weeks in both free and pay chat rooms, amazed at the low level of information that's dribbled around out there. Learn to hear what a professional trader sounds like.

Aspiring New Daytrader

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Your Trading Discipline is your "safety balloon" that protects your capital.

Pro market makers and Ripoff high-priced chat room pump and dumpers who want your money

====>>>



### Finally, develop a Disciplined Trading *Personal Action Plan*:

Let's look at making a plan to help you develop the discipline you need to succeed. Get out a 8 1/2 x 11 piece of paper and list the following:

- **Top 3 reasons why I've lost money** in the market trading overall.
- **Top 3 things I've done right** recently to either take a profit or limit a loss.
- **List of 3 techniques I am going to start using to be more disciplined** in my trading (eg taping reminders to monitors, putting trade confirmations on the wall, keeping a brief weekly trade journal).
- **One thing I will do to reinforce or reward myself for following my trading rules and discipline.**  
Eg buy yourself lunch on days that you followed "the rules".
- **One thing I will do to 'punish' myself for not being disciplined and breaking my rules.** Try something fun, like "make yourself eat something you don't like on days you don't follow the rules". Simple but effective behavior mod tips that work to shape trader behavior to be more successful.

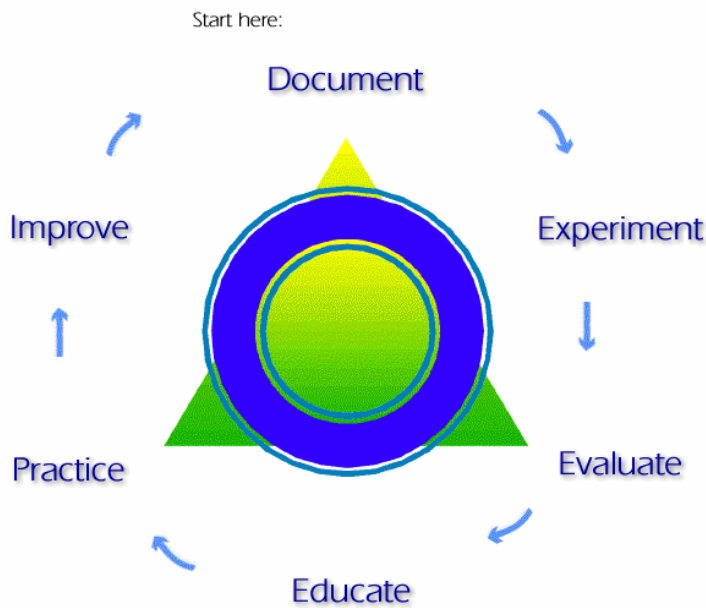


- Minimizing Losses and How to "Turn the Corner"

• **Main Points:**

- Are you tired of losing money in the market? A lot of "almost got it's?" or "oops I really missed it on that one!" or "my broker's getting rich why aren't I?"
- **Here is a step-by-step process designed to help you "turn the corner" and stop losing, to become consistently profitable trading in the market.** I can't promise that it will happen for you, as the real work (and profit/loss) is solely your responsibility. These are effective trading guidelines that we haven't covered already, put together in a logical model that we hope will help you start sweeping profits off the wall street table.
- **The bad news?** It's not easy. Nothing that's worth having, like financial independence, is ever easy. Trading stocks is tough work. You want to get rich, you have to work hard at it. It can, and has, been done, by thousands of other men and women. Why not join them?
- **The good news?** This process is designed to help you take control of your trading outcomes and should help you identify and take action on personal trading areas for improvement. Commit to it for 2 weeks and see how it does for you. It helped me get out of frustrating, frightening trade situations and develop a more experienced, relaxed, profitable professional trading style.

Trader's "TURNAROUND WHEEL" © 2000 DTU



Let's look at how to successfully go through each step in the "Trader's Turnaround Wheel" to help recover on the road to profitable trading:

## Document

It's well-known that "you can't improve what you don't understand". To understand how to trade more successfully, **you need to begin by documenting some of what you are doing**. Even if they are very brief bullet points, begin by keeping track of each of these:

- **Decision criteria** you are **currently using to enter** most of your trades (it's usually a combination of things), which of these are the most important to you: chart patterns/TA, momentum indicators like T&S, the price of the stock, the time of day, current news/cnbc mentions... Also make a note if you are trading on 'hunches' etc. vs technicals.
- **Decision criteria** you are **currently using to exit** the trade: do you have price/% 'targets' you follow (eg a retracement or breakthrough goal), momentum indicators,
- **Money and risk management**: this is an eye-opener, **do a "post mortem" on your last month's worth of trades**. What is your average gain per trade and average loss per trade? If we make that a ratio, what is it? Even money? 3:1 win:loss? 1:3 win:loss? what are your stops and how small/large have they been? You know you're supposed to define your stops/maximum risk before buying stock, what % of the time do you hold to your stops?

## Experiment

The next step is to clearly identify which parts of your trading you can experiment with (your trading "variables") and define different alternatives for these. You may find, for example, that you do better at swing trading this year than in scalping/daytrading. That's fine. You need to find your best personal "trading style". Are you a cowboy? An analyst? What's your style?

The point is that you should not get locked into one particular trading style, especially if it is not profitable for you. Also, you may do "just ok" at one type of trading but do much, much better with a different style. Experimentation is the key. Give yourself permission to "try out" new ways to trade, until you settle on a successful personal trading style.

Some common areas to consider experimenting with in your trading include:

- **Which stocks you trade**: Nasdaq/NYSE, Internets, Semis, Retailers, Biotech etc.
- **How many shares you trade at a time**: Is your average trade size 300 shares? 100? 500? 1000?
- Your **average time in the trade** and what **time of day** you typically buy/sell stock.
- Your **trading software, broker and trading environment**. Try a few. See what works.

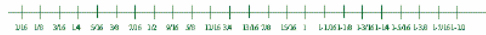
*Let's say, for example, that you picked up some bad habits in a chat room and are using Datek to trade 500-share lots of junky stocks like ELOT. You've been losing. Well, try switching to better stocks using our trade criteria (Module 1), scale back to 200-300 share trades, try buying stocks around 10:30 on days that open down (looking at \$COMPQ/\$SPX), and use cyber or mbtrading and esignal vs. a free quote service. That stuff all makes a difference. Try out what's available. And, you decide to make your own trades and mute CNBC instead of following a bunch of losers in a chat room.*

## Evaluate

This is the easiest part, I suppose. Evaluate your daily Profit & Loss, measured in dollars, and put it on a graph. Use a spreadsheet if you want, plot your daily win/loss.

One thing I did that was helpful was to make a horizontal trading fractions checklist and place check marks near the amount of my wins/losses for each week. It was a tremendously helpful tool; below is an example of what it looks like, just make a similar one and place x's on it to record each trade you've made each week.

#### WINNING TRADES



#### NON-WINNING TRADES



What else can you do to evaluate your trading success? Part of it is to keep track of your emotions while in the trade: did you keep hope, greed and fear down while entering and exiting in logical, mechanical, professional manner? This takes a long time to get right.

## Educate

Virtually everybody who has lost a fortune has also read a few daytrading books. Let's look at other ways you can get successful trading education:

- **Observe a professional day trader in action** - this is the best way, spend some time looking over the shoulder of a pro (and don't distract him/her with too many questions). You may be able to do this at a live daytrading brokerage firm, or through a training provider. NOTE: Be cautious of so-called "boot camps" that encourage hyper-active trading and then sell you a broker account as well; they just want you to "blow out" your account, giving them several thousand for the training and several thousand more in commissions or commission order flow. They should teach you money and risk management, using small shares, in slower-paced trades at first, not level 2 scalping 50 trades a day. I've heard plenty of horror stories. Check references thoroughly. Go one-on-one with a good trader, and **require the trainer/trader to show you his personal recent trade confirmations to prove he's a good trader.**
- **Learn from other traders:** see if you can get a "Daytraders of (your town)" group started as a way to network and swap stories with others who trade.
- **Seminars and workshops:** I'm sure some of these are great and most are not. Check references and ask for the email address/ph# of others who've attended, and really check it out. Don't waste days of your life and \$3,000 on something that isn't going to help you. **Carefully check the content outline** of the seminar and see if it's just basic information you've already learned or if they can teach you advanced level 2 trading techniques and chart patterns. Ask: **how much time** is spent on chart patterns, risk management and level 2? vs. the basics of "what's an index? how do you buy stock?" types of topics you can find anywhere. **Many traders make for poor trainers; they have no facilitation/platform skills and thus do a lot of one-way lecturing vs. interactive activities.** Check for the trainer's style: **ask how much time is spent in hands-on interactive learning? vs. listening to a lecture.** If all they do is lecture, ask to buy their audio/videotape/book instead!

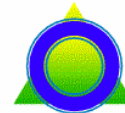
- **Spend at least 10-15 hours/week on your various learning activities** (including your time at DTU). You are attempting to learn a very complex and difficult subject: trading the financial markets has made some people wealthy and many people less wealthy. It's a zero-sum game. Don't let positions go too far against you. It's fine to go buy a bunch of books, but watching a pro trader is the best experience you can get.

## Practice

Closely related to "experiment", you need to now try out various activities and trading styles to see which one best fits you as a trader. There is no "right way" or "wrong way" to trade *as long as you make money consistently*.

- Do not try out too many ideas at once, you need to isolate and optimize each part of your trading to develop the best combination possible. Try a new software package/broker for one week, try trading a different stock the next week, etc...practice until you assemble a successful trading style. Test it out.
- Practicing with paper trading is ok, but I'd encourage you to trade live as soon as you feel comfortable, because the "mental game of daytrading" is impossible to master until your money is on the line. Besides, slippage in real trades (eg trade delays, computer problems etc) needs to be experienced as well. Just start off slow, don't worry about commission break-evens too much, just **do 3-4 trades a day max on 100-200 shares of lower-priced stock with 5% stops to test out your ideas & minimize risk.** *"Capital is harder to replace than ideas are."* (my quote).

## Improve



**Okay, we're at the last step in the wheel: improvement.** It's a never-ending circle (or at least it doesn't end until you retire wealthy from your stock gains, which you should plan to do now.)

Go back over each step of the wheel and ask yourself: what am I leaving out? what else do I need to work on to get my trading %ages up?

**Improvement is measured by your ability to carry out successful trades, in dollars.** It's your P&L at the end of the day, nobody else's. Do not make dumb trading mistakes and give money to the other guy. He'll just go buy beer with it or something :).

**How, specifically, does one implement trading improvements?** Start with the process **measures** that we looked at above (number of trades, time in the trade, average P&L per trade etc). Then look for **incremental** improvements, "fine-tuning" your trading skills until you arrive at the best combination. It takes a heck of a lot of persistence and an unwavering desire and personal expectation to succeed. I had no doubt I could succeed at this, it's just a matter of time. The less time it takes the better.

**Motivating Yourself to Trade Successfully:** Do something worthwhile with your gains, like help your family, donate a bit to charity, whatever it takes to give you a motivation beyond the simple dollars. You'll find that when you're on a "mission for money" you can make great things happen; many of us need more than just the dollars to motivate us. I go out and buy hobby stuff, take the wife out for a nice dinner etc. as a reminder to myself as to why I'm doing all this. Find your own motivators. Make it happen.

- **Celebrating Victory: Trading Rewards and the Daytrading Lifestyle**

● **Main Points:**

- To become a successful trader, you must really believe that it can happen. Many people expect to lose unconsciously and therefore do. You must overcome this.
- Please educate yourself 10 times beyond what you normally would to effectively trade stocks. Buy at least 20-30 books on daytrading and technical analysis, and review this site often as well. Do not rely on stock picking sites and chat rooms, unless the emphasis is on **Why the trade was made**.
- By arming yourself with all of the knowledge available at DTU and other good resources, you will significantly put the odds in your favor for being a consistent trader.
- Read a lot of books, view a lot of tapes and develop your own trading style. There are no "magic chart pattern" setups, there is only learning how to trade like a professional. This takes time. Anyone who's traded longer than 2 weeks know that pros play against amateurs who try to buy dips on higher highs higher lows etc... that's why there's so many reversals and headfakes out there in 1999-2000 trading.  
percentage trading opportunities. Basic TA is not enough to win, though it's a start.
- There is a very long learning curve involved in trading stocks profitably - you need to reinforce your effort, energy, and money spent in pursuit of learning how to trade by **giving yourself small incremental rewards when you do things right**.



- **How do you celebrate victory?** If you're like me, you'd rather beat yourself up over a dumb trade rather than pat yourself on the back for making a good trade....perhaps it's human nature.
- **You need Energy**, and small rewards (like taking yourself out to lunch or dinner, or buying the latest trading book etc.) will help motivate you to continue your efforts.
- **Do Not reward yourself for a winning trade that you got by breaking the rules (eg doubling down or holding through a long dip). In the long run, those plays will eat your capital.**
- **Reward yourself for being a Consistent, Disciplined trader** that follows a trade plan, whenever it pays off for you.
- You can make a living trading by being right manage your money and risks properly. It's the risk management piece that costs most people their capital, not the trade entry side of it.
- This lesson will walk you through some techniques for reinforcing winning trading skills that you are developing.
- Also [review this link](#) from the homepage for a bit on "Daytrading Rewards".

What Motivates you To Trade?

**Personal (Inside) Motivators:**

These are things that are related to your personal values and actions that get you "pumped up" to trade from within yourself.

Make a mental check - Which of the following are most motivating for you?



**POSITIVE**

- Your sense of satisfaction from executing a trade correctly
- You value not losing money, preserving your capital.
- You want to develop the trading skills to gain profits.
- You're motivated by learning new trading strategies and skills.

**External Motivators:**

These are motivators that come from outside of you that reinforce your trading skills.

Make a mental check - Which of the following are most motivating for you?

- Money. Lots of nice trading profits.
- A new place to live, bigger & nicer.
- A different car to drive.
- Upgrade computer hardware.
- New clothes.
- Afford better restaurants. No more 99-cent food. :o
- Praise from family/friends.
- Independence from having to work for someone else to get a paycheck

### NEGATIVE:

- Fear, Hope, Greed
- Sense that you need to impress family and friends with home-run trades.
- Apprehension, worry, concern over personal trading skills.

*What else motivates you to trade better, from inside?*

- for doing what they tell you to do.
- Geographic flexibility, being able to live anywhere you choose, as long as the internet connection's good.
- Ability to provide better for your family, give them nicer things.

*What else motivates you to trade better, from outside?*

Note: Although they may seem less important at first, it's really the personal motivators that often have the most genuine power over your results.

Figure out your targets and methods to acquire them before trading. Then figure out why you should care about trading anyways.

Realize that a Trader is a Trader, eg you are buying and selling something, and you need to become good at prices. You need to become good at timing.

And, you need to become great at mastering your emotions and developing the skills that will enable you to compete with professionals. Never gamble or enter an uncertain trade. Learn to spot the high-potential setups and play them, with small stops and small shares, until you become good. Then increase size and tighten up stops, to take more profit at lower risk.

## The Daytrading Lifestyle

Here are the four steps you need to get through to gain a daytrading lifestyle. How long will each one take you?

It could very well be a year in each phase. Or it could be a matter of months in each one. It's all up to you and your personal skills and temperament. The key is to make daily progress towards reaching each new step. Here they are:

**1st - Stop the Losing: Learning to Trade**

**2nd - Getting to "Breakeven-Trading"**

**3rd - Taking Small Consistent Profits**

**4th - Trading in Size for Large Gains**

THEN, you get to where you're:



**Living the Life**

I'm no millionaire daytrader playing with \$200,000, I have a decent capital base I use to make a living trading, and it works.

The key is getting thru the learning curve as painlessly as possible, while learning everything you can, constantly taking notes and watching the market.

Do you think that stock picking sites and chatrooms are useful? The educational ones are, but many are not... learn how to trade independently of CNBC and chatrooms. They were a huge waste of time when I was first learning. Do your stock screens with the free [www.bigeasyinvestor.com](http://www.bigeasyinvestor.com), use [www.quotetracker.com](http://www.quotetracker.com) to follow a portfolio of a few hundred stocks, watch for breakouts and news etc.

Living an independent lifestyle is very important to me personally, I think that living in hawaii fulltime and spending more time with my family is great - I hope you can also achieve your goals and profits by becoming a trader.

By the way, that's very important, to **set in your mind's eye the self-image of you trading stocks professionally**, with an educated eye. You knew why you bought and sold the stock at the prices and times and share sizes you did. You weren't looking for a magic bullet or a "good stock pick" to follow... you learned how to recognize plays **on your own**, and because of your continued hard, intelligent work you learned how to become a stock trader. Not a stock-pick follower, **a trader in your own right**.

Please realize that it's difficult, I keep saying this because I see a ton of undereducated amateur gamblers in the chat rooms who lose their money. After the April selloff/crash the free chat room members dropped by 30-40%! Wow a lot of guys went broke and are now flipping burgers or something. Don't let it happen to you.

Learn how to trade professionally, not to try to make "lucky" trades now and then. That's rubbish, and in the long run you'll lose, just like 95% of the people who go to Las Vegas. Ask any local, they don't gamble. They have to pay the rent. Vegas businessmen didn't build those multimillion dollar resorts out of thin desert air, they built the playground out of the public's lost money. The bank and financial centers are built in part from the trading winnings made at the expense of others as well. It's a leapfrog game. Don't be a gambler, be an educated trader, and make some real money out there.

Your goal should be to make a living at this, or at least rake in consistent profits, week after week. Sure, it takes hard work. Is it worth it? Yes, if you have discipline, intelligence and persistence. No, if you're lazy and want easy money. No such thing.

#### PERSONAL REWARDS FROM THE DAYTRADING LIFESTYLE:

Finally, I want to ask you to take out a piece of paper and list out 10 things you want to achieve as a result of your trading activities. These can be financial or non-financial...anything that makes it all worthwhile for you.

What rewards would compel you to put in all the enormous energy and work it takes to become a professional trader? What gets your enthusiasm up in terms of things you could do with extra capital? Remember, that extra capital is won \$300, \$800, \$1100 at a time, very rarely do traders take huge gains consistently, its the small consistent payoffs you're after. You can only get that with a consistent set of trade rules.

Trade well and prosper!

Worksheets

Module Three: Worksheet 1- **What to do When You Lose**



- The Powerpoint worksheet below can help you learn how to manage and deal with trading losses more effectively
- You should complete this at the end of each day or each week, depending on your individual trading style and needs
- Use it to help you deal with trading losses professionally, without getting discouraged.



## What to Do When You Lose - A Worksheet to Help

Let's face it - nobody wants to lose any money when they trade stocks. Unfortunately, this fear keeps people from taking trading losses when they're small and letting them get too big.

That common amateur approach either ties up capital in a "dog pound" of losing stocks that you need to hold onto for months or years to get your money back from (if ever), or permanent, large losses.

Learning to recognize and take smart stops is a crucial key to successful trading. I might take 2 or 3 1/16-point losses before I get the bottom of a stock, from which I then get a 3/8 - 1/2 point gain from, for example (in scalping).

Sometimes, though, especially when people are new to trading, they may make mistakes and end up taking individual losses of over \$500, which is harder to deal with. Since that \$500 loss is really \$1000 worth of buying power, with margin, it's tough to trade your way out of that loss.

This worksheet is designed to help you write down some of your thoughts, your plans and ideas for dealing with trading losses successfully.

**Small losses/stops are what I call "winning losses"** (oxymoron?); large losses are what I'd call "losing losses". Taking small stops is fine; You can afford to take many more small losses vs. several big losses, right? Timing your entries to take small losses of no more than 2-3 spreads (usually 1/4 point max for stocks priced at less than \$50), ever, is a hallmark of the successful Nasdaq stock day trader.

Let's look at how to deal with them professionally.

**You should use this worksheet (or a similar one you make yourself) to help you analyze and deal with trading losses effectively. This is a "mental/emotions" - handling type of trading loss worksheet vs. the analytical/ trading stop-loss mechanics type of worksheets found in the earlier Modules 1 and 2.**

### Notes on Trading Losses:

1. Frequently, when traders make a losing trade they feel a sense of **loss of control**, and tend to take things out on others, or on themselves through unhealthy habits. Regaining one's control over the situation, and of a sense of commitment to keep on trying, is essential to become a successful trader.
2. Don't beat yourself up; **it's a very non-logical market** where events happen that make no sense. Don't try to impose logic on a non-logical market. If there was an easy logical science to trading, everyone would do it and nobody would go to day jobs (and the companies whose stock we're trading would suffer (^\_^)).
3. The best science we can develop to improve consistent trading profits is what we're presenting in DTU, all the tips and do's and don't's of trading stocks. Even then, the traders' emotions are their biggest enemy, as they cause losing trade behaviors. Surrounding oneself with a trading plan, following the rules of the game, and making a commitment to **improve your ability to stick with your trading plan** is important.

### Directions:

1. **Print out a copy of the worksheet below and fill it out on the next 3 days that you suffer trading losses, particularly if they are large (over-\$500) losses.** (hopefully you took small stops, but you may have an occasional swing trade w/overnight gap down and end up closing a losing position at a loss).



## Dealing with Trading Losses Worksheet

Goal: Improve my ability to mentally handle the disappointment and frustration of trading losses in a helpful, professional way



Stock That I Lost Money On: \_\_\_\_\_  
 Dollar Amount That I Lost: \$ \_\_\_\_\_  
 Fraction/Points that I Lost: \_\_\_\_\_  
 Number of Shares Traded: \_\_\_\_\_

List 3 Words That Describe How You Felt When You Hit "Sell", Knowing that You Were Taking a Loss:

### Trade Analysis:

**Why did you buy this stock when you did (circle one or more):**

- TA: Saw a Breakthrough on Volume
- TA: It was Bouncing off a support level
- TA: Other Chart Pattern
- News/Earnings Release Play
- I Just Thought it was going up
- Dumb Chatroom Call
- Level 2/Time and Sales Momentum

**Why did you sell this stock when you did? (circle one or more):**

- hit my predetermined stop
- started tanking and I panicked out
- had been holding it for days or weeks and I got tired of watching it not go up
- Other reason:

### Lessons Learned:

**In retrospect, how would you have managed this trade differently then you did, overall?**

**What TA or other solid indicators could you have used differently?**

**Did any emotions cloud your judgement during the trade? If so, what did you learn about yourself and your trade management skills?**

My Personal Commitment to Changing How I Trade Similar Situations Next Time:

**This is the important part of the worksheet. Give some thought to these, and print/tape a reminder of them on one of your monitors.**

**Based on my trading losses and trade analysis, what are THREE THINGS I RESOLVE TO DO DIFFERENTLY FROM NOW ON, EVERY TIME I TRADE A STOCK:**

- 1)
- 2)
- 3)



**Module Three**

The Mental Game of Daytrading:

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Worksheets

Module Three: Worksheet 2- Finding Your Daytrading Discipline



- The Powerpoint worksheet below is designed to help you develop faster, more solid trading discipline
- It takes months if not years to develop iron trading discipline. The key is to **stay in the game long enough to survive with most of your capital intact, until you can "turn around" and become profitable.**
- Discipline, Profit, Success, they are all related.

Let's look at trading from a military perspective for a minute. You're at war with the other guys, the "open market" out there. You are fast and correct or slow and wrong - which will you be?

Finding your discipline is tough! It starts from within, a commitment to your mission of profitability, and your unwavering expectation that your trades will be right more often than they are wrong.

But there's a lot more to it than that, from a traders' personality standpoint. Many people lead undisciplined lives, they are procrastinators, they do not maintain control over their careers and their results, and end up blaming others vs. taking personal responsibility for improving their living situations. *(I chose to be financially independent, have a great family and live on a tropical island by the age of 36. I did it. I'm not special. I'm just highly disciplined and work very hard. For myself & my family, not for another man's profits)*

**That's all it takes in trading, too.**

In helping traders from around the world, one thing I find is that most are woefully underprepared to wage war in their trading activities, least of all daytrading, the toughest type of trading of all to master consistently.

As we've seen, gaining a disciplined trading approach requires the **heavy** use of metrics and actions. That is to say, you have to be able to make rapid data-based trading decisions consistently. Having predetermined exit stops is crucial, as are approximate profit targets.

Finding your discipline is a process. I find that documenting things helps me, I have brief 40-pt size printed trading reminders ("Small Stops Keeps You In The Game" etc) and encouraging notes around my workspace.

Having discipline in your life also means having fun in other areas as well. Both are needed for balance. **Look at your discipline from a military standpoint: you're on a mission in hostile territory and you want to capture profits.** You have to watch out for the land mines and enemy soldiers that dot the trading landscape. Be committed to achieving the mission. Focus. Do It.

**You should use this worksheet (or a similar one you make yourself) to help you go through the trading thought process needed to achieve better trading discipline.**

**Notes on Discipline:**

1. New traders need to have fences, or reminders, around their trading activities to help them make better trade decisions, in a faster, more timely way. One thing you can do is have your software alert you to breakouts or bottom bounces, you should also experiment with mechanical stops and trailing stops while in a trade.
2. **Lack of discipline is a career-killer in trading**, as in any serious business endeavor. Making an effort to develop the proper discipline needed for success can help you in many areas of your personal and professional life. Committing to deadlines, going the extra mile within a tight time frame, even something simple like being more decisive when order lunch or dinner at your favorite local restaurant, will be of help to you as a trader.
3. The best tool I found when I got started was to write down, on a pad of paper next to my keyboard, the stock ticker I was considering buying, the number of shares, and both the stop loss and profit target I would have for each of my trades. This might be like: SPLS 500 Buy at 20 1/8 Stop 19 7/8 Target 20 1/2-20 7-8. Something like that helps - so when you see the stock price falling you are also looking at your stop loss and have a finger on the mouse ready to click Sell when the trade goes against you. The profit target I use to sell right under whole (or major fraction) resistance, esp. if I see a wall of sellers on level 2 after a nice 3/8 to 5/8 point run up in the stock. It all helps. Discipline & Logic is your friend. Emotions are the enemy of traders. Be Spock. Completely Logical.

**Directions:**

1. **Print out a copy of the worksheet below and complete it once every few months, or whenever you feel the need to gain better discipline in a trade.**

	<b>Finding Your Trading Discipline Worksheet</b>	<b>Goal: Improve my trading discipline.</b>	<b>Where's your Stop on AMZN, \$100?</b> 
<p><b>PTDI - Personal Trading Discipline Inventory:</b> Place a check mark by each of the following that you want to improve upon:</p> <p><input type="checkbox"/> I need to focus on only a few stocks instead of watching too many.</p> <p><input type="checkbox"/> My trade entries are okay, but I am not sure when to sell and either take a large loss or a too-small profit.</p> <p><input type="checkbox"/> My trade exits are okay, but I enter my trades too late or at the wrong time; I don't get as much profit out of my trades as I should.</p> <p><input type="checkbox"/> Speed is a problem for me, sometimes I hesitate and lose profits instead of acting immediately.</p> <p><input type="checkbox"/> I need to improve my discipline and knowledge of the stock market in general; I need to understand more.</p> <p><input type="checkbox"/> My trading system needs to have more discipline checks built into it that I use, like trading alerts and stops.</p>			
<p><b>Disciplined Trading Environment:</b> List 5 things that you will put near your monitor/trade area to help you improve your discipline:</p> <ol style="list-style-type: none"> <li>1.</li> <li>2.</li> <li>3.</li> <li>4.</li> <li>5.</li> </ol>		<p><b>My Personal Attributes of a Disciplined Trader:</b> In the space below, take 5 minutes to describe what kind of trader you want to become during the next six months. Use words or phrases that best describe what kind of discipline, skill and professionalism you want to start developing that will help you make consistent profits by trading stocks:</p>	

Worksheets

Module Three: Worksheet 3- **Developing a Daily Trading Matrix**



- The Powerpoint worksheet below is designed to help you identify your trading habits, patterns, strengths and weaknesses.
- **Do you feel like you're fighting back and forth with the market, like the cartoon on the left?**
- One of the best ways you can learn to 'break out' of a choppy trading style (which only makes your broker rich), is to learn to capitalize on trading patterns and habits you have with our Daily Trading Matrix (below).



## Your Mental Trading Patterns: Make them Work for You

All of us trade using our habits and skills that we've developed over time.

The amazing lack of discipline and market knowledge I see in new traders who are trading (and mostly losing) real money makes me wonder if they're truly committed to trading for consistent profits, or are just gambling.

"If you keep doing what you've always done, you'll keep getting what you've always gotten", applies to trading as well. Maintain and enforce the skills that make you a good trader, and find a way to isolate and reduce those habits that cause you to lose money.

One of the areas that is overlooked in many books is the need to be able to quantify and reduce unhelpful mental trading habits. Telling traders to "have discipline" and "take small stops" is fine, but usually not enough.

This worksheet is designed to help you recognize behavior patterns in your trading that are both successful and unsuccessful, and reshape your trading style to one that is more profitable.

As I always say, we go for consistency in this game. I'd much rather be a trader that can get 80% of my trades right on 1/2 point trades than 20% on 1-point 'home run' trades. The sign of a professional, in trading like all careers, is someone who can consistently post the numbers that show success. Like golfing, or bowling, or going on sales calls, or playing billiards, it's the consistency that we seek to achieve.

The tools I've developed are all here to help you gradually learn how to trade consistently, and profitably.

**You should use this worksheet (or a similar one you make yourself) to help you learn to improve your mental trading habits.**

### Directions:

1. **Print out a copy of the worksheet below and complete it daily for one week out of every month (example: do it each day for the first week of every month), or whenever you feel the need to understand your mental trading patterns more thoroughly.**

## Daily Trading Matrix - The Mental Side

Goal: Identify my successful and unsuccessful trading behaviors and patterns



Instructions: Complete the following matrix each day when you're finished trading for the day. Unlike our earlier technical trade analysis worksheets and activities, this one is designed to help identify and reduce the impact of "emotional trading".

Circle the word(s) that best describe your mental frame of mind:

	Calm	Ready	Frantic	Peaceful	Tired	Energetic
<a href="#">Today's Mental Preparation</a>						
<a href="#">Today's Technical Preparation</a>	I knew support & resistance levels		I am not prepared yet	I've defined breakouts, gaps and bounces		
<a href="#">Today's Financial Preparation</a>	I was ready to go, cash and looking to trade		I was in a bunch of losing positions	My broker kept emailing me with margin calls		
<a href="#">Readiness To Enter Trades</a>	"Scared to trade"		"Eager to trade"	"Uncertain to trade"		
<a href="#">Readiness to Exit Trades</a>	I didn't use stops		Stops were identified	I didn't know where to place my stops		
<a href="#">Sensitivity to Market Conditions</a>	I entered and exited based on composite and sector index direction		I ignored the market indexes	I knew the current reports and other key economic data that were due today		
<a href="#">Hopeful, Greedy, Fearful</a>	My trading today was highly emotional		My trading had very few emotions in it	Today, I was Spock.		

Now, compare your day's Profit and Loss with other days for which you've completed this Daily Trading Matrix. Look for patterns that were clustered together on profitable days, and identify and try to reduce patterns that led to losses. Take market conditions into account too, of course... did you do well on an up day and limit your trading on down days?

Today's Profit/Loss: \$ \_\_\_\_\_

### Module Three

### The Mental Game of Daytrading:

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MODULE 3

### Worksheets

### Module Three: Worksheet 3- Increasing and Decreasing Trade Sizes



- The Powerpoint worksheet below is designed to help you learn the important skill of Position Sizing. This is when you add and subtract to your position in a single stock based on profit targets and chart patterns.
- You may, for example, buy 400 CPQ at 22 1/2.... then add another 100 at 24 1/8 in an uptrend, then sell half (200 shares) later at 25 7/8, and the other 200 at 26 5/8.
- Scaling in and out of positions like this is a very important skill to learn. You should not always be trading in "all-or-none" type trades, you want to adjust your total position size based on price action and chart patterns.
- You do this to lock in a percentage of profits at a certain price and "try for more" with the rest. It's a professional variation of using trailing stops...every pro daytrader and market maker trades like this, you should too.
- While not a 'mental' trading technique, I thought it might be good to add it in here since it involves a change in the way most beginning traders consider managing their positions.

## Increasing and Decreasing Trade Sizes

Adding to a position does not mean "averaging down", although that may be one technique that

The technique is to:

people are familiar with. As opposed to that (generally losing) method, we want to instead look at ways to dynamically change our total position size based on price action and chart patterns.

Professional daytraders trade in total lots of 1000 shares, generally speaking, and may scale up from an initial position of 300 to add to a winning position. As I mentioned in an earlier lesson, you should not add to a losing position, and should not add to an uptrending position in gradually larger sizes.

Instead, you want to play the probabilities. Let's look at a few examples:

- Buy/add smaller share sizes in winning (uptrending for long) positions, til you reach a top or resistance level, then fade out of the position either all at once or gradually, with the biggest number of shares added at the top. **Example:** I buy 300 DCLK at 46 1/2...buyers come in and I add another 100 at 48 1/4, and add a final 100 at 49. I then sell all of them at 49 3/4 around 10:15 am, or, sell 300 at 49 3/4 and use a trailing stop for the other 200, eg sell them if it drops to 49 1/2. Total profit: \$1225

This worksheet is designed to help you add and manage trade size position scaling more successfully. Yes this technique costs a bit more in commissions, but is well worth it when you learn how to manage it professionally.

**You should use this worksheet (or a similar one you make yourself) to help you learn to manage your trades by using the technique of "position sizing".**

**Directions:**

1. Print out a copy of the worksheet below and complete it whenever you are contemplating initiating a new large position (either long or short).

### Increasing & Decreasing Trade Sizes


*Goal: Identify my successful and unsuccessful trading behaviors and patterns*

Use this worksheet to help you decide when to add or subtract from a current position you have initiated.

**INITIAL BUY OR SELL DECISION POINT:**  
fill in the blanks

TICKER: \_\_\_\_\_

INITIAL POSITION SIZE:  
\_\_\_\_\_

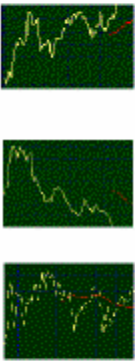


**SECONDARY BUY OR SELL DECISION POINT**  
(after you've initiated a position)  
circle which one you'll do...

**BUY more?**  
(add to current position)

**SELL?**  
(stop out)

or, No Change



**FINAL SELL (or cover) DECISION POINT**  
(as you're exiting the position)

**SELL THE ENTIRE POSITION?**

**SELL PART OF THE POSITION w/trailing stop for balance**

*Example:*  
I've just bought 600 SPLS at 16 3/4 (initial size)

The stock has increased in price to 17 1/8 and has an uptrending wedge (bullish) pattern, so I add another 400 at 17 1/8

SPLS gets more buyers, we're up in the high 17's. I know SPLS has a 1-day intraday range usually, and, the nasdaq composite has just turned downwards and my L2/T&S shows lots of sellers at 18. So, I sell the entire lot for a 1 1/8 (\$1125) profit.



**Module Three: Activity 1 - "Thinking Like a Professional Trader"**

- **Professional traders look at their work** as any career business person does, with a sense of **responsibility** towards producing results, of meeting the **expectations** of their boss, of being **competent** and effective in what they do. So should you.
- **It helps to imagine having a "pit boss" looking over your shoulder as your trade.** Is he going to yell at you for entering that last trade you entered, or say "looks good, let's see where it goes?"
- What would an imaginary traders' manager say as you enter or exit each of your trades? If he's a coach-type he might ask, "okay, why did you buy there?", "was that the best place to sell?" "good effort, you got a good piece of the momentum on that last one!" etc. Be your own "pit boss" and critique each of your trades with a practiced, professional eye.
- In turning professional with my trading, I found that over time I evolved to "not being surprised" at anything that happens for a stock. Instead, **I became opportunistic and faster** in what I did. If I see a stock gap down, I'll check my realtime news, the 5-day, 10-day and 6 month chart for 100- and 200-day MA and chart pattern etc, all in the space of 10-20 seconds. **Then I make a trade decision:** should I buy, short, or wait? Then I execute it.
- Developing a professional traders' eyes for the market takes **hundreds of hours of practice** in market watching. **There is no other way.** Watch realtime tick charts and time & sales 'tapes' over the months ahead to gain the experience in seeing how the market behaves.
- It does you absolutely no good to just look at chat rooms and stock-picking sites alone. Sorry if that's not what you wanted to hear. Those resources can certainly help accelerate your learning, if you choose wisely, and that is good. But **to trade for a living you need to do it on your own.** No CNBC, no chat rooms, no stock pick of the day sites. It takes time.
- Trading stocks is a profession that takes a minimum of months, and usually at least a year or two, to become good at. It is difficult work and I have never said otherwise. It can be worth it, if you are persistent and willing to be strong at doing what it takes to succeed.
- **This activity should help you learn to evaluate trade opportunities and look at the market like a professional trader does. Remember, the vast majority of would-be daytraders overtrade and "blow out" (lose) their accounts in a short time. Do not become a statistic. Learn to slowly do this successfully. Commit to it.**

**Pros Respond Differently than Amateurs Do:**

Situation:	Pro Traders' Action:	Amatuer/Losing Traders' Action:
1. <b>Divergence exists in the market, semis (\$SOX) are stronger than internets (\$GIN) today.</b>	1. Ignore/turns off charts for all 'nets, puts up a few more semiconductor charts to look for trade opportunities (takes 1-2 minutes).	1. Still watches the same group of stocks, including a 'favorite internet' they like to trade. May try to buy the 'net on a dip, even though the sector is weak that day..
2. <b>A trade is going against him (or her).</b>	2. Exits immediately, waiting for a better re-entry price.	2. Waits, hopes for a turnaround. Position goes so far against them they hold on to it, putting another mutt in the "dog pound" of stocks they stay long in as a 'investor' vs. trader.
3. <b>Trade is going with him (or her).</b>	3. Takes some fast profit, sells the position off a bit at a time, small shares at small gain, more shares near the top until position is completely liquidated by the time the stock starts to weaken before lunch.	3. Sells the whole position for a tiny profit, even though there's still buying strength in the stock. Does not partially fade out of a 500- or 1000-share position 200 or 300 shares at a time.

- |  |  |   |
|--|--|---|
| <p><b>4. It's lunchtime.</b></p>   | <p>4. Goes eats lunch, or quits for the day if it's been a profitable day. Golfs/shops.</p>  | <p>4. Watches a chat room, trying to make low-percentage lunchtime trades, nibbling down capital with shakes and wiggles. Brokers love this trader.</p>   |
| <p><b>5. Time and sales shows blocks going off as stock price rises.</b></p> | <p>5. Pro trader bids in between the spread, adds to position based on T&amp;S momentum, fades the position out when blocks start going off in opposite direction.</p> | <p>5. Can't read time &amp; sales for their stock, since they're using a free cheap service. Doesn't invest in proper tools, using a slow discount online broker. Gives money to the professionals.</p> |

## Activity to Help you Trade Like a Pro Does:



Get out a piece of paper, and work on developing 2-3 specific trading actions for each of these key areas. They are designed to help you think (and trade) like a professional trader does.

### Technical Analysis: Chart Patterns

- After looking at hundreds of charts, identify one chart pattern you want to be especially "on the lookout for" that can be profitable for you to trade. (Examples, opening gaps, volume reversals, bouncing off support or breaking through resistance on volume).
- Choose 1-2 technical indicators you want to use closely. I recommend starting with volume and moving averages.

### Market Sector Scan & Analysis

- Identify 3 different market sectors you want to keep a close eye on, and on what exchanges they are traded (eg Nasdaq semis and internets, beaten-down dow stocks that are bouncing, retailers etc).
- For each sector, identify both the "generals" (eg YHOO EBAY AMZN AOL for internets, INTC AMAT KLAC for semis)
- Activity: during the next trading week, I want you to identify Which sector was strongest for that day. Was it the semis? The nets? Software? Biotechs?
- Finally, practice paper- and realtime trading stocks within the sector leader for the day you're trading.

### Trading Someone Else's Money

- A pro trades with client's money in a fund account, and he or she is accountable to the company's trading %age expectations. Pretend you are trading for a friend's account, and you need to generate capital quickly through trading profits. Would you really have entered that last trade if it was someone else's money? Why or why not?
- In a sense, you are already doing this, as the money you earn or lose will probably impact the lives of others close to you.
- Think of yourself as Goldman-Sachs "Head Equities Trader"-in training. What do you need to do now to become head trader for this company? How will you start trading differently?

### Daily Trading Expectations

- Setting arbitrary 'profit targets' should only be done on a "daily average" basis, eg don't say "I want to earn exactly \$500 a day each day", say instead "for the month of April I want to earn a profit of \$10K, which averages \$500/day.". Why?
- On strong days you should trade much more than on weak or choppy days, depending on your trade style. If you're a scalper, you want choppy days, if you're a shorter, you want sell/weak days.
- Also set trading process goals (eg "I will trade 100% of the time I see a high-percentage trade opportunity).

Activities



**Module Three: Activity 2 - "Becoming Focused on the Trade"**

- It is essential that you narrowly focus your attention completely on the trade that you are playing at any given point in time.
- Trying to juggle 30 stocks, participating in a chatroom, surfing financial sites and listening to CNBC all at the same time you're in a trade is a disaster. Adding noise from family/friends/other sources makes it worse.
- The only thing you really need to be focused on is time and sales, after you've confirmed a chart pattern that looks like a good setup....use level 2 to time your exact entries/exits.
- If you're in a professional trading room, make sure you're around traders who are consistently winning...a few winning traders w/80% losers is Not a place you want to be. That includes chatrooms too.
- Let's look at how to get yourself in the frame of mind to trade successfully, how to build a concentrated frame of mind for "microtrading" that's needed to win.
- Think of the whole market as a cloudy day, your goal is to have a laser-like beam of sunlight that penetrates the clouds to allow you to profitably enter and exit. You can't pay attention to the scenery, you must close in on a trade like an eagle swooping out of the sky to nail its prey...absolute concentration is a must.
- Use earplugs if they help. Set your monitors against a wall, so there's no distraction (I close the blinds to my ocean view here in hawaii when afternoon trading so I don't lose concentration).
- Look for things in your trading environment to help you become the most concentrated you've ever been.
- Think back to studying for final exams in college...you need to have that library/study-hall type mentality, with 100% focus. Don't trade til you can achieve it.
- Try doing each of the four tips below, and check your trading progress.

**Setting Up Your Trading Software**

- A cluttered PC monitor makes it tough to trade - make sure to have at least your trade execution window always in the same place on your desktop (and get two monitors).
- Make sure to narrow the focus of how many different software programs you have running at the same time - too many can slow your pc down and make it difficult to concentrate on the trade.
- Experiment with different font sizes, different fonts, and color combinations. Make it interesting to yourself and easy to read and understand.
- Keep your software's extra functions to a minimum, don't use all the bells and whistles unless they really help you trade. Analyze your winning trades.
- Try not to shuffle back and forth between too many windows each day - it's tiring (I remember back when I only used 1 monitor, what a headache!) and takes your energy away from trading.
- Check to update the latest version of all your software. For example, 16% of the thousands of people who visit us here at DTU are still using IE4.0, for example. Stay on par with your competition, and get the best and latest software possible.

**Clearing Out Distractions**

Place a check mark next to each of these potential sources of distractions for you during your trading activities:



- \_\_\_ Television (eg CNBC) and/or radio on
- \_\_\_ Family members and/or pets making noise
- \_\_\_ Environmental noise, eg street traffic, neighbors
- \_\_\_ Internet distraction: you surf around too much during trading hours
- \_\_\_ Financial information distraction: you are looking at too many 'inputs'
- \_\_\_ Cluttered work area - you have disorganized stacks of stuff laying about
- \_\_\_ Mental distraction #1: you obsess over losing money and are fearful
- \_\_\_ Mental distraction #2: you focus on the financials (how much can I make?) vs the trade mechanics and chart setup patterns
- \_\_\_ Other (specify): \_\_\_\_\_

**Personal Action Plan:** On a pad of paper, write down 1-2 things you will do to clear away and reduce each of the distractions you checked in the area above.

**Critical:** give yourself a timetable & deadline for implementing each action.

### Finding a Mental 'Anchor' Statement

Finding a "safe harbor" in your mind, as a trader, helps you achieve mental discipline and security. There's two steps to this activity:

**Step #1: Write down 5-6 words or short phrases** that you associate with fun, pleasurable, rewarding activities (note I'm excluding 'vices' like eating junk food etc here). I want you to get in the mental state of being comfortable, of achieving personal happiness. What are these words, for you?

- .
- .
- .
- .
- .
- .
- .

**Step #2:** This can be fun - combine the words and phrases you just came up with into 1 or 2 sentences, a "mental anchor statement" that describes the state of mind you want to achieve in your trading activities.

At the end of each day, your goal is to feel this way. You might want to include technical success phrases ("I traded the best I could and kept small stops", "I took consistent profits" etc).

**My anchor statement(s) are:**

- 1.

2.

## Committing to a Focused, Successful Trade

Finally, let's look at some concentration tips to help you make a solid personal commitment to yourself and your family to make successful trading a way of life, not a surprise.

#1. Practice some of the first steps of meditation: a few [slow, deep breaths](#) will help each morning

#2. [Focus on one success symbol or sign with your eyes shut](#), for a few minutes. I like to create a visual image of a green P&L statement, eg the number [P&L +\\$1100](#) in green is a motivator for me, my end of day target.

#3. [See stock charts in your imagination](#), with your stops carefully taken along with your profits. A successful trader takes small stops, and larger profits. Both are critical.

#4. [Tell yourself the types of things you need to win](#): I need to check my chart patterns, only carefully pick the high-percentage setups and sit out the "iffy" - questionable trades, especially longs in a down market, for example.

**Module  
Three**

[The Mental Game of Daytrading:](#)

[Back to  
MODULE 3](#)

Activities

### Module Three: Activity 3- "Using Your "Lessons Learned" in Trading

- One technique that I've found useful in building consistent trading skills is to build safeguards in my trading style to alert me to low-potential situations that I should not be trading in.
- Another important tip is to be sure to capitalize on all that you've learned in each trading week, so that you increase your profits steadily over time. If you only do well in bull markets, then you might want to look at this area as well. It's important to be able to trade in all 3 market environments: bear, bull, and 'choppy'.
- Let's say, for example, that one of your 'lessons learned' is that it's a good trading strategy to buy a certain stock back once it's broken above a key resistance level and has consolidated for at least 8 minutes. The challenge becomes, how do you now standardize this knowledge in your trading approach?
- Repeating the same trading errors over and over again is also costly, it is in your best interest as a trader to avoid these mistakes using a set of trading rules and guidelines that you use as automatically as you drive a car.
  - You know to brake at red lights (eg take small stops).
  - You know to accelerate when there's space in front of you (add to winning positions).
  - You know to take curves slowly (eg avoid trading in lunchtime or other low-volume times)
  - You know to give pedestrians the right-of-way (eg don't trade against our "4

- "horsemen" strong market makers (SBSH GSCO MLCO MSCO).
- etc.
- So, this activity is designed to help you use all the things that you've learned via trial and error over the months to build a more successful trading method that works for you, with the stocks you trade and the time horizon that you trade them in.
- It is an individual process for each trader, it is our hope that these guidelines will help you to build more consistency and success into your personal trading style.



**You must learn how to make more consistent, profitable trades that are booked repeatedly. An occasional win that's offset by many losses is not acceptable.**

**The most important goal is to preserve your capital - to do this you need to identify your trading mistakes and find a way to avoid making them again.**

**Of course, you want to also figure out "what you did right" about winning trades that wasn't due to chance - what were your effective trade entry and exit rules that help you win consistently?**

## Activities to Help You Build Trading Consistency



- Make it fun, first of all - **pretend you're a market maker at Goldman Sachs** trading an account with other people's money. How would your trading be different? Would you take the same chances?
- Although it's not exciting, it's very important that you: **Keep a brief daily trading journal**, with your trade entries, stop losses, and profits for each day's trading.
- In a place that you can see throughout the trading day, keep a list of several **trading guidelines in large, bold print** where you can see them. As your knowledge grows, adapt these trading rules to be more specific. Eg, I have "Tight Stops - No Exceptions - 2 spreads/1/4 point is your max stop loss" still posted.
- **At the end of each week, make a list of "Things I did consistently" and "Things I did not do consistently"**. Never mind if they were right or wrong, for now - just make a list of things about your trades that were both consistent and inconsistent, and work on improving.
- If it helps, have fun rewards/punishments for being a consistent, disciplined trader vs. inconsistency. **If you traded according to your trade guidelines, even if your profits were only modest, then reward yourself.** If you broke all your rules and took a larger-than-necessary loss, look for ways to change it the next time you're in a similar trade.
- **Make a firm commitment to yourself** to "become a consistent trader". Look at yourself as a professional. If it helps, dress up a bit before the trading day starts and pretend you're at work with the head trader of GSCO watching over your shoulder. What would this professional say to you during your trades to help you win? Remember, winners are consistent and profitable.

## Activities to Help You Avoid Mistakes: Your Costly "Lessons Learned"



Let's all agree to learn from our mistakes so we hopefully don't repeat them, okay? Here's the technique I've found successful to help trim trading losses to an absolute minimum.

Remember, the cost of commissions and a small 1/4-point loss is fine compared to commissions plus a 1-point or more loss, right?

Here's what to do:

1. First, print out your last month's trading account history, available from your broker's site.
2. You will annotate 1 month's trade history with 2 felt tip markers, one green and one red.
3. Use a green pen to connect the profitable trades, and a red pen for the losses. Write the dollar figures in, as I have in the example below:

Symbol	Shares	Trans. Type	Price
DCLK	400	Buy	42 1/2
RNWK	300	Buy	38 3/8
ATHM	1000	Buy	18 1/2
DCLK	400	Sell	44 3/4
RNWK	300	Sell	39 1/2
ATHM	1000	Sell	18 1/4

Handwritten annotations: A green arrow points from the DCLK buy price (42 1/2) to the DCLK sell price (44 3/4) with '+900' written next to it. A red arrow points from the ATHM buy price (18 1/2) to the ATHM sell price (18 1/4) with '-360' written next to it. A green arrow points from the RNWK buy price (38 3/8) to the RNWK sell price (39 1/2) with '+369' written next to it.

Okay, now you need to find out Why each was profitable and/or a loss...

Simply make a list with columns for the symbol, your net profit/loss and why:

STOCK:	Profit/Loss	REASON:
DCLK .....	+900 .....	Bought at bottom end of trading range, sold at resistance
ATHM.....	- 250 .....	Got stopped out (small stop), chart pattern reversal
RNWK.....	+ 339 .....	Momentum play, Time & Sales was all buyers when I entered

This was a very useful tool for me, each day I would print out my trade records and attach a reason to the profits/losses I made to help me learn from my trading experiences. It's an "A" type activity.

## Activities to Help You Repeat Successes: Your Profitable "Lessons Learned"



The activity above will help you improve on both areas, minimizing your mistakes and maximizing your profitable trades. Let's look at another set of ideas for helping you to repeat these successes. Remember, you cannot improve what you do not understand. That's why all these activities and worksheets are helpful, they are a guide to build your professionalism and trading skills.

<b>Time of Trade Buy/Sell</b>	Carefully note when your winning trades are entered and exited, on general. I used a graph and found my winners were usually entered around 10:30 +/- 15 minutes.
<b>The Stocks You Trade</b>	Take a close look at the types of stocks you've traded profitably vs the ones you've lost in. Avoid the cheap oversold stocks, buy quality stocks on dips.
<b>Number of Shares Traded</b>	For your winning trades, see if there's a pattern to the number of shares you're trading, as well as your trade length of time (eg scalp, overnight hold etc)
<b>Trading Equipment/Broker</b>	Trying to scalp daytrade with a 56k dialup connection is bad. Make sure to adjust your trading style to your capital and equipment capabilities. Is swing trading ok?
<b>Reasons for Buying &amp; Selling</b>	Ok, you're looking at your profitable trades - see what patterns emerge regarding your buy/sell signals - was it a chart pattern? Time of day? Time & sales? List it out.
<b>Position Sizing: Scaling In/Out</b>	We covered this in a previous lesson - find out for yourself if you're good at this technique. I find I like to sell half at a good profit target, and use a trailing stop for the balance. Find what works for you.

Activities

Module Three: Activity 4 - "When All Else Fails...."

- Remember the market tank in April and early May 2000? Many traders were wiped out. Many others suffered huge losses. It didn't need to be that way.
- There are many things that cause frustration during trading: bad fills, wrong trades, market unpredictability, and financial losses.
- Frequently, traders will overtrade to compensate for trading losses, making the situation even worse.
- This activity is designed to help you if you feel like you're "down so low the only way left is up", so to speak.
- Most successful traders have had their ups and downs - this is true of successful people in all walks of life. Becoming a winning trader takes persistence, and above all else, caution.
- Instead of giving up, or trading even riskier plays in an attempt to "win back" trading losses, let's take a step-by-step approach to gradually get back to even, then on to success.
- When all else fails, you should increase your efforts, but in entirely different ways than you've taken before. Think about golfing, for instance - if you keep slicing the ball, you may change your stance, your grip, your clubs, and the course you play on, all to no avail. It takes a change in your swing dynamics.
- The analogy to trading is that you need to isolate the things that are keeping you from becoming successful, and experiment until you find a better combination of trading strategies.
- Maybe you're watching the market too much....there is no reason to watch the market all day long, it can get boring after years....instead, scale back your market watching time from 9:30am to 11:30am each day - no more. Maybe you're playing the wrong stocks, maybe you need to learn more about technical analysis and chart patterns. I don't know - it's an individual journey for each stock trader.
- Let's do some activities to help recover and get back from the edge:

When all Else Fails..Or,  
"What To Do When You Feel Like Giving Up"



Papertrading to 80%

- Stop losing real money for awhile - regroup and modify your trading strategy.
- Practice on paper as closely as you can to the 'real thing'. Get the free cybercorp.com simulators or just a pad of paper and pencil and go for it.
- Try many different trading techniques if the one you're using is inconsistent or provides poor profits.
- Practice trading "on paper" until you get to

Trade Listed NYSE Stocks

- NYSE stocks are much less volatile and have narrower trading ranges than Nasdaq stocks, in general.
- Try trading NYSE stocks for awhile, there's plenty out there and they're all good for trading: CPQ T HET MGG JNJ PG BBY F A MRK YUM etc.
- Trading NYSE stocks gives you a good opportunity to improve your "tape reading" skills, as you will be watching time and

where you're roughly 80% correct, consistently, before going back into the market with real money.

sales, not a level 2 window, for trading NYSE stock.

- Try trading NYSE stocks over a 2-4 day time horizon as well...you may be surprised at the improvement in your trading profits.

## Talk with Other Traders

- Sharing trading stories with other traders in person, by phone and by email is a great way to build a sense of community and understanding.
- Try to find a local group of traders to meet with informally once a month or so. (You might start with DTUSA, [www.worldwidetraders.com](http://www.worldwidetraders.com), for a start).
- Get a group started in your local area. Put a free ad in the local business section of your newspaper's "Current Events" column, eg "Daytraders of Portland" meeting at the Bistro Cafe, 12:00-1pm, call (123) 456-7890 for directions. Get involved - start a networking group. (or, call a few local brokers and ask)..
- In addition to sharing trading strategies, talking with others, even via email, provides you with additional energy to trade day after day.

## Go From Day to Swing Trading

- If day trading ain't your thing, then don't fight it. You might want to try "swing trading", short-term momentum trades lasting several days or so.
- Swing trading is less stressful, and you can use wider stops (with a higher profit target) than we do in daytrading, although you incur greater risks as well.
- If you're consistently losing at daytrades, then take a break, learn a lot more, papertrade, and then try swing trading with small shares (typically 100-300).
- Swing trades let you enhance your chart pattern/TA skills as well.
- You can use a cheap online broker and no level 2 quotes if you're swing trading, and still profit very well.
- The main thing is to experiment until you find a trading style that's comfortable and profitable for you. Expect this to take some time. Use small stops so it doesn't cost a lot.

## Take a Break



- Take a few weeks off from the market if you're tired, frustrated and beaten.
- When you're frustrated you're likely to be more stressed and less able to trade successfully.
- Put the odds in your favor by sitting out a few weeks of the market - don't worry, it'll always be there.
- During your "time off" from the market, resist the urge to look at financial websites or watch CNBC. Take a real, 100% Break from the market.
- When you're ready to come back to the market, take stock of what you plan to do differently this time - what changes are you making in your stop loss strategy, and how are you going to change the stocks, share sizes, and time intervals of your trades? Experimentation is key to success.
- It's difficult to take a break from the market.
- It's difficult to take a break from the market, especially if it consumes all your time. Look at a break as a 'winter break' from school, where you can spend more time with family and friends, or simply by yourself in a new hobby or something you enjoy. (I like watching movies and golfing).

## Read More Books

- We should all be continuously learning from other traders who have identified profitable trading strategies. Apply the authors' ideas that make sense and blend them with your own trading experience.
- Many books have been written about the financial markets and about trading skills - read as many as you have time for and highlight them as you did college texts. Ideas that are particularly useful should be clipped from the books and put in a "Master Trading Strategies" notebook. I find this is helpful.
- Although many books are 'fluff', there are many good ones out there as well - focus on the technical analysis and chart pattern ones the most.
- Also visit more websites - although most are junk there are a few excellent ones, such as [clearstation.com](http://clearstation.com) and [equis.com](http://equis.com).
- You must value the hunger for new trading skills in order to succeed at this game. Do not search for magic, instead, search for disciplined, practical, simple trading techniques that generate profits most of the time for people.

## Module Four Swing Trading Strategies

Click on each link for a new daytrading lesson. Be sure to complete the trading worksheets and activities for each module.

[Back to DTU CAMPUS MAP](#)



Click on each line for daytrading lessons from the list below. Keep checking back every couple of days for new lessons, activities and worksheets. An underlined link means the content is now available.

Trading Lessons



= Updated pages w/in last 48 hours.

DTU Module Four Lessons:

- [Introduction to Swinging It: Major Differences in Swing vs. Day Trading](#)
- [Avoiding Low-Percentage Swing Trades and Bad Investment Risks; Chart Pattern Intro](#)
- [Choosing the Best Stocks for Swing Trading](#)
- [Risk Management for Swing Trades Part 1: Managing Time in the Trade vs Optimum Share Sizes](#)
- [Risk Management for Swing Trades Part 2: Using Stops, Portfolio Management & Diversification](#)
- [Swing Trading Technical Analysis & Charting Part 1: 20/50/100/200 MAs, using MACD](#)
- [Swing Trading Technical Analysis & Charting Part 2: Identifying Trends, Channels and Overbought/Oversold Conditions](#)
- [Understanding the Mechanics of Swing Trading: Recognizing Recurring Stock Patterns & Likelihood of Fibo Retracements - \*New!\*](#)
- [Chart Patterns: Buying into Pullbacks vs. Dead Cat Bounces](#)
- [Identifying High-Percentage Swing Trading Patterns: It's Saying "Buy Me Here"](#)
- [Knowing When to Turn a Day Trade into a Swing: Overnight Gaps and Chart Patterns](#)
- [How to Clear Your Profits in Swing Trading: Taking Money off the table at the best time](#)
- [Making the transition from swing trading into day trading, and vice-versa](#)
- [How to Make a Living by Swing Trading Stocks: a Professional Traders' Advice](#)
- [Answers to DTU Traders FAQ's Re: Swing Trading: Send us your questions!](#)

*Note: Module 4 is in the process of being posted; as each new page is developed it will have a link underline and an icon next to it to alert you. I'll mark new content "-New" for our traders.*

Worksheets



[Click here for Powerpoint viewer program](#)

[Click here for MSWord view program \(3.5Megs\)](#)

- [Trading Sectors and Market Indexes: Swing Trading Big Patterns](#)
- [5-Day and 10-Day Swing Trading Patterns](#)
- [Timing Your Buys for Swing Trades](#)
- [Portfolio Management: Balancing Your Swing Positions](#)



## Activities

- [Swing Trading Research: Picking 12 Stocks for Swing Trades](#)
- [Swing Profit Play #1: Bottom Fishing on Small Shares](#)
- [Swing Profit Play #2: Trading Breakouts and Uptrends-](#)
- [Swing Profit Play #3: Playing Positive News and Earnings Trades](#)  
*- New!*
- [Scaling In and Out of Your Swing Trade Positions-](#) *New!*



- Introduction to Swinging It: Major Differences in Swing vs. Day Trading

● **Main Points:**

- There are many differences in day vs. swing trading that are worthwhile to learn about. Each technique can be highly profitable *when used correctly*.
- **Our primary focus in this module on Swing Trading Strategies will be on technical analysis and winning trade management:** understanding how to scale in and out of trades, manage trade sizes and recognize high-probability chart patterns that are worth trading for profit. Not exotic detailed TA, but rather an expansion of the chart patterns that are not in most books that you can use to your trading advantage.
- The rules of each type of trading are vastly different; one of your keys to success will be to know when to exit vs. stay in the trade, and to not mix up your daytrading with swing trading efforts. Do Not hold on to a losing daytrade and say "well I guess I'm an investor/swing trader now"...**You must enter and exit each type of trade differently, using different rules. Remember this.**
- Throughout this module, you'll learn new ideas on how to work a trade to your favor, using appropriate risk management and entry/exit trading skills. Realize that unless you are extremely well-capitalized (eg you can tie up blocks of capital for extended amounts of time tie up blocks of capital for extended amounts of time "til a stock comes back"), your risk and reward are higher for swing trading than for daytrading.
- Both your stops and profit expectations are much wider for swing than day trading; we'll learn how to work this to your advantage in later lessons.
- **If you are losing money daytrading, you can rebuild your confidence (and hopefully your trading capital) by scaling back to 100-200 share size swing trades,** "casting a wide net into the market" vs. the rifle/pinpoint style approach that is required for daytrading.
- Give yourself time to experiment with different styles of trading; many people make as much or more swing trading than they do in day trading; **both are perfectly valid styles of trading stocks.** It's up to you to try out new styles until you come up with the one that best matches your skills, profit/loss expectations, and money management results.
- In terms of your lifetime progress as a trader, I would begin as an **investor** (buy mutual funds etc, have a 6 month plus roundtrip trade time horizon), then move to **swing trading** (2 days to several weeks), and then finally, after you know the market fairly well, try **daytrading**. Then, use the techniques in Module 2 etc. for fast scalping profits as a maximum revenue technique. But, it's fine (and recommended) to stop at swing trading if that's where you make the most money at.
- Daytrading in the truest sense of the word is exceptionally difficult. The Module 1/2 content has gotten you started on many of the undocumented pro techniques and strategies that professional daytraders use, and we'll share much ~~and professional daytraders use, and we'll share much~~ more in later modules, as market conditions and trading techniques change over time (eg moving to decimal trading this summer).
- For now, see the "major differences" table below. We'll add charts sometime soon at the bottom of the page. Think of swing trading like Volleyball, and Daytrading like Tennis/Racquetball. What are the differences?

**Swing Trading**



VOLLEYBALL - slower, lobby/spike

vs.

**Daytrading**



TENNIS - fast, quick exchange

**SWING TRADING DEFINED:** Trading stock for short-term holds, usually from overnight to 1-2 weeks maximum. My typical swing trade round trip is 3-5 days.

**TRADING STYLE:**

**DAYTRADING DEFINED:** Daytrading can be one of several types: **Scalping daytrades** (300-1K shares) for 1/16th to 3/8 or so gains, rapid buying and selling, usually no longer than 5-10 minutes maximum. **Momentum daytrades:** trading a stock that's moving for anywhere from 5 minutes to 2-3 hours. **Swing daytrades:** Trying to buy the bottom and sell the top of

- Requires patience, lots of it
- For the occasional trader, who may enter and exit from 3-20 positions weekly.

#### DECISION CRITERIA:

- fundamentals and analysts ratings are important
- technical analysis of both short-term (5-10 day) and long-term (3-6 month) trend and volume patterns is useful
- look at the 20-day, 50-, 100- and 200-day moving average lines for your stocks to see where fund managers are likely to put their stops and buy programs.
- research and TA play an important role; we look at breakouts, channel plays and bottom bounces, as well as earnings release dates, the stock price's response to mergers/acquisitions, and other news.

#### TIME FRAME - ROUNDTRIP:

- Since profit expectations are higher for swing trades, most swing traders stay in their positions from several days to several weeks before exiting.
- We try to enter at the low of the day, so entries are usually at one of three places: the start of the day, sometime over lunch where the stock has sold off, or at the end of the day if there is a price breakdown to a multi-day support level.

You can also enter near the end of the day if it's a high-of-day to play the anticipated morning gap up, though this is more an "overnight hold play" vs. a swing trade.

#### STOPS & RISK MANAGEMENT:

- Stops are much much wider in swing trading; and your profit objective is larger.
- For oversold stocks, you should look at a 6-month or 12-month chart at first, then a 5- or 10-day chart, to get a feel for the trading range. Then the 20/50/100/200MAs.
- Stops for swing trades can be as high as 5-10% (but no higher), eg if I bought WMT for a swing trade at 50 I would let it go down to about 45 max (10%), before stopping out.

a stock during the day, may hold for several hours and sell near 3:30-4pm.

#### TRADING STYLE:

- Requires fast decision-making ability
- For the active trader who wants to trade a minimum of 3-5 trades daily, if there is a good trade to play. Many professional daytraders may do from 50-300 scalping trades each day.

#### DECISION CRITERIA:

- what's an analyst? who cares about fundamentals? what's in motion now?
- technical indicators are more momentum based; including stochastics, volume, and intraday support/resistance levels
- research is more on stocks that are trading on higher-than average volume or are responding to news, earnings, or other momentum-driving events

#### TIME FRAME - ROUNDTRIP:

- Daytrading roundtrips are typically less than 20 minutes in and out, and may last up to a maximum of the full trading day (unusual).
- Since prices tend to weaken over lunch, most daytraders will play for a morning momentum run (in and out multiple times from premarket through 11:30ish), close out before 12:00, and perhaps play the breakouts or breakdowns during the last two hours of the day, from 2pm-4pm.

#### STOPS & RISK MANAGEMENT:

-Daytrading stops are never more than 1/2 point or so, depending on the stock price, and usually we'll use from 1-3 spreads as our stops.

For less expensive stocks, eg \$12-\$40/share, our profit objective is small, eg 1/4s to 5/8s, maybe up to 1 1/2 points.

Percentage-wise, that means we limit our losses to about 1-2%, and shoot for a 3-5% win rate..the ratio should be 3:1 or 4:1

- We will look at chart patterns for many swing trades throughout this module, to acquaint you with trading opportunities as they arise.

- Unlike many books, I do believe that averaging down can be okay for *some* swing trades in *highly-rated* stocks (only!) that are oversold for *certain* chart patterns (only!); we'll look at some of these later.

- The "reverse pyramiding" approach may be ok here, eg buy 100 at 50, add 200 at 48, add 300 more at 46 (total average position price now at 47). Lets say it consolidates at 45-46, then heads back up, your stop is at 45; in 8 days we're at 49 7/8, you sell the whole lot for a \$1200 profit, or hold another couple of weeks and sell at 52 for a bigger profit etc... There are more "dont's" in this approach than "do's", we'll look at how to manage this correctly in a later module.

- In general, I prefer to bottom fish over buying breakouts for swing trades, I haven't lost on a swing trade I've made in over a year, but this is a matter of personal preference. Bottom fishing in a "channel", eg SPLS from 21-25 is safer than bottom fishing in a stock that has no bottom (like the retailers lately, S ANN BEBE ROST, though they may be ok for position plays).

In bottom fishing swing trades, as in daytrades, you must see a volume reversal, showing real buyers are back (not just short covers, which will give a short pop, then continued selling).

#### SHARE SIZES:

- I tend to keep a swing portfolio of smaller share sizes for stocks, usually just from 100-300 shares in each of from 2-6 stocks I'm holding. My current swing trades: DBCC HAS CCL VISX AOR YUM JBX SPLS (3/4/00).

Have a basket of several stocks, then sell when you get at least a couple of points/10%+ out of the trade.

MORE TO COME ON THIS PAGE

...stay tuned

wins/losses. "Small Stops are King" in daytrading.

#### SHARE SIZES:

-For scalping, you tend to need to trade from 300-1K shares at a time to make good money. Of course, this also depends on the share price and volatility.

I've made good money trading 50- or 100-share lots of DCLK, for example, to get from 4 to 7 points on it. Typically, though, I'll daytrade in blocks of 300-500 shares for stocks priced at from \$12 - \$60.

**Note:** if you are not a decisive person who can get in and out of trades quickly, then try swing trading small shares for awhile (100-300 shares). Many new daytraders "blow out" their accounts by overtrading in Level 2 without knowing the market's rhythm and pace.

Swing trades force you to do research, understand the unpredictability of the market, and learn the fundamentals you need before trying to daytrade. Use "Investors' Business Daily" to help decide the relative value and strength of the stocks you want to swing trade, eg 80/80+ rated stocks.

## Module Four

## Swing Trading Strategies

◀ PREVIOUS NEXT ▶

Back to  
MODULE 4

- Avoiding low-percentage swing trades and bad investment risks

### • Main Points:

- Unlike daytrading, in which Time & Sales, momentum and Level 2 are important trade tools, **swingtrading is much more dependent on proper technical chart analysis**
- This lesson will share some tips for avoiding dangerous situations in your swing trades: I will show some **chart patterns to avoid** for entering swing trades. Like the lesson in an earlier module says, we are looking for high-percentage trades, **not poor trades and not "indeterminate"/uncertain trades.**
- You should use chart patterns heavily in daytrading as well, of course, but **in Swing Trading 90% of the reason I get into the trade is because of a chart pattern that looks good to me** (not a news event, the momentum in Time and Sales, anything to do with market makers, etc.). We'll look at swing trading chart patterns and technical analysis in a few lessons forward from here.
- Also important in swing trading is **analysts ratings**, eg buying highly-rated (eg profitable, good earnings) stocks that are getting stronger, or when they are oversold. Remember we don't care at all about analysts ratings in our daytrading activities, that's solely momentum-driven. I may swing trade a stock like WMT that doesn't have good analysts ratings, though, if the chart pattern is good.
- **A good rule of thumb I like to use is to avoid swing trading stocks with an analyst rating over 2.0 and give preference to stocks with analysts ratings of 1.6 or better.** Ratings of 1.6 to 2.0 are "just ok". That's not to say you can't make money swing trading all stocks, but I like to stack the odds in my favor, having highly-rated stocks is helpful.
- From a chart standpoint, you also want to **avoid swing trading stocks that have been in a steady downtrend** for more than 5-10 days in a row. **Bottom fishing is best done on sharp drops** that get buyers' attention, not on stocks whose price has slowly eroded over time. More on this in a later lesson on swing trading chart patterns. **Bottom fishing is also done on stocks that tend to trade in a "channel"** with established support and resistance levels (ex: SPLS HET ROST SSCC)
- **Buy Jack Schwager's "Getting Started in Technical Analysis"** (only \$15), super starting TA book.

## Positive Signals for Entering Swing Trades:

**Chart patterns:** breakouts from consolidations, trading a channel off support/resistance, bottom bounces. See below for examples.

**Delayed reaction to good news:** buy stocks that show a steady uptrend and follow-through of several days based on good news or earnings that were released.

**Volume Reversals:** if you see buying volume at what appears to be a reversal point for the stock, get in as soon as possible and ride it up for a few days (eg YUM ROST ANN Mar 17, 2000).

**Post-earnings gap downs:** if a stock gaps down on decent earnings, it may have buyers over the following days or weeks (eg XRX UIS CCL).

**Positive analysts ratings:** oversold stocks (eg bouncing off a 52-week low or other key support level) that are highly-rated (1.5 or better) can be profitable plays as well.

Make sure to plot the **20-50-100- and 200-day moving average lines** for all 90-day to 12-month long term charts you look at for swing trade stocks. Example: plot these lines for QCOM DCLK WMT CIEN at bigcharts.com or on your chart software.

Stocks frequently get buyers when the stock bounces off one of these key support lines, especially the 200-day moving average line.

These are what fund managers with capital frequently use to help assess stock entry and exit points. You should, too - they control the money flow. Be particularly keen on patterns where you see blocks in Time and Sales go off right above a 200MA bounce, for either a momentum daytrade or swing trade.

In addition to chart TA, be sure to know your stocks' ratings before buying it, I frequently buy stocks like HRL HET SPLS DCLK that have good ratings and avoid poorly rated stocks for swing trades. Get ratings at these two links: [ZDFinancial](http://ZDFinancial) and [Zacks/BigCharts](http://Zacks/BigCharts). Below are some examples.

## Good Analyst's Ratings:

Examples: AOL, DBCC, SPLS: I trade these actively

Number of brokers recommending as:	Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)
Strong Buy	25
Moderate Buy	15
Buy	3
Hold	0
Moderate Sell	0
Sell	0
Strong Sell	0

## What to AVOID in Entering Swing Trades:

If the stock has **lost a key support level** do not enter (or stay in a current trade), wait for buyers to come back through this support level before buying

If the stock pattern is **"indeterminate"** don't guess, wait for a high-percentage play to present itself. Don't be like the guy in the "My sources say no"-commercial

If **volume** is lighter than average for the stock, stay out of the trade. Note, however, that in choosing stocks for swing trading you **can expand your stock picks** to include lower-volume stocks (down to 200K average daily volume, as intraday liquidity isn't as important as it is for daytrading).

If the stock has **poor analysts ratings** you should be cautious about buying it for a swing trade unless strong buying momentum exists.

If the **chart pattern** doesn't show you a clear direction that you feel comfortable with, don't buy the stock. Again, "make it break through" a key resistance level before buying.

**Don't swing trade just 1-2 stocks at a time**, diversify much more than you do for daytrading. My swing trading account has anywhere from 4-10 stocks in at a given time, I wait for one of them to pop up to give me a good profit, at which point I sell it and reinvest in another play.

Don't buy **overextended stocks** that have run up a lot for swing trades unless you're very careful, eg CORL NOVL CEGE GENE all fell 30-40% in a matter of weeks off recent highs.

Also, it is generally not a good idea to hold through **earnings releases**, as stocks will frequently gap down.

## Poor Analyst's Ratings:

Examples: ETYS, BA: I usually don't trade these

Analyst Ratings BOEING CO	
Next Earnings (Approx.): 1/20/00	
Number of brokers recommending as:	Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)
Strong Buy	1
Moderate Buy	9
Hold	13
Moderate Sell	0
Strong Sell	0

Number of brokers recommending as:	Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)
Strong Buy	2
Moderate Buy	0
Hold	0
Moderate Sell	0
Strong Sell	0

Number of brokers recommending as:	Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)
Strong Buy	1.00
Moderate Buy	1.00
Hold	0
Moderate Sell	0
Strong Sell	0

Number of brokers recommending as:	Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)
Strong Buy	9
Moderate Buy	7
Hold	5
Moderate Sell	0
Strong Sell	0

Number of brokers recommending as:	Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)
Strong Buy	1.79
Moderate Buy	1.73
Hold	-0.06
Moderate Sell	
Strong Sell	

Analyst Ratings ETO'S INC	
Next Earnings (Approx.) 4/28/00	
Number of brokers recommending as:	Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)
Strong Buy	1
Moderate Buy	6
Hold	7
Moderate Sell	0
Strong Sell	0

Number of brokers recommending as:	Average Recommendation (strong buy) 1.00 - 5.00 (strong sell)
Strong Buy	2.36
Moderate Buy	2.38
Hold	0.02
Moderate Sell	
Strong Sell	

Why care about ratings if you're not a long term investor? I like to look at the money flow on the street, it tends to flow into highly-rated stocks that people are comfortable with.

Your odds are better of getting buying behavior for highly-rated stocks during the time you're in a swing trade than for poorly rated stocks, in my experience. Money tends to rotate into well-liked stocks, as a swing trader you want to capitalize on this price momentum. Of course, analysts ratings are frequently uncorrelated with price movement, so **you need to use chart technical analysis as your primary indicator**, ratings as a secondary. Get [bigeasyinvestor.com](http://bigeasyinvestor.com) (free) for good swing trade research and screening.

### Examples:

#### Good (High-Percentage) Chart Patterns:

#### Poor Chart Patterns:

We will have detailed looks at these and other charts in later lessons, for now I just want you to **familiarize yourself with some of the types of swing trading patterns to be on the lookout for**. Left column = good chart patterns to trade, the right column = don't trade these. These are all **10-day** charts.



**Steady uptrend on volume:** ok to buy on pullbacks



**Spike buying pattern,** don't buy after it's ran up, "if you missed it you were too late", don't chase. Common chatroom pump n dump pattern to avoid.



**Bottom bounce off oversold condition** for no good reason, buy after the bottom levels out for awhile in consolidation pattern.



**Indeterminate pattern:** ATHM is not telling us much here...you might want to try and play the channel, buying at 27 support, but it's a relatively "low-percentage" pattern.



**Buying off key support levels:** I had sold at the top (to the left, at 9 5/8), I bought again at what I think is a bottom at 8 1/4 (on the right, 8 days later), see volume at the far left and far right, these are support/resistance levels for DBCC (check with a 6-month chart). Below is a sample trade confirmation from March 8th.

**Making \$1156 on 3 day swing trades -> Close P&L \$ 1156.25**

Orders Exec Trades Opens Alerts Stats None

Stock	Bought	Shar...	Sold	+/-	P&L
DBCC	8 11/128	700	9 5/8	+97/128	531.25
DBCC	8 3/8	300	9 5/8	+1 1/4	375.00
HET	19 11/16	200	20 11/16	+1	200.00
MRK	54 3/4	100	55 1/4	+1/2	50.00



**Buying at a consolidation point:** this is risky bottom, fishing, we've had a selloff in GENE from 75 down to 30, at which point you see a lot of shares changing hands for several days with no price movement. I'd buy at 30 here and put in a stop right under the consolidation level (say at 29 1/2 or so). The heavy volume at 30 is what makes this one "ok to play", using a closer-than-normal stop.



**Buying a cup-and-handle breakout:** these are usually a safe breakthrough play, in this case I was in at the bottom (18 5/8) since I play SPLS for a living, sold at the 23 top; a good trade entry would be on the breakout above 20 resistance and sell at 23. Since everyone knows them, though, expect selling shortly after the breakout.

Volume and price action is not telling me anything, and besides the retracements are pretty sharp, I'd probably get shaken out. I don't play until it breaks through 30.



**Cup and handle:** well, if you weren't in from the bottom on this CL run, it's too late to enter now. I'd put it on the watchlist and buy only if it breaks through 55 on decent volume in the morning or late afternoon, for example. I wouldn't initiate a new position yet.



HLTH not too healthy here: Now, it's still in a **steady downtrend**, so a swing play might be risky on the way down. The heavy recent volume is a bullish indicator, though, so it's on my watchlist, make it break through a previous resistance level (eg 40) before buying. Dont catch a falling knife, you might get a bounce on the way down but it could have a ways further. Eg I recently got faked out by CCL, thought 32 was a bottom, actually it's 22. Missed it.



In a **tight range:** These are great for daytrading plays, but not for swing trades, your risk/reward ratio isn't good enough to buy when the stock is chopping around like ORCL is here. Buy only if you see a heavy volume breakout above the current resistance level at about 85.

*Watch for additional Module 4 lessons on chart patterns and technical analysis.*

- Choosing the Best Stocks for Swing Trading

● **Main Points:**

- Review our brief guidelines for "how to choose the best stocks for daytrading" first at [this link from Module 1](#).
- This lesson will help you look figure out what types of stocks make good candidates for swing trading. Again, swing trading is defined as trading smaller shares (100-300 is the number I use most often, may go as high as 1000, but not often), over an expected trading timeframe of from 2 days to several weeks.
- **For swing trades, I tend to "bottom fish" more than I do buy breakouts**, although breakouts are fine as well, especially candidates for overnight gaps up on good news or other buying momentum.
- We look for chart patterns, and to a lesser extent, pre-earnings release momentum, analysts ratings and news, to help decide whether or not to enter a position. Charts rule in TA.
- **It takes practice to learn swing trading TA, expect to spend at least 6 months or so before the patterns start to become 'second nature' to you, and for you to be able to trade profitably consistently.**
- Trading is not easy money. Anyone who tells you otherwise is trying to sell you something. Stock picking sites are a bit more valuable for swing trading than for daytrading, but I'd still advise you to do your own research and learning.

- **There are 3 general types of swing trades to enter:**

1. Buying towards the **lower 1/3 of a 'trading channel'**
  2. Buying a **"bottom bounce"** for oversold stocks
  3. Buying a **breakout above a key resistance** level.
- Learning to trade these three profitably is how to make good daily money on swing trades. Note I made close to a thousand dollars on 100-300 share trades held less than a few days each on Fri. Apr 7 (IMGX/CHR overnight holds):

Making \$882 on longs Fri 4/7/2000: \$ 882.81

Stock	Bought	Shar...	Sold	+/-	P&L
CHTR	14 1/2	100	15 1/2	+1	100.00
IMGX	12 33/64	300	14 1/2	+1 63/64	595.31
WOMN	5	200	5 15/16	+ 15/16	187.50

Swing trades should be held with the expectation of making at least 10% profit within a 2-20 day trading cycle.

## Choosing the Right Stocks to Swing Trade:

*This section will help you learn how to screen for the best types of stocks to swing trade: what price level? what to look for on a chart? when to buy vs sell vs wait?*

### FUNNEL SCAN: 1-YR, 10-day, Intraday Charts

We first introduced you to this concept back in Module 1 - do you remember how it works?

Your stock scanning must start with the big picture of the stock's ratings, price movement, trading range and overall 1-yr trend. This is the widest part of the funnel. Then we drill down and look more closely at the specific support/resistance areas for the most recent 10 days of trading, along with volume patterns before buying.

In daytrading, we look at market (\$compq/string), 10-day, then sector (\$gin, \$sox), then intraday charts, followed by T&S, finally using level 2 to time our entries and exits.

In swing trading, we start by looking at the analysts' recommendations (must be <1.8), volume patterns, 1-year chart and it's 200MA, 100MA, 50MA, trend and support/resistance lines. As long as I buy the stock somewhere in the lowest 1/3 of the day's trading range I'm happy. Or, if I buy a strong stock that's breaking out above a key resistance level that's great too.

Swing trading is much more approximate than daytrading is. My swing trading stops are often determined by the prior 2-3 month support level.

If I'm swingtrading, I may well let a \$24 stock go all the way down to \$19 3/4 before a stop is taken...it depends on how many shares you're trading and for what time horizon. Of course if I were daytrading this same \$24 stock my stops would be no more than 3/8 of a point, more likely just 2-3 spreads.

The point? Swing trading has a wider 'margin of error', and requires more patience. Worst case, you may have to wait almost an entire quarter (3 months, 60 trading days!) before a healthy profit is available (eg ORCL last summer, CCL now). I generally prefer to hold only 2-10 days max however, as I do not want to tie up capital waiting for a stock to come back'.

**Your scan should accomplish one main objective:** to narrow your list of trading stocks to a small handful with the highest potential for price improvement in the near term. It's like planting seeds, you buy 100-300 shares of a handful of stocks and take the profit from each one as it 'sprouts' and the price has gone up over 10%.

## Examples:

Let's look at IMGX. (by the way, I don't even know what the name of the company is or what they do, or who their competitors are, and I never will. I buy and sell based on chart patterns. I know earnings release/ratings for the stock, that's it.)

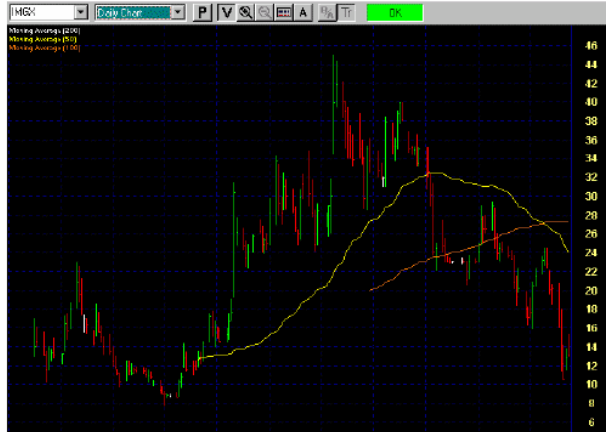
All I know is, they IPO'd about 6 months ago, have strong analysts ratings (1.7) and recently dropped back to retest the low of the trading range, so I'm a bit interested:

### IMGX 6-month chart: 6 month trading range 8 1/2 - 46

Usually, you want to look at the 1-year chart and plot the 50MA 100MA and 200MA lines on it. See the DCLK example below for more on why. This stock IPO'd 6 months ago, so that's all the data we have to work with.

You can anticipate that buyers will look to get in if the stock retests its previous major low, which was around 10. Sure enough, that's exactly where this stock bounced. So, you want to enter early and ride it up. I would expect IMGX to trade up into the high teens over the next several months. I could be wrong, but I'm probably right.

Now let's look at the 10-day chart, to look at what the other traders have been doing with this stock lately. Avoid stocks that have had no buying interest at all, of course.



### IMGX 10-day chart: The MOST IMPORTANT ONE in Swing Trading. Support at 10, resistance at 25, volume reversal 10-12:

After checking the 1-year chart to determine major support/resistance and trend line, we focus in on the 10-day chart to look for volume patterns and bounces.

Here I've annotated this chart for you...IMGX was a short when it lost 20 support, a cover/buy long off 10-12 support. We bought at 12 1/2 and sold 2 days later at 14 1/2 for a healthy 16% profit. Our stop was at 9 7/8; we would've sold it had it dropped this low and waited for it to regain 10 1/4 before buying it back.

All these swing trades are watched realtime, with alerts, to help us squeeze the most profit possible out of each trade.

Let's look at the final chart in our arsenal, the intraday chart. I didn't use level 2 or time and sales to manage this winning swing trade; that level of precision isn't needed when your trading range spans several days or more. You want to roughly enter and exit with a 8-10% profit, not scalp fractions.



**IMGX 1-day/Intraday chart:** Ok, now I sold at 14 1/2 (the 2nd top), which was correct, on this gap up. Remember to SELL GAPS UP on the OPEN and BUY GAPS DOWN on the open. I'll be watching IMGX to play it again on Monday April 10.



This stock closed the day prior at around 13. It gapped all the way up to 13 7/8 on the open and continued clear up to 15 before being sold off. Instead of taking the first profit (which would've been fine), we waited to see if it would make a higher high.

It didn't, so we sold shortly after the next top, at 14 1/2. This was the right decision, as the stock retraced back down to 13 at the end of the day.

The play on the day following this pattern? If it drops down to 12-13 and starts to sell then wait for it to get back above 13, if it gaps up to 14-14 1/2 I'd still wait for it to push above 15 1/4 before buying back, if it's up on volume and moving before 10am.

The swing trade's goal is to buy relatively low on one day and sell higher on another day. That's it.



## ILLUSTRATED TIPS FOR SWING TRADES: CHOOSING THE RIGHT STOCKS

### Drawdown for Swings

- Decide where you will take a stop loss at, based on a prior support level, before entering a swing trade. Play one step ahead of the game, knowing that the mm's/specialists will try to take out stops at the "obvious" areas...choose something slightly different.
- In selecting stocks to swing trade, make sure you're not buying overbought expensive stocks that have had a huge runup in the last couple of months. Focus on buying towards the bottom of a trading range, as a stock is "starting to come back". Or, buy early in a breakout on good news/earnings. Just don't be the "bagholder" who paid more than everyone else did.

### Bottom Fishing - How Deep?

- There's a difference between correctly 'nailing the bottom' and 'catching a falling knife'.
- Frequently, the first round of buying isn't strong enough to sustain the stock, and it will continue to sell off. A good example is CCL, I bought at 33, it lost 30 and continued all the way down to 22! Or WMT, I bought at 53, it went on down to 43! Before bouncing.
- So, make sure to set stops if the market proves you wrong and they continue selling it off. Usually, it's a good idea to buy a bounce off a bottom, using the previous bottom as a stop loss point.

### Overreactions?

Overreactions to news/earnings can provide profitable swing trade opportunities too.

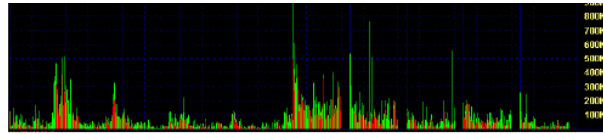
Here's a recent 10-day chart of LGTO. LGTO's stock got cut in half - 56%! Apr 3 after revealing it would have to restate 1999 earnings due to misreporting by its sales staff.

As you can see, the first drop, to 22, wasn't the real bottom, that happened one day later, when it dropped to 16. I think 56% is a bit much to drop the stock, and that a retracement of 15-20% is highly likely over the next 2 months. Sure enough, it's climbing back up out of the pit.

It will have a tough time over the next few weeks but a drop this sharp (like PGs), seems a bit much. I could be wrong,



this sharp (like PGs), seems a bit much. I could be wrong, it could go lower, but this looks like a bottom consolidation area to me. If I were to take another long position down here, which I might, on an up day, the stop would be set at 19 3/4.



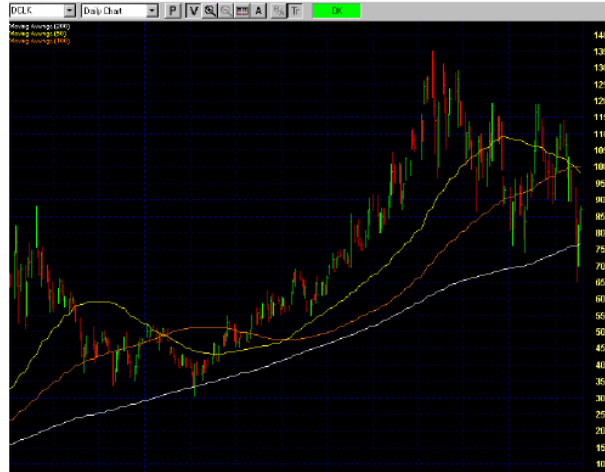
## Major Trend

Is "the trend your friend"? Well, maybe, if you buy strong stocks on pullbacks. Overall, though, trends have seemed to whipsaw strongly during the first part of 2000 and volatility seems to be the name of the game. So, Buy Reversals and Pivot points is more profitable.

Let's look at this 1-year chart of DCLK. We have plotted the 200-day MA (white), the 100MA (orange) and the 50-day MA (yellow). Why care about these numbers? Weeellll, an interesting thing here, you see, DCLK has never lost it's 200 MA, and unlike QCOM/JDSU it's not trading at a multiple of its 200MA either.

**The 200MA is a key support line for all stocks.** Why? Fund managers and other institutional traders watch the 200MA for support/resistance. This tells us DCLK is almost certainly a BUY at 75-80, it's 200MA, with a stop loss at 70ish.

The 100MA-200MA spread is often a trading range, so you can look to exit the position before it touches the 100MA (or possible 50MA) line.



## Volatility

Volatility is wonderful - it's how I make my living. The key is to be on the right side of the volatility.

Here's a nice 10-day chart swing to trade: YUM. That's Taco Bell/Pizza Hit/KFC... nice to eat there too. I like to snack at the YUM chart often; you can see that it's usually a buy right above 30 and usually a sell at 31 1/2- 32 recently.

For fast-food stocks, I like to trade YUM PZZA JBX OSSI.

Capitalizing on volatility in stocks like this is a goldmine, look how much it swings over a 10-day period. You can see every time it touches 32 people look to sell it. All of the food stocks are oversold down here (April 2000) and I would be a long-term buyer of all of them. Same thing with many retailers, such as ROST WMT TGT ANN etc.



- Risk Management for Swing Trades Part 1: Managing Time in the Trade vs Optimum Share Sizes

● **Main Points:**

- In managing your risk for short-term swing trading, (several days to weeks), it is advisable to look at three main variables you will manage for the trade:
  1. **Number of shares** you will trade
  2. The **length of time** you expect to hold the stock
  3. The **support/resistance areas** you will use to determine stops and exit prices
- This lesson will focus on the first two of the three areas, we'll cover support/resistance in the TA lessons later in the module.
- In general, I find it useful to swing trade no more than 300 shares of any one stock, with a rare exception of cheap (under \$15) equities. Why? You want to limit your risk. Also, I often swing trade as little as 50 shares of expensive 'net or semi stocks, between \$60-\$120/share, for 5- to 8-point profits over a several-day to week time horizon.
- You should also have what I call a **"time stop"** on the trade as well - if you're tying up capital in a stock that's slightly down or choppy for longer than 2-3 weeks then consider taking the small loss and buying a different stock...you're losing the profit potential you could gain by rotating the capital into a better performing stock. If you're wrong, get out and try again with a different stock.
- From a risk management standpoint, you want to **limit your exposure in both share size and time wasted** waiting for the stock to go up.
- **A tradeoff can be made between the number of shares traded and the length of time in the trade:** it's generally better to add in smaller increments to your winners than it is to average down on losers. Example: You buy 200 shares of DELL at 44 one day, you see 2 days later it's up to 46, you might add another 100 shares, and sell all 300 4 days later at 48. Add in small increments to your winning swing trades, do not add in larger increments (eg doubling the position).
- Also, if you must average down, do so with a larger position on the bottom, using stops, to weight your position more heavily at the lowest price possible. In general, we avoid averaging down, or "throwing good money after bad", the only time you should average down is when the stock is rebounding on volume off a true support level, then you should add a larger position off this confirmed bottom (using a stop at the previous support level). Again, this is technically an independent trade, which is (hopefully) a better one than your original position, which was taken too high.

Managing Risk in Swing Trades:  
Time vs. Number of Shares

Number of Shares to Swing Trade "How many shares should I buy?"

Remember, your risk:reward ratio is higher for swing trades, so you should buy less shares than you would for a daytrade.

Overnight holds may get a gap down on bad news. The reverse can happen too, of course, you can profit from a gap up on good news. But, we want to be overly cautious when we trade. The key is to limit your risk in as many ways possible, one way is to trade less shares, from 50-300 shares.

As you'll see in the next lesson, one way to maximize your leverage is to swing trade a number of stocks at the same time. I do this, I will be long in from 3 to 16 positions simultaneously, and sell whenever one 'pops up' past my profit target.

It takes a bit longer than a daytrade of course, since I'm trading fewer shares each time. Typically I'll buy a handful of good quality stocks in 100-200 share increments that are

Swing trade examples:



200 shares of a \$22 stock that goes up 1 1/2 points in 1 week = \$350 profit

400 shares of a \$11 stock that goes up 7/8 points in 2 weeks = \$348 profit

100 shares of a \$41 stock that goes up 2 5/8 points in 4 days = \$262 profit

50 shares of a \$68 stock that goes up 6 1/4 points in 3 weeks = \$425 profit

If you're sitting in a half-dozen or so positions and take these types of profits 1-3 times every day you can also make great money trading the market.

bouncing off a bottom, or breaking out above a previous trading range.

Like the fish, you are slowly swimming along, scooping up daily profits, which add up nicely over the course of a month.

*Managing risk with smaller share sizes: as always, you still need to identify stops ahead of time and stick to them. You can always buy the stock back later if it goes up through your stop area. Your stops will be wider (3-5%) than they are for daytrading, where we use 1-2% max stops.*

## Timing your Swing Trades "How long should I expect to hold the stock for?"

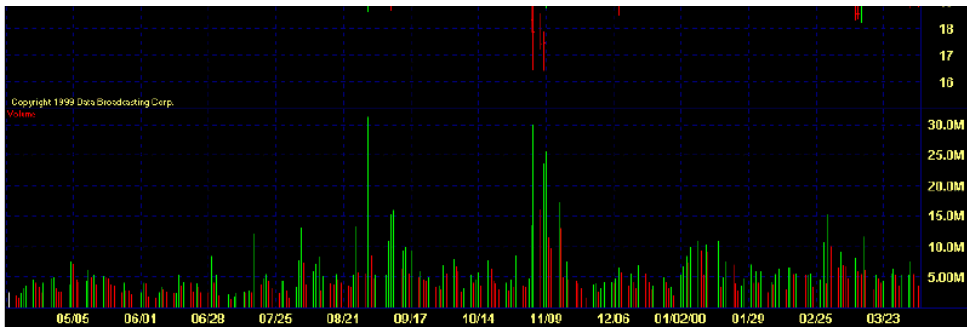
This is where technical analysis and your trading plan come into play.

- Limit the time you are in a swing trade to no more than 2-3 weeks, in general.
- Why? You don't want to tie up your valuable trading capital in a non-performing "wrong" trade. You're not a long-term investor.
- You should feel very comfortable taking a 10% plus profit anytime it presents itself. You may, for example, buy a stock one day and see it gap up 14% on the open the very next day. Even though you bought the stock thinking "I may need to hold it a few days or weeks to get a good profit out of it", be opportunistic - if you see the green, then Sell it and bank the profits.
- Let the buyers' and sellers' behavior in the stock's chart pattern tell you how long you should expect to be in the trade. Look at a 5-day and 10-day chart as well as the longer term 6 month/1-year charts.
- How much volatility is in the stock? You want to swing trade stocks that are in a steady uptrend, have bottomed and are bouncing, or are in a predictable trading range.
- Look at the chart to define your expectations of how long you want to be in the trade before selling your position.

**Example:** Let's look at the SPLS (Staples) chart below. It's a one-year chart.

- What's the overall trend? down
- What's the major support/resistance areas for the last several months? Support at 19 and resistance at 23.
- Where do you swing trade it? Buy at 19-20 1/8 and sell at 22-23.
- How long do you expect to be in the trade? Based on the chart volatility, no longer than 2 weeks.





## Timing Tips for Swing Traders:

- **DRAW THE CHART AHEAD OF TIME:** No I don't mean one of those hokey future-chart prediction websites, rather, print out the 3-month chart of your stock and draw out the support/resistance lines and the 'deadline' you will give the trade to be profitable, or to be stopped out at, in.
- Example: If you enter the trade April 16th, maybe give it til the end of the month (or meeting your profit target or stop loss). If it's still chopping around and you're +/- 1/2 point with no major movement after a couple weeks, consider closing the trade and rolling the money into a different stock pick.
- **THE MORE SHARES YOU TRADE, THE SHORTER YOUR TIME HORIZON SHOULD BE:** if you're only trading 50-100 shares of a stock and it's taking up less than 10% of your trading capital, then maybe you can sit in the trade for a month, or even two, to wait for a decent profit.
- If you're trading 200-300, or more, shares, expect to get out within 2 weeks maximum. Other opportunities are out there for this amount of trading capital you've allocated to the trade, if it's not performing, then "fire it" and buy a different stock instead.
- **DISCIPLINE IS STILL IMPORTANT IN SWING TRADING:** Don't fall into the common trap of letting "bad daytrades turn into investments/swing trades."
- Your only protection against sloppy trading is to **WRITE DOWN AND STICK TO** your stops, entry and exit points. This can be simple and brief, on a blank piece of paper. The main thing is to use it to help you trade with defined boundaries, so you don't lose money.

### Module Four

## Swing Trading Strategies

◀ PREVIOUS    NEXT ▶

- Risk Management for Swing Trades Part 1: Using Stops, Portfolio Management & Diversification

Back to  
MODULE 4

### • Main Points:

- This is another "big picture basics" lesson that is designed to help you get started in swing trading successfully.
- Risk management in this lesson will help you figure out **how to best allocate your capital, use swing trading stops and diversify the stocks you are trading.**
- **In swing trading, we recommend that you have a handful of stocks that you trade simultaneously.** I have held anywhere from 2 to 6 different stocks, almost all small shares (50-300 shares each), for a 3-day to 2-week or so hold.
- What types of stocks to have? I'd suggest picking 1-2 from each of several different sectors (eg retailers, nets, semi's)
- **Why do we recommend this swing trading approach?**  
Simple: if you only have 1-2 stocks you're playing you will probably get impatient waiting for it to go up faster, and exit the position too soon, with a small profit.
- If you have a handful ("basket") of stocks you're in then you can sell one when it "pops up" to give you a decent profit (of 5-20%) and use the capital to buy another stock, rotating your money over ever couple of weeks into new stocks while your capital base grows.

## Managing Risk in Swing Trades: Using Stops, Portfolio Management & Diversification

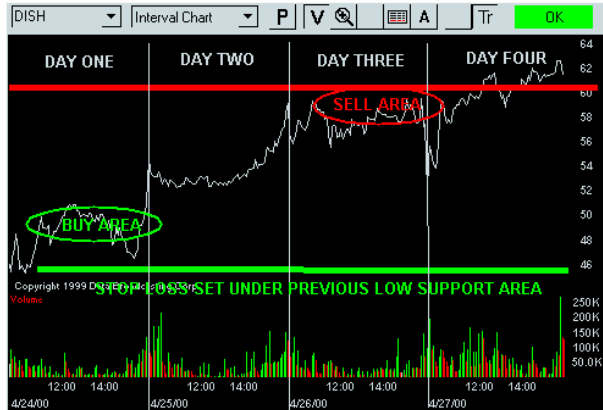
### Using Stops in Swing Trades

On Day One of this DISH trade you can see some initial buying in the first half of the trading day. **Where would you set your stop loss here?** No more than 5% away from the trade entry, or 45 1/2, right under the day's low.

How do you determine a trade exit area? Again, I always like to exit right under whole number support, especially "decade" numbers like 60 in this example. Now, DISH kept running up, and

That's fine, half the time stocks will go right back down again as well...better to book the profit and the re-buy the stock again if it pushes it's way through 60, say you might buy again at 61-62.

In hindsight it's always easy to see how a trade "should've" been managed; let's figure out how to make these decisions Before you get into a trade. Here's an activity to help you with this:



### SWING TRADE STOP ACTIVITY:

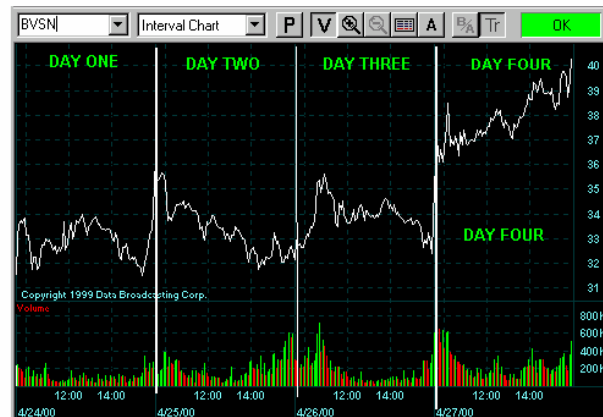
Take a look at the three chart examples shown here. Let's do an introductory Technical Analysis simulation activity to learn this critical skill.

For each 4-day chart, I want you begin by to cover up the "left 3 days" with a piece of paper. Now, move the paper slowly to the right, to simulate each trading day.

Let's say you entered the trade anywhere on Day 1. Now, where is your stop loss at (remember it must be less than 5% of the stock price). Now, how would you figure an exit strategy? Where would you book a profit, or use a trailing stop at? How would you manage your stops for each example?

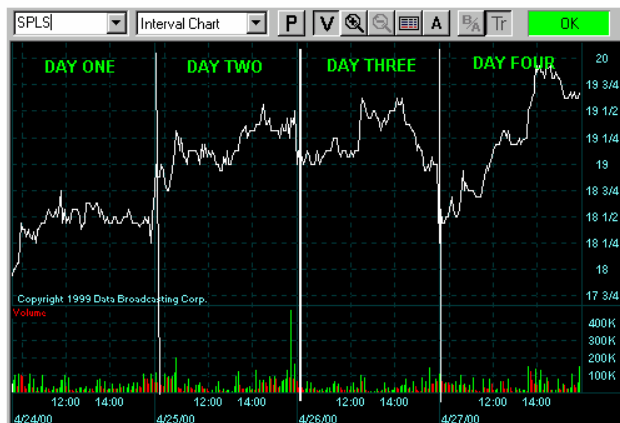
#### BVSN:

- Support is Where?
- Resistance is Where?
- Trade Entry Would Be Where?
- Trade Stop Loss is Set Where?
- Trade Exit Would be Where?



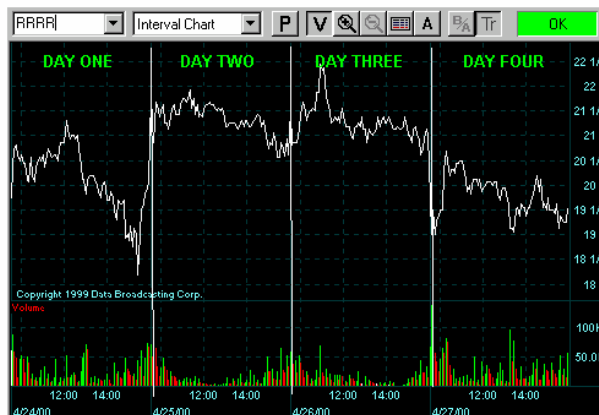
#### SPLS:

- Support is Where?
- Resistance is Where?
- Trade Entry Would Be Where?
- Trade Stop Loss is Set Where?
- Trade Exit Would be Where?



RRRR:

- Support is Where?
- Resistance is Where?
- Trade Entry Would Be Where?
- Trade Stop Loss is Set Where?
- Trade Exit Would be Where?



## Managing Your Portfolio: The DTU ROTATION METHOD

When swing trading (which I've been doing a lot more of lately), it's a good idea to keep a "rotation crop" of stocks that you're swing trading. Here's how it works:

Be sure your support/resistance levels decided on by the same time horizon you have for the trade, eg if you're planning on holding less than a month then look at 1-2 months worth of data, if you're planning on holding less than 10 days then look at 10 day support/resistance.

**1. Buy 100 shares of each of 4-6 stocks.**

**Example:**

100 RIMM @ 37

100 DCLK @ 62

100 BVSN @ 33

100 NOVL @ 19

**2. Write down major support levels (no more than 5% lower than what you paid for the stock) for each stock.**

**These are your stop loss areas (you will sell if the stock drops to these prices).**

**Example:**

RIMM Stop Loss = 34 7/8

DCLK Stop Loss = 59 3/4

BVSN Stop Loss = 29 7/8

NOVL Stop Loss = 17 7/8

**3. Write down major resistance areas and profit targets for each stock in the portfolio:**

**Example:**

RIMM resistance = 46, exit target = 44-46

DCLK resistance = 70, exit target = 68-70

BVSN resistance = 40, exit target = 38-39

NOVL resistance = 22, exit target = 21 7/8

**4. Okay, now you have a swing trading plan defined. This is critical.**

**Another tip to remember is to use trailing stops in your swing trades as well as day trades (see Module 1 for more on this)... eg if you buy at 33 and it goes up to 34 1/2, your trailing stop is at 34, which means you will sell at 34 to lock in a 1-point profit if the stock goes down to 34.**

Finally, you wait and watch. Let's say DCLK goes to 68 1/2 and you see another oversold stock starting to rebound. Well, you can sell your DCLK here since it's near a resistance level, book the profit, then go buy the other stock, "rotating your capital" into a higher-percentage trade.

Let's say that NOVL drops to 17 7/8, so you sell it, taking a minor loss. Your 12% gain on DCLK outweighs the 4% loss on NOVL, so you're still at a profitable 3:1 reward:risk ratio.

You simply keep doing this process, rotating your capital into new stocks for 2-day to 2-week swing trades, selling when the stock has hit a new high near a resistance level, and buying stock that's either bouncing or breaking out above a key resistance level. It works - try it.

## Diversifying Your Stocks by Sector

Finally, let's look at managing risk by diversifying your portfolio by sector. You shouldn't, for example, just swing trade all computer stocks, or internet stocks, or brokers.

Try spreading your picks among several different sectors so that you maximize the odds that at least one of them will do well on a given day. This is a "swing trading hedge"

For example, the stocks in the above example are all from different sectors. You might include 1 semiconductor (eg VTSS XLNX AMAT INTC), 1 telecom (T WCOM), 1 wireless (QCOM AWE), 1 retailer (WMT ROST) and one pharmaceutical (AMGN BGEN), for example.

All sectors don't move together, some days one sector will take the lead and others may be weak. In swing trading a portfolio, make sure it's diversified into different, strong sectors.

- Swing Trading Technical Analysis & Charting Part 1: 20/50/100/200 MAs, using MACD

● **Main Points:**

- Moving average lines play an important role in helping you to determine where other traders will see support and resistance levels.
- Large financial trading firms buy and sell large quantities of stocks based on equations that include MA lines, so you should be on the lookout for 'bounces' and breakthroughs based on these important lines
- The most important lines to plot are the 20 50 100 and 200 MAs.
- The MACD is a pair of lines that you can use to help determine likely entry and exit points as well, when the lines cross each other it signals a trend reversal is likely.
- MA Lines are very useful in helping us determine how to play the 3 major chart patterns:
  1. Buying breakouts above resistance
  2. Bottom bounces off support
  3. Playing the support/resistance in a range

The chart patterns below are great examples of each of these three patterns in motion, captured May 2000. Notice in each of the three TA lesson examples below we have a pair of charts: the 6-month "big picture" chart and the 10-day "swing trading" chart.

**BREAKTHROUGH SWINGTRADING PLAY ABOVE RESISTANCE USING MA LINES**

**PLOTTING 20 50 100 200 MA LINES: 6-MONTH CSCO CHART**

Notice in this 6-month chart that CSCO has:

- 1) always stayed above its 200MA (white) line,
- 2) has almost always stayed above its 100MA (orange) line.

What does this tell you? Overall, it's a strong stock, and that any weakness should be seen as a buy opportunity. It looks like 50-80 is the "wide range" for this stock, and that the 100MA at 63 should be considered a key support level. Use the MA lines to "map out" support and resistance for trading here.

We need more detailed information to trade it, though, so we look below at the 10-day chart:



10-day CSCO chart: What do we see here?



Sure enough, CSCO bounced off low 60's, once on 4/24 and again on 5/3.

This tells us that if we were to enter a swing trade here we should place our stop loss at right under decade resistance, or about 59 3/4 or so.

Our exit target should be right under the next MA line, the 100 MA, at about 70. So, the swing trade is:

**A breakout play** would be to buy once CSCO has crossed 70 1/2 or so, with a stop right under 70. **Bottom bounce play:** Enter/buy low 60's, stop loss right under 60, exit target 68-69.

**Using MACD:** notice where the lines cross at the bottom? First time/buy signal is towards the end of the day on 4/24, sell signals at the top on 4/26 and 5/1, buy signal on 5/3.

#### PLOTTING 20 MA AND MACD LINES: 10-DAY CSCO CHART



#### BOTTOM BOUNCE SWINGTRADING PLAY OFF SUPPORT USING MA LINES

**MA Lines: CMGI has "lost 200 MA support at 80,** so major fund managers probably won't be buying til it's over 81.

Notice that unlike CSCO from above, the MA lines (especially the red 20MA) have crossed over, a bearish downtrend reversal pattern.

In general, avoid these types of stocks for position trades, the swing trades you enter must use a previous (eg recent or 52-week) low as a stop loss level.

One bullish signal, we have CONSOLIDATION (choppiness) around the 50-70 level on the chart, this can precede a trend reversal.

**Pop Quiz:** Where should your maximum stop loss be for CMGI based on this chart? Answer below.

#### PLOTTING 20 50 100 200 MA LINES: 6-MONTH CMGI CHART



## RANGE TRADING SWINGTRADING PLAY USING MA LINES

### PLOTTING 20 50 100 200 MA LINES: 6-MONTH SPLS CHART

Finally, we have SPLS, a classic "rolling stock". You can see the recent trend is down, and that 22 is hard resistance, at the 200MA.

The other MA lines are not useful for us in trading this stock based on the chart to the right. What else do you notice "big picture"?

When SPLS dropped to 17 in Nov 99 there was a huge upside reversal. This is an important example of the kind of "big picture" chart patterns you should be aware of.



### PLOTTING 20 MA AND MACD LINES: 10-DAY SPLS CHART

The MACD told us we had a buy opportunity on 4/27 and 4/28, when the lines crossed to the upside.

Notice the heavy selling volume on 5/3.

Based on our 6-month chart, I would enter a long position at 17 1/4 and expect a bounce back to at least 18 1/4 within a few days.

Knowing a stock's trading range and playing the channel is a fairly good way to swing trade. Make sure you're not channel playing a stock that's run up hugely in the last several months, those are "bubbles" that may burst, like the biotech did in Jan-Feb 2000.

Your stop on this swing trade would be right under support at 16 3/4 or so.



These sets of chart patterns should help you identify similar high-percentage trading opportunities as they occur.

In swing trading, you must always look at both the "big picture" 6-month (or longer) chart as well as a closer 10-day chart.

Stops must be adhered to right under support levels, to insure against large downturns.

Plot similar graphs using [bigcharts.com](http://bigcharts.com) or your quote provider, and see where you should set alerts and make trading decisions.

● **Main Points:**

- Unlike daytrading, swing trading requires you to look at the "big picture" of multiday trading ranges to help determine good entry and exit prices.
- It's frequently helpful to look at stock charts in 6-month, 10-day and intraday timeframes to help determine where a good entry and exit is.
- My favorite strategies in swing trading involve buying towards the lower end of a trading range or buying breakouts above a previous resistance level.
- This lesson will show you a number of illustrated charts for oversold, overbought, trending and channel plays.
- 10-day charts are also particularly helpful in avoiding low-percentage trades, eg buying in the middle of a 10-day trading range is not a good idea for swing trades.
- Once you learn to recognize high-percentage chart patterns, you will be more likely to be successful in trading with the market sentiment. This lesson will show you what to look for in several key chart patterns.
- Swing trading is almost all based on chart pattern recognition, adding things like recent price movement and MA lines, volume and financials as additional reasons to enter/exit your trades.

**OVERSOLD SWINGTRADING CHART PATTERN USING 10-Day & 6-month Charts**

10-Day PSUN Chart:

**Notice in this 10-day chart that PSUN has:**

1) sold off to a low of 11 1/2-12, at which point you see huge buying volume.

2) started to rebound from the 12-13 area from a previous 10-day high of 23

What does this tell you? The first thing to do is to check why the stock dropped (same-store sales weaker than expected)...then, decide whether you think the drop in price was overdone or not.

The trade would have been to buy at 12, using a stop loss right under 12, eg at 11 1/2 or so for the swing trade. 10 would be the absolute maximum stop loss for this trade.



We should also look at the 6-month chart for PSUN as well

6-Month PSUN Chart:

to see where it came from.

Overall, the stock showed nice volatility and buying volume during the last six months.

Additionally, you can see that the drop to 12 had a Huge volume spike, which indicates a short-term bottom is probable.

Where is your exit target, then?

Well, I'd look to exit once right before 15, say at 14 3/4...sit out the run over 15, re-enter at 15 1/2 and sell right under 20, say at 19 1/2, and then perhaps buy again in the low 20s, say 20 1/2, selling out right under 25 again.

I sit out resistance areas, and re-buy once (and if) the stock breaks through resistance. I buy off support and sell into buyers on the way up.



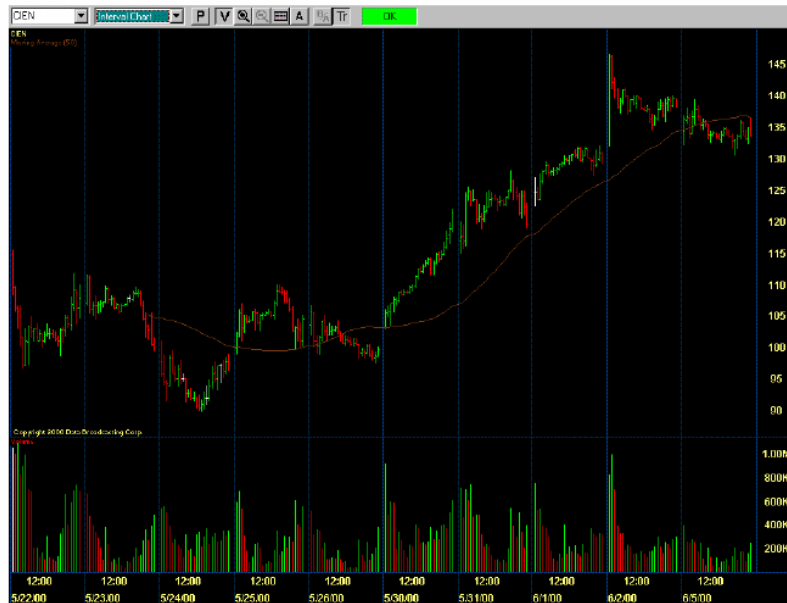
### OVERBOUGHT SWINGTRADING CHART PATTERN USING 10-Day & 6-month Charts

10-Day CIEN Chart:

Overbought patterns are important to recognize for three trading opportunities:

- 1) to close out a long position you're in with a profit, before the stock turns back down
- 2) to avoid entering new long positions, since they are dangerous at overbought areas, you shouldn't chase the stock
- 3) to enter a new short position, with a cover stop right above the resistance area.

**What does this 10-day CIEN chart say to you?** Hopefully, you see that the market sold off the gap up to 145, and that it's consolidating in the mid 130s range. I would go long if it broke over 145 on volume, or, short it if it loses 130, with a cover stop at 131 or so.



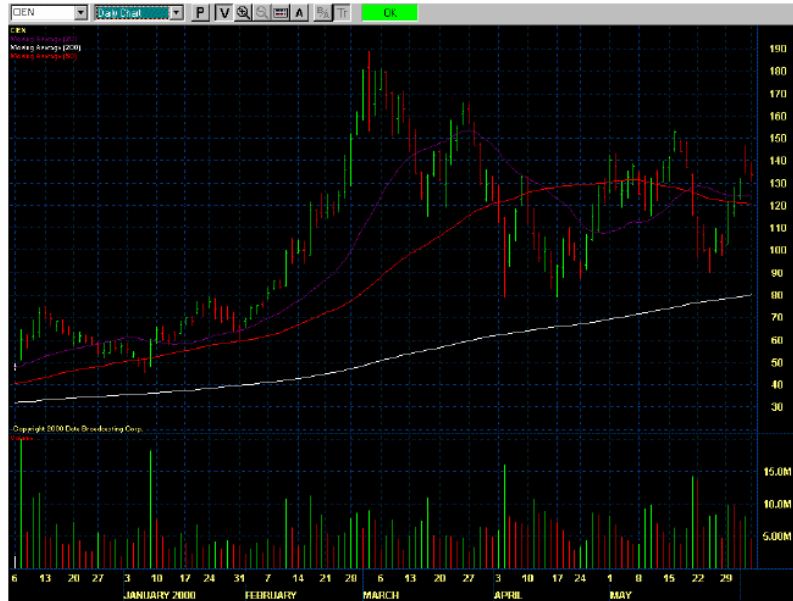
6-Month CIEN Chart:

Notice a couple of key things from this 6-month CIEN chart:

- 1) It's been in a trading range from 90-100 support to 140ish resistance the last couple of months.
- 2) The stock will probably get sellers as it approaches 140-150 resistance, and buyers as it approaches 100 support.
- 3) If a breakout occurs, eg it goes over 150 on strong volumen, then it should be bought again.

Those are the three messages this 6-month chart tells me. That, and the 200MA is 80, so that's a likely support zone if the stock really tanks hard for some reason.

These are the things I want to encourage you to get a professional's eye for.



### 10-Day PUMA Chart:

Here's a **short-term** overbought PUMA chart from Mon June 5th 2000. We ran all the way from 20 to 35 in a matter of 3 days, on good news.

What are the trading opportunities here? Do you short it? Do you chase it and buy it here?

I would say do neither. You're too late for the huge run that the stock made, and, you don't want to fight the overall trend by shorting, as it could go higher.

Note the large end-of-day buying volume that propelled the stock's price up. This indicates a likely gap Up opening on the next trading day.

Let's look at PUMA in a 6-month perspective now so we can see what's going on:



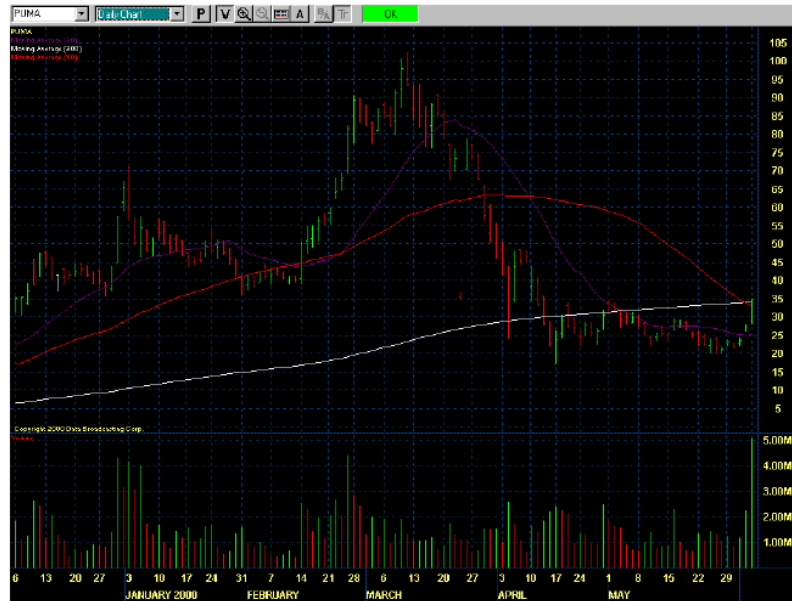
### 6-Month PUMA Chart:

PUMA in a 6-month horizon is telling you what? A couple of things:

- 1) it sold off from a high of 100 down to 16 in a couple of months.
- 2) PUMA was in a trading range from 20-30 for April and May.
- 3) PUMA just broke out of its trading range on record volume.

Is it overbought? Intraday, yes, I wouldn't be a buyer at 34 on the day it ran up from 27. But, the overall technical picture tells us there's a lot of room for PUMA to run to the upside if buyers continue. So, I'll be watching PUMA to look for new trading opportunities in this stock.

The chart shows high volatility, it tends to both run and drop quickly. Stop loss at 32ish for an entry at 34. Sell under 40 resistance.



### CHANNEL SWINGTRADING CHART PATTERN USING 10-Day & 6-month Charts

#### 10-Day RNWK Chart:

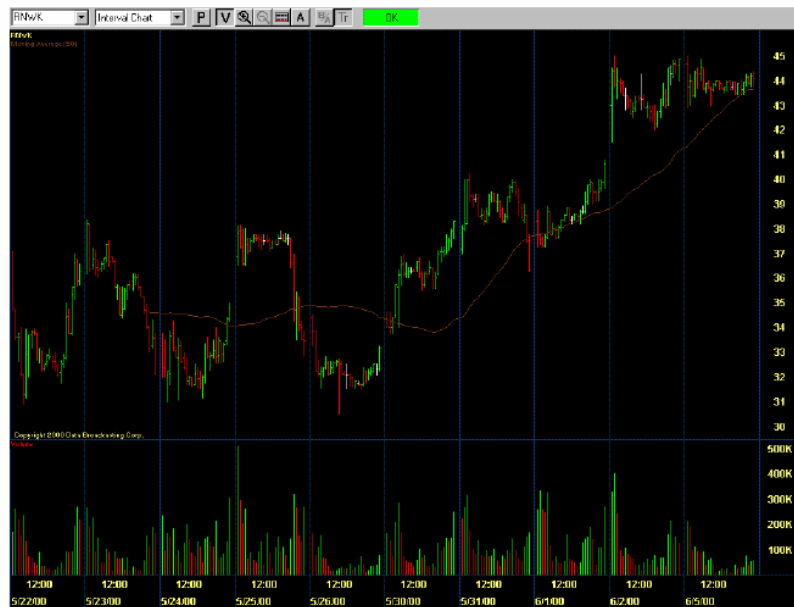
Here's a stock that's been oversold and is relatively safe for a trading channel, prior to a recent breakout, RNWK.

RNWK's 10-dy pattern shows you that it "rolled" between 31 support and 38 resistance several times, before breaking to the upside over 40 recently.

This stock was easy to play in the trading range, and was in our daily pick list for the entire week due to this. It's broken to the upside and has probably entered a new trading range. All we can see for now is that 45 is resistance and 40ish is support.

How do you trade it? I would not enter here, for a swing trade you'd wait for it to break over 45 to buy, or, wait for it to drop to 40 to buy, with a stop loss in at 39 3/8 or so.

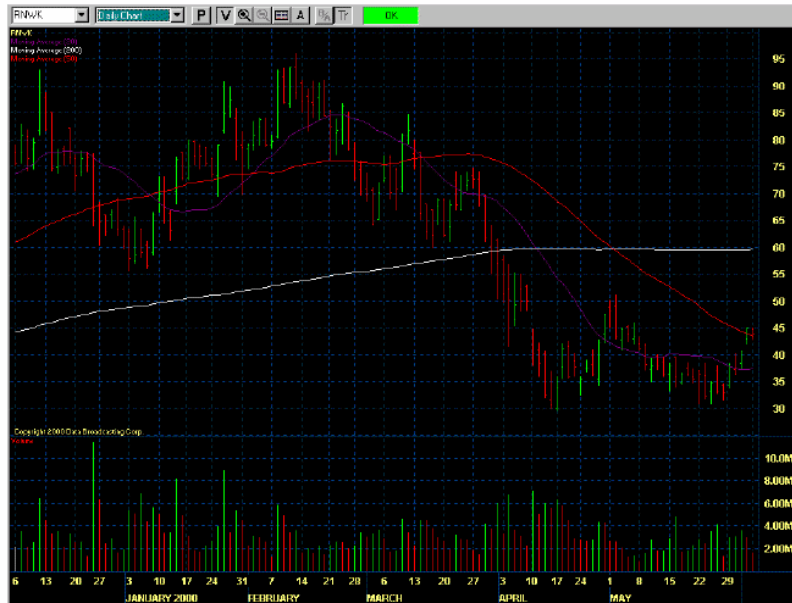
What does the 'big picture' 6 month chart tell you here for RNWK?



#### 6-Month RNWK Chart:

- 1) Lost 60 support from a high of 95 and sold off to a low of 30.
- 2) Recent trading range 31 to 40 or so.
- 3) Next major resistance at the 200MA at 60, next minor resistance at 50.
- 4) Caution sign: Volume has been lower in April/May timeframe than back in Jan-March... so, we want to make sure that VOLUME is a key determinant for making trade entries in this stock.

Other experienced traders all see the same things here, so we trade the support/resistance accordingly. Learn to trade on the side of the market and profit.



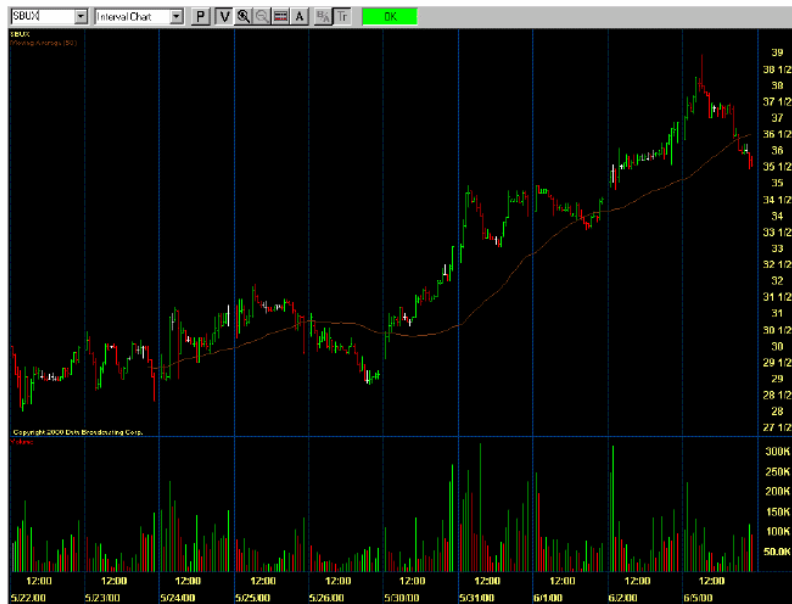
### UPTRENDING SWINGTRADING CHART PATTERN USING 10-Day & 6-month Charts

10-Day SBUX Chart:

Finally, let's look at a couple of steady uptrending charts. It's tough to enter a trade for a stock that's been going up for a long time, because you know it's a matter of time before it sells off, and you don't want to buy the top, right?

The first chart I've shown here is a 10-day SBUX chart. It has had recent positive news and has been in an uptrend for the last couple of weeks. It seems that 40 is a strong resistance area for the stock, and the uptrend broke on the 10th day, with a close that was lower than the open, at around 35 1/2.

How would you trade it? Me, I'd scalp it on the way up, and consider a swing only if it bounced off a major support level like 30 (or, had an upside breakout above 40 1/2 or so).



Let's look at XLNX. The

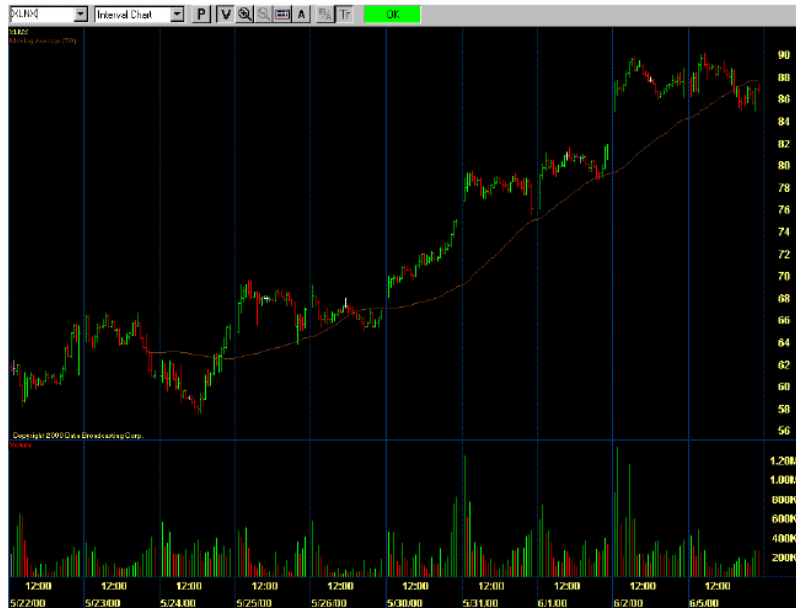
10-Day XLNX Chart:

semiconductors (AMD VTX: XLNX) have all been doing well.

The chart shows steady buying over the last 10 days from low 60s to high 80s. We see a resistance area at the top near 90, right? So, you'd wait for the stock to go over 91 or so on volume before buying, or, wait for a bounce off a decade number support level (eg 80, 70, 60).

Recognizing trends is helpful, when there's no sellers than it means most people are confident the stock price will continue to rise over time, and are hesitant to sell.

Right now, it looks like a trading zone of 80-90 defines where the next trade opportunities will be for XLNX.



Remember, as is any kind of trading, we're always looking for high-percentage trading setups, ones where our risk:reward is small as possible. These chart patterns should help you learn what to look for in successful swing trades.

Remember to get 10-day charts and news at [www.bigcharts.com](http://www.bigcharts.com) if you don't have a pay quote service provider.

## Module Four

# Swing Trading Strategies

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- Understanding the Mechanics of Swing Trading: Recognizing Recurring Stock Patterns & Likelihood of Fibon Retracement

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MODULE 4

### ● Main Points:

- We use support and resistance to identify decent trade entries and exit points, right? Okay, let's look at this a bit closer using what are called **Fibonacci retracements**.
- Basically, you look to enter and exit positions based on a stock retracing off lines at approximately 38%, 50% and 62% of the total amount of the stock price's movement in one direction.
- For daytrading, this roughly divides the day's trading range, once established during the 9:30-10:30 period (roughly, that's where the highs and lows are often made), into the midpoint and the top third and bottom third.
- Similarly, for swing trades, you want to look at the 3-month and 6-month charts, along with the 10-day charts, to establish fibo retracement lines, to help you plan your trade ahead of time... you want to identify where the stock may be likely to run into sellers (if you're long) and get ready to exit the trade before the stock goes back down.
- I call these "recurring patterns" because they are price points at which buyers and sellers tend to reverse, or, points at which the stock may consolidate and "chop around" at. during morning trading.
- [Review this link](#) for a quick one-page tutorial on Fibon retracements at [Equis.com](http://Equis.com)... they have a great free online "TA from A to Z" resource there too, it's required reading for everyone, along with [clearstation.com](http://clearstation.com)
- In time, you will not need to mechanically calculate these lines, or use software for it, it becomes 100% intuitive, eg you get a feel for automatically calculating these reversal areas. This, of course, occurs after you've spent hundreds of hours looking at thousands of charts.
- Again, a good rule of thumb is to look first for the midpoint of a trading range (eg notice a stock will make its "big move" from 9:30-10:30 then settle in at roughly half the distance between the high and low, the midpoint? This is where you should not be trading, low-percentage zone, rather look to buy off the fibo bands and the previous days' high and low support and resistance areas, etc.



## USING FIBONACCI RETRACEMENTS WITH 10-DAY CHARTS FOR SWING TRADING

Look for trade entries and exits within a trading range at the 38%, 50% and 62% (or, roughly the midpoint and 1/3 and 2/3 points of the trading range)

See in this 10-day CRDS chart that:

1) our 10-day range is 7 to 14

2) after running up, the stock sold off down to a low of roughly 1/3 of the range, or 9...the buy point would be on a breakout above this level (also a good secondary target to cover a short in the stock off the top of the range, as is 68%, the first cover target)

3) buyers brought the stock back up the 2/3 of the total range, to roughly 12 1/2.

4) the next buy would be on a breakout above the range, above 14 or so, or, off a bounce that occurs on any of the prior bounce areas, eg off 9, 10, or through 12.

We look at a lot of midpoint (fibonacci 50%) trading in this 10-day chart of RNWK:

1) Ok the chart is busy, I wanted you to look for the same types of things that I do when trading RNWK.

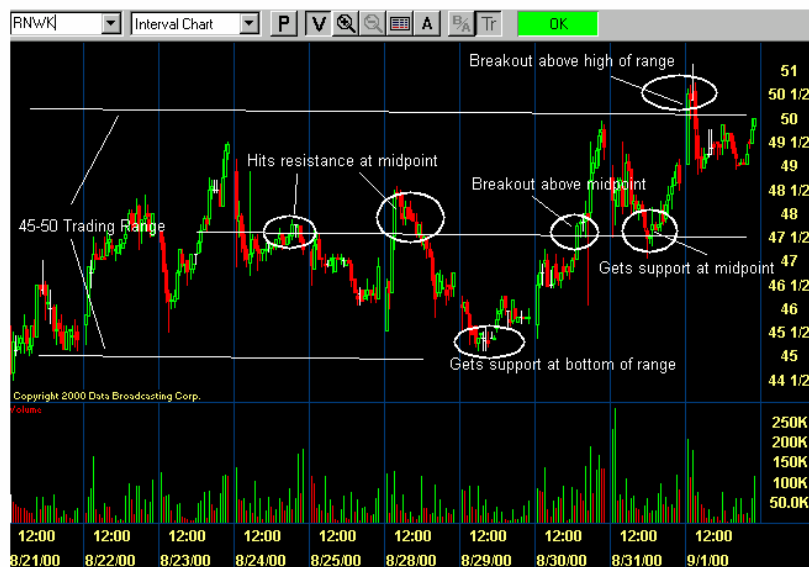
2) The buy on 8/29 was obvious, as it was retesting a prior low... the stop loss would be at 44 1/2 or so, but we did in fact get buyers, at 10:30 as usual, off support. High-percentage easy day or swing trade entry.

3) there are a number of minor breakouts earlier in the week that would have been fine for daytrades (can you spot them in 8/23 and 8/28?).

4) the midpoint becomes a new support level for the stock on 8/31, as it went through 47 1/2 on good volume.

5) It broke out above a key resistance area, 50.

6) The next buy would be over 50 1/2 on good morning volume, with a stop loss at right around 50. Or, off support



at 47 1/2 bounce, or off support at 45 bounce.

**Finally, let's look at 10 days of KANA** - another well-annotated chart to help you see the precision with which I look at stocks. By the way, I do all this stuff I have annotated in my head, I wanted to show you what I'm looking at when I see this chart, using fibo retracements.

1) Okay, we define our range as 34 1/2 to 40... note that we didn't know where a bottom would attract buyers til 8/29... which is why we just watched it til then... never try to catch a falling knife or guess where the bottom is, for all I know it could have gone to 17... I wanted to see buyers come back in with strength.

2) Having defined our trading range (on 8/29), we then draw our midpoint line, at 37, and patiently wait to see buyers come back in above 37. If you are a swing trader who can't watch the market closely intraday, you might enter a buy limit order at 37, for example.



3) Now we know there will probably be resistance at the previous high, at 40, especially since it's a whole decade number, right? Right? Ok then.. so our exit target is right under 40, at, say, 39 5/8 or 39 3/4 or so. We lock in a 2 5/8 point profit on an overnight swing trade hold.

4) Did you blink and miss it? Remember this is how we trade professionally - you have to be aggressive and know your technicals and execute trades accordingly. It takes discipline, study and practice. No it's not easy. A 9-5 day job is easy I suppose. Then again, you get paid a whole lot less for that too!

Does this make sense to you? Not yet? That's ok, it will in time - just remember to use the 1/3, 1/2 and 2/3 as a rough trading guide to help you decide when to get in and out of trades. This also applies to intraday and to longer-term (eg 3- or 6-month) time intervals as well. Apply it to the unique trading style and risk management strategy you have for your stocks.

## Module Four

# Swing Trading Strategies

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MODULE 4

- Chart Patterns: Buying into Pullbacks vs. Dead Cat Bounces

### • Main Points:

- When it comes to identifying good trade entries for swing trades, I like to pay attention to both "dead cat bounces" and buying into pullbacks on slow uptrending stocks.
- **Dead cat bounces:** when a stock sells off more than 15-20% for a big gap down, and gets a wave of buyers within the first trading hour after the gap down... (these are also good for daytrades, especially when played premarket over ISLD).
- **A note on buying bottoms:** frequently, I've found that the first bottom isn't the 'real' bottom, a second selling wave can also follow, which can be painful. which is why stops are so important... look for consolidation (see column to right) before trying to buy a bottom, or an otherwise compelling technical reason on the chart, eg it's bouncing off a 52-week low that's a decade number (like 20 or 30) at 10:30... and of course you need to still keep a tight (3-5%) stop.
- **Buying into pullbacks:** a stock has been gradually bought over a long time period (eg 3-6 months) in a slow steady uptrend... you can buy it on a pullback, again with a stop loss right under a previous low.
- **Consolidations and why they're important** when you're bottom fishing: a 'consolidation' is when a stock has reached a tight trading range that it hasn't yet broken out of. Let's say AMZN sells off down to 28 over a couple of days... do you buy yet? No... you wait for either a sharp reversal (more of a daytrade), or wait for the stock to "settle" into a tight trading range for at least 2-3 days. Why? Because this tells you buyers and sellers are evenly matched, eg the sellers are no longer in firm control. The stock looks flat. You then buy when the stock makes a new high right above the trading range (with a stop under the top of the range). This tells you that buyers are in control, at least for now, and a trade can be entered from the long position. The inverse of all the above is true for shorts, naturally.
- Another good example is HLT after it sold off, it stopped selling off and traded in a tight range for several days before getting buyers, at which point a high-percentage trade entry could be made.

## BOTTOM FISHING (BOUNCE) CHART PATTERNS

In swing trading, we always pay attention to both the 3-6month and 10-day chart.

Here's a tip you never hear about: when buying into dips for a downtrending stock, Make Sure that **buyers re-emerge regularly** and that it's not a slow decline with no buying interest (see ETYS for example)...in other words, make sure there's some volatility, **ups and downs**, in the 6-month or 3-month chart if you're buying into a downtrend. You can see this in the 6-month DISH chart to the above right.

Lets look at the 10-day DISH chart now for the 'real action'... Where do you see consolidation in this 10-day chart? The middle 4 days or so...eventually buyers win and the stock breaks above 34 1/2, where a swing trade buy should be entered.

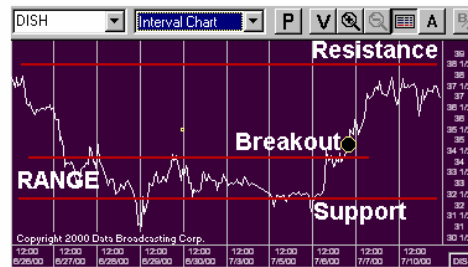
Now let's look at DCLK, my favorite daytrading stock of the moment. The downtrend looks pretty ugly, but, looking at a 1-year chart you see that 30ish is a 52-week low and we can expect support there. The stock consolidated around 40 for a couple of weeks, before dropping (and then bouncing).

When buying swing trading bottoms, I often have found the first bottom is not the real bottom...we see this in DCLK...I bought at 33 here, thinking it was the bottom, it sold off some more (you would stop out at 32 at the end of the day, taking a small loss)

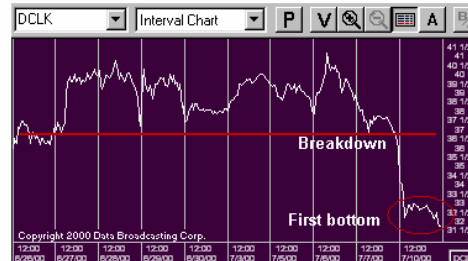
The next day, you can see it dropped all the way down to 29-30... you would buy again once it breaks over 30.

Now the real question is, where do you sell? I would sell right under 40 (previous consolidation zone, where buyers and sellers disagree), and re-enter right above 41 or so. Earnings are due out,

6-month and 10-day DISH Charts:



6-month and 10-day DCLK charts:



which provides another gap wild card'.

HLIT: Strong selloff down to low 20s from a high of 160...hmm probably a good time to buy, with an exit target of 60-70 over a one-quarter (3-month) time interval.

I like the consolidation right over 20, this looks to be the bottom for HLIT.

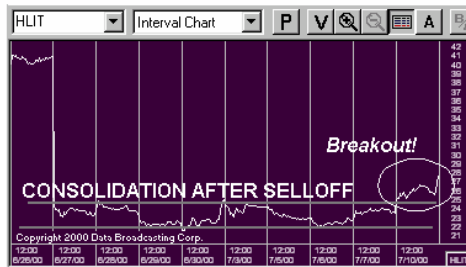
In looking at the 10-day chart for HLIT, we enter a buy after the breakout from the consolidation range of 22-25...eg we buy the stock at 25 1/2 or so. Our initial exit target is roughly 1/3 to half the difference from where it dropped...eg it dropped from 41, we buy at 25 1/2, we look to sell at right under 30 (29 1/2) the first time, then buy again at 31 or so and look to sell again at 37-39. Sit out the resistance areas at 'decade' numbers like 20 30 40, sell at the 8-9 and rebuy in at the 1-2.

**Using the Composite and Sector Indexes to swing trade:**

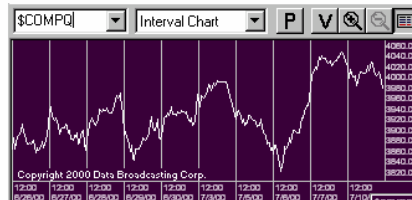
Ok, we also always watch our sector/index charts right? The one thing I want you to take away from looking at these two charts (Nasdaq Composite and Internet composite) is this:

The \$GIN is underperforming the \$COMPQ, so you dont buy internet stocks yet (wait for key support areas at the \$GIN for a bounce), and look for other sectors to play in long right now, eg semis or networkers, whatever's strong...use the divergence as a relative strength indicator.

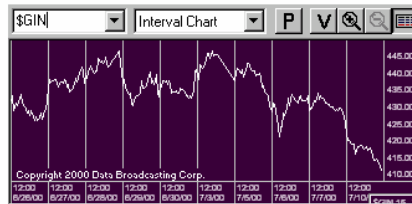
**6-month and 10-day HLIT charts:**



**10-day Nasdaq Composite and Goldman-Sachs Internet Index charts:**



internets are weak, short/sell/wait for a bounce (don't hold longs):



**BUYING INTO PULLBACK CHART PATTERNS**

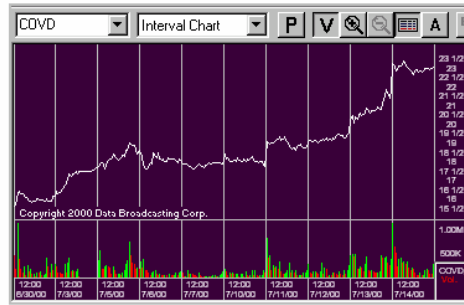
**10-Day COVD Chart:**

I find it difficult to buy into uptrends, as I hate to be the "bagholder" buying the top of the day. But, we need to be able to buy strong stocks that are getting stronger. How do we do this?

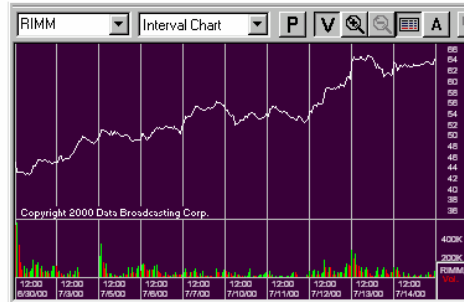
One strategy is to buy dips and breakouts in uptrends.

We said COVD was a buy at 18, ok it was, now what? I would have sold right under 20, buying again at 20 1/2...you see a consolidation here on the last day...I'd sell here and wait to rebuy a dip later. During the run up, you try to buy towards the "bottom 1/3rd" of the day's trading range as a general goal.

Looking at RIMM here, you see lots of buying over a 10-day period. What do you notice regarding time-of day effects for RIMM? It generally tends to get afternoon buyers, do, this is a stock I'd look to buy more often in the afternoon, say 1:30-2pm, than in the morning. The low of the days tend to be at 10:30 and in the late afternoon as well, say at 3-3:30. These are the buy times for this stock.



10-Day RIMM Chart:



Well, that should help with some of the patterns you should be on the lookout for in terms of swingtrading bottom bounces and uptrend buying times. Get to know the 'personality' of a few stocks and trade those.

## Module Four

# Swing Trading Strategies

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MODULE 4

### • Identifying High-Percentage Swing Trading Patterns: It's Saying "Buy Me Here"

#### • Main Points:

- We've covered a number of effective swing trading strategies in earlier lessons. This lesson will help you identify chart patterns that should be profitable if played with proper risk management and profit-taking strategies.
- Remember from one of our day trading lessons that you do not want to be "trading just to trade" or trading because you're bored, or because you're pressuring yourself to trade. Instead, you want to be a sniper looking for selective high-percentage chart setups
- A high-percentage swing trade is generally either buying a breakout above a 2-3 day consolidation, or a reversal after a sustained decline (eg it finally looks cheap to more buyers than sellers).
- In swing trading, this means we rely heavily on chart patterns, earnings calendars, and market/sector/index charts, along with 200MA and 50MA lines.
- Below, I've gathered a handful of what I consider to be high-percentage swing trading chart pattern setups that are worth watching for trade opportunities (August, 2000).
- Remember that good traders **respond** quickly to buy and sell patterns, **versus trying to predict** what will happen. I've been burned, as we all have, by "trying to catch a falling knife"...in swing trading many traders were wiped out in April's dip, because they did not use stops.
- The chart patterns below may well sell off and not be good swing trades, I don't know. All I know is how I'll trade each of them based on what the buyers and sellers are doing, I've got trade entry and exit points, along with stops identified for each pattern.
- Remember we use 10-day charts for all trading, especially good for identifying swing trade support and resistance levels. I also refer to a 1-year and a 3-month and/or 6-month chart.

## MORE BOTTOM FISHING (BOUNCE) SWING TRADING CHART PATTERNS

### KLIC Swing Trade

Remember, when buying what you think is the bottom, make sure you see an uptrend and/or volume reversal before buying, as the first bottom is often just the first of two. Let's look at KLIC here:

If you had bought the first bottom at 25, you'd be wrong... instead, you should pay attention to 2 things before buying any bottom for a swing trade:

#### 1) Heavy volume

#### 2) An uptrend, indicating buyers are stronger than sellers.

You did **Not** see either of these on the first drop on 8/1, so you **wouldn't** buy. You'd buy on either of them, eg on 8/3/00.

Where do we see this? On 8/3/00...is the trade good for more? Maybe, but I'd put my first exit target right under the consolidation at 23... since I sit out decade resistance I might buy at 16 1/4 and sell at 19 1/2 or so. A stop loss would be at 15, of course.



### CRDS Swing Trade

Again, buying the first bottom at 9 on 7/27 would've been wrong...also I never buy 9's anyways (9,19,29,39,49) since there'll be resistance at the decade number above it. We see a heavy volume reversal at 11am on 7/28, a swing trade could've been entered there with a stop at the bottom at 4...

I'd wait though...a good next entry would be over 10, or, if the stock drops to 5 or so and starts to bounce, think is the bottom. Remember to be skeptical and wait for strong buying strength to enter the position...don't chase, but make it go through a previous resistance level or new high of day (hod) to enter.



### MRVC Swing Trade

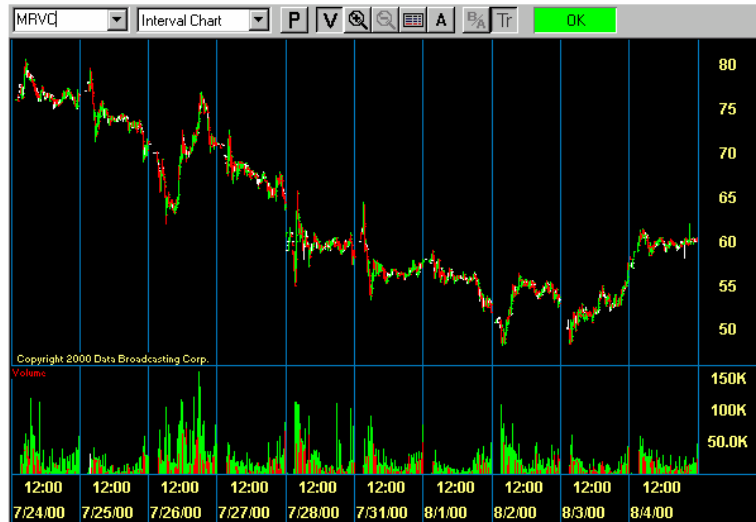
(I first heard about MRVC from Tony Oz's new book, it's got great volatility for trading).

What's the 2 key patterns you see here?

a) **Volume uptrend** off 10:30 bottom on 7/26.

b) **A double bottom at 50 support** on 8/2 and 8/3, followed by buying on 8/4.

What's the play? Well, I bought at 50 on 8/2 for a good trade...it ran 5 points in 1/2 hour, easy to play. Buying seems to have stalled at 60 on 8/4... If it gaps to 62 or so on the next trading day And Still Has buyers at 10am in an uptrend then I might buy, or off a pullback to 55 or so at 10:30.



### KANA Swing Trade

What's the story on KANA here? Well, a bunch of people sold it down to 40 on 7/27... but we didn't buy because ... ?

No uptrend...no buyers means I'm not going to buy either. Sure enough, it fell another 25% down to 30 on 8/3.

When do you buy next, you ask? Well, I'd wait til it's over 40 1/2 resistance in an uptrend on better than average volume, or buy in the low 30's (30 to 31 1/2) on a reversal at 10:30.

Buying on the close on 8/4 at 36 probably would be ok too for a possible open gap to 36 1/2 - 37, but I wouldn't buy on a Friday for a weekend hold, rather I'll play on Monday 8/7 instead.



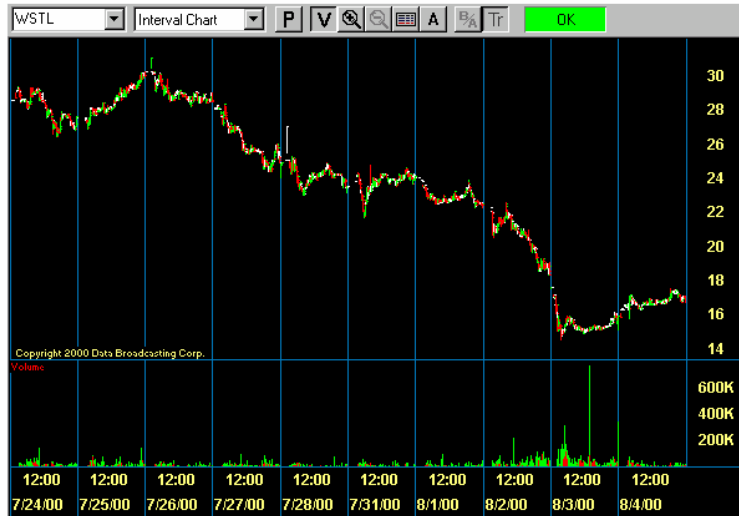
### WSTL Swing Trade

Do we have a bottom bounce here? Well we do see both volume and an uptrend, so the answer is Yes, a buy on 8/3 would be ok...

Next entry would be at 18 1/4 on a morning uptrend, with a first exit target right under 20. Swing trade exit is at previous low in the downtrend, eg I'd be out at under 24 (buy 20 1/4 sell 23 1/3 or so).

Stop losses: Well you always place it at a previous low, so the absolute stop loss would be at 15 or so, I'd keep it a bit tighter, on cheap stocks like this every 1/2 point counts in a swing trade.

Bounce pattern: This is typical, look closely at 8/3: you see a morning selloff, a quick bounce, then it sells a bit and consolidates. The next trade entry would be right Above the bounce point on 8/3, about 16 or so... This occurred at the end of the day, so I'd either buy for the next day's gap up (risky), or, more likely, buy on the next day as long as it stays above 16.



### T Swing Trade

Whatever happened to poor T? I guess all those bargain long distance plans ate their lunch. Hah it's about time.

Anyways, what's the play? Actually, based on this chart pattern it's still a short.

However, we're getting close to 30 in a sustained downtrend. I would expect a lot of stops to get taken out at 30, and there should be a some volatility to take T up a fair amount from its current levels. That is, I'd expect to see 33 before I'd expect to see 27.

30 probably "looks cheap" to institutions, it looks cheap to me, I'd be a buyer, with a stop at right under 30, say at 29 3/4. Exit target at half the 10-day chart range (a fibo number), say at 32 1/2 or 33.



### USING 1-YEAR CHARTS TO HELP IDENTIFY HIGH-PERCENTAGE SWING TRADES



Note: the bottom three 1-year charts are sorted in descending order of "strength", eg RNWK has the strongest chart, followed by DCLK followed by ATHM.

I also frequently (eg daily, before entering any swing trade) refer to 1-year and 3-month or 6-month charts to identify 50MA 200MA and major support/resistance levels.

### RNWK Swing Trade- 1-year chart pattern

What do we see here? RNWK is in an uptrend here and now is a good time to buy the pullback to 40ish.

If you draw a trendline you see support at roughly 35, and tops right under the 200MA at 60.

A stop loss would be at no more than 5-8% of the share price, eg 2 points or so, with an exit target of right under 50 the first time, then a re-entry at 51 or so and exit target at right under 60.



### DCLK Swing Trade- 1-year chart pattern

DCLK has got to be the very best buy out there right now, in my opinion. If I had 100K for a single position trade I'd buy DCLK at 36.

The one-year chart shows we're testing the 52-week low, and the financials on DCLK are the best of the internet stocks, period.

Privacy overhang issues have been resolved, and I am positive DCLK, once over 40, will "never look back". Keep this one on your watchlist.

I could be very wrong, maybe DCLK will go to 15 in the next few months. That's what stops are for.

DCLK is currently my favorite trading stock for both swing and day trades, along with EXDS RNWK MRVC.



### ATHM Swing Trade-1-year chart pattern

ATHM looks like it's taken a beating and the sellers have clearly won for calendar 2000. Waiting for a bottom? I thought 20 would be a good bottom, but buyers never really came back into the stock.

Here we see it's dropped all the way to 13 1/2...this is probably the 'real bottom, but I'd wait til it's over 15 1/4 to buy back in.

Note that analysts ratings are often worthless (the first 4 letters kind of say it all lol), this stock is highly-rated, as both RNWK as DCLK are, but has been selling all year long.

A somewhat riskier ATHM entry is to buy now and put a stop in at 13 1/2 (which I did last week).



- **Knowing When to Turn a Day Trade into a Swing: Overnight Gaps and Chart Patterns**

**Main Points:**

- Sometimes you may enter a trade and then wonder when to take profits/losses...eg should I turn it into a swing trade?
- The answer depends on the price momentum of the stock and your entry point.
- Never take home a losing position saying "oh well it's down for the day so I'll make it into a swing trade". That's how traders go broke.
- If, however, you are buying an end-of-day selloff bottom in anticipation of an upside gap the next day, that's another story. Some stocks that sell off more than 8% or so on no news may well rebound a couple of %age points the next day, good for an open bounce scalp.
- The other time would be when the stock closes out strong, at the high of the day, and you expect an upside gap on the next day. Again, it's a matter of extremes, if the stock has skyrocketed you should sell half your position to book the profit, holding the balance in case there's an upside gap. If it gaps down, wait, and if it keeps selling, stop out with a partial profit still in hand.
- When to turn what was a day trade into a swing trade? When you think the buying momentum will continue, of course. It's a matter of degree, and the trade sizes you are playing. I'm a big fan of varying your share position size, eg start with 300 shares, add 100 if it continues, sell out 200 at what you think is a top, hold the balance etc.
- Let's look at chart pattern examples below:

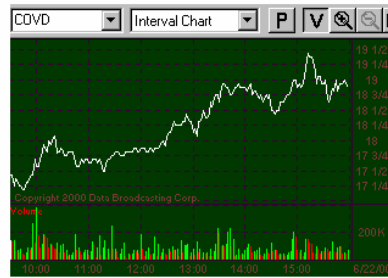
**Remember to Swing Trade with 10-day and Intraday Charts**

**Swing Trading Strong Bounces: COVD Example**

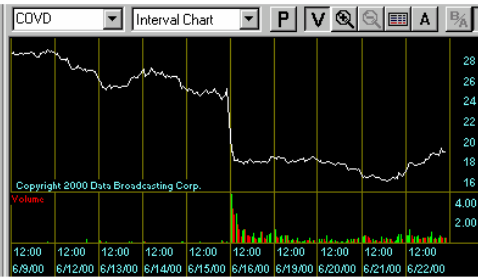
Here's COVD, a stock that recently sold off down to 16 1/2. It has broken through resistance at 18, and is trading over 19 at the close of the day.

A day trade entered during any of the previous 5 days on a 'dead cat bounce' buy should be sold 1/2 here at the end of the day to lock in profit, with the other 1/2 held for a sell right under 20.

1-Day COVD Chart:



10-Day COVD Chart:

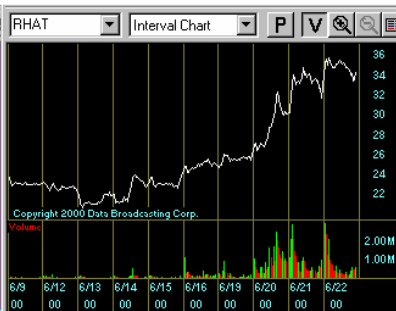


Even if the stock had been entered as a day trade early in the day, you would still hold 1/2 the position into the close for a swing trade, with a trailing stop at 18 1/2. If the stock gaps over 20 the next day, you would add to the position. If it gaps down a bit, use a trailing stop loss at no lower than 18.

1-Day RHAT Chart:



10-Day RHAT Chart:



**Buying Pullbacks in Uptrends: RHAT Example**

You can see that RHAT has been climbing for 5 days in a row. Do you sell or buy? I would buy if the stock climbed over 36 1/4 on volume; if I was already in I would have sold the 10:00am top this am at 35 3/4 and waited for a lower point to re-enter.

If you are entering a new position, you would place a stop at 33 here. (33 1/2 if you wish).

What does the volume tell you? Buyers in the am, low volume the rest of the day.

1-Day RNWK Chart:

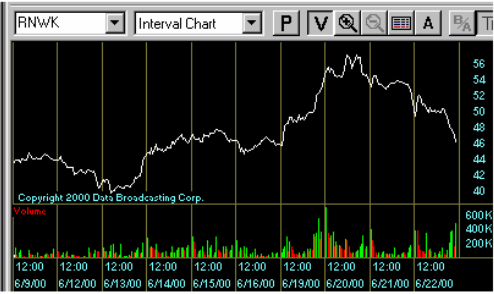
10-Day RNWK Chart:

**Risky Bottomfishing #1: RNWK Example**

It's important to know the trading range and trend for your swing trades. Here is RNWK, it broke over 44 resistance a few days ago and has dropped to near that level today.

I entered a small-share long position on the close at 46 1/16th in RNWK, with a wide stop at 44 1/2.

Why? The stock had plenty of buyers for at least 1/2 of the previous 10 days (closed higher), no adverse news has come out, and the stock lost 12% for no 'good reason'...



Why is this a risky play? 10-day support is at 40, and it's at 30 for a month-long timeframe. I am risking an open gap to the downside, as low as 40, but more likely in the 42-44 range. I believe that it will retest 50 within a week, however, so I am willing to chance it. I still have a firm stop at 44 1/2, if it gaps lower than 45 on the open and continues to sell I'll exit the position, and not re-enter til it has climbed over 47 again. If I had been playing it earlier in the day, 50 was the support level and I would have exited once it lost 50, or entered a short position.

1-Day DCLK Chart:

10-Day DCLK Chart:

**Risky Bottomfishing #2: DCLK Example**

I bought DCLK on the close at 40 7/8. hmmm...why did i do that?

No buyers anywhere in sight for DCLK, is this a bad entry? Maybe, except I know that DCLK tends to gap up on the open after a selling day. Previous support is at 38, which is where my stop is at. Let's say it gaps open to 41 1/2, and starts to climb the next day. Where do I sell? Right under the previous days' major trendline, at 43. So, I'd sell at 42 7/8.



These are a risky type of swing trading, buying a down close at the end of the day. **Some guidelines:**

- If buying at the end of day low for a swing trade, make sure the stock **has sold off significantly**, eg over 8%. I like to buy especially if it's dropped over 15% for no 'good reason'...the price tends to correct back up within 1-2 days for at least a few percentage points.
- **Stops are still important.** Do not panic out, however, if the stock gaps down premarket. Remember buyers tend to be attracted by large gaps down. Only sell out if the stock heads lower 10-15 minutes after the open **after the open gap down.**
- **Take an open profit** if the stock gaps up on the open a decent amount, eg 4-5% above what it closed at. I tend to do well on overnight holds that gap up.
- Remember that gaps on the open of over 5% on volume above 20K attract traders...both on the upside and downside. **Be prepared to trade gaps**, they are among the most profitable of trading opportunities. Remember not to trade the first 10-15 minutes of the open, except to close out open gaps up.
- **Watch time and sales...** I remember seeing a lot of traders getting burned on shorting ISLD after a gap up, only to see it continue higher. Remember, open gaps up don't always sell off, and open gaps down do not always get buyers.... watch time and sales the first 15-20 minutes to get a clear picture of the market's direction. Cup and handle patterns are important to look for using your 3-minute bar or candlestick charts during the first 20 minutes of the market open.

- How to Clear Your Profits in Swing Trading: Taking Money off the Table at the best time

● **Main Points:**

- As in any type of trade, when you sell is much more important than when you buy. Let's look at how to know when "enough is enough" and you can exit your position with a solid profit.
- The challenge is to let your profit run, but not to wait so long that other sellers come in and the price drops to below where you would want to exit.
- Nobody can pick tops and bottoms exactly, the key is to manage your trades, stops, and exits carefully.
- In swing trading, I tend to look at Chart Patterns/TA, Percentages, and Exit Targets.
- Since you are risking more, in terms of a bigger stop, in your swing trades, you must develop the patience to let the trade work in your favor, and not sell to soon at the first sign of green.
- Map out your trade ahead of time and write down where your stop loss is and where you will look to take profit at.
- If the stock you've been holding for several days has a terrific breakout day and runs, go ahead and take the profit... don't give up a nice profit because you're only a day or two in a trade that you had expected to need to hold on to for longer. Take the money.
- Let's look at some specific strategies below:

**Always Sell Right Under "Decade Resistance" and Buy Back if It Breaks Through**

**Always Sell Right Under "Decade Resistance" and Buy Back if It Breaks Through**

This is an excellent guideline to follow for helping you exit your trades with the maximum profit possible. The only time you don't sell as it approaches whole decades is if it's running up through the price point on good volume.

Always always sell your stock as it approaches a "decade" number, such as 10 20 30 40 50 60. You can always buy it back 1/4 point above the decade number if it keeps going up, but you should Always take your profits right under the decade number.

Example: You bought RNWK at 42 for a swing trade on 4/24/00. You set your stop at the support level of 39 3/4 (right under a whole number).

Your profit target is high 40s. You get ready to sell at 47. The stock gets buyers, You fire off a sell order at 49 5/8, booking 9 5/8 points profit in 1-2 days.

Look at RIMM - same story, it approached but could not get buyers to bid over 50 for it. It fell back into a trading range here. The next time to buy would be off a dip to 36-38 or above a breakthrough at 44.



**Take Profits if the Daily Percentage is Over 15% in Your Favor**

Keep a portfolio tracker where you can see it at all times. (eg esignal or quotetracker.com etc).

The more a stock goes up, especially above 15% on the day, the more likely you are to get sellers in this region. Of course, you should use trailing stops, don't exit the position prematurely.... However I find that I'm antsy to hit the sell button if the stock is up over 15-18% on the day, that's a bit extended to the upside.

I always keep a portfolio list sorted by Percentage, with the green/up stocks at the top of the list. I'm looking at the deep reds (eg over 8% in the red) for possible bounces if the reason they sold wasn't earnings or other major "real reason" for selling. A selloff above 6-8% in an otherwise flat/up market on no news is always a good candidate to look for bounces.

In this example, we called VISX as a sell from a previous hold since it's up 18.6% on the day.

Symbol	TSize	Pct
VISX	100	+18.6%
BRCD	100	+13.6%
ERTS	3.00K	+12.1%
MKWTW	2.50K	+9.3%
SPYG	100	+10.3%
NEON	400	+9.4%
CNET	900	+7.9%
PSUN	5.00K	+5.4%
GENE	100	+4.5%
MMPT	1.00K	+3.3%
KR	100	+3.3%
RIMM	2.00K	+3.2%
BVSN	200	+3.3%
OMKT	300	+3.6%
ROST	100	+3.2%
CMGI	600	+2.5%
PMTC	300	+3.3%
INTU	100	+2.4%
CS	300	+2.7%
IMGX	100	+2.4%

### Look at the Big Picture: 6-month, 10-day, Intraday Charts

As we mentioned in Module 1, you should use a "zoom" approach to TA for your stocks, eg start by looking at the 6-month or yearly chart for major trend, support and resistance.

In this VISX example, you can see we had a nice long consolidation period from 14-19, with a recent breakout. Resistance is at 19-20.

What's the 6-month chart also tell you? Look at the MA lines, we're finally above the 20MA, which is bullish here, and we have a green "volume spike", so we are going up on decent volume. That's a good sign.



Next, take a look at the 10-day chart. What's it telling you? No sellers anywhere.

The stock has been in a steady uptrend for the last 2 weeks, and finally on Friday we had a volume breakout above 20, a very bullish sign.

We exit the position right at 19 3/4, however, and Sit Out the tug of war between buyers and sellers as it tries to take out the resistance at 20. That's a low-percentage battle to be involved in, so you want to take your profit out beforehand. If it breaks through the decade resistance level and consolidates above it, then we can buy back in.



In our 2-minute intraday candle chart with MACD and stochastics, we see that the stock trended up nicely all day long. The stock consolidated right at 20, which we expected over a week ago.

So, we exit right under 20 to take a healthy profit and wait for another profitable trading opportunity in this stock.

The fact that the stochastics are in a wiggling downwards trend is bearish, plus the MACD looks to be weakening, so it's a triple confirmation of a time to exit the trade.

Use all 3 of these rules profitably in the market and you'll be ahead of the "herd" of paper/new traders out there.



Knowing when to take your profits is always a struggle - I've often left large amounts of money on the table as I sell with a nice profit, only to see the stock move much higher. I always say "Doh!" like Homer Simpson when that happens.

But, for every time I leave money on the table I sell at the top 2-3 times as often. So, I learn that nobody can pick tops and bottoms, you just need to have a solid, disciplined risk/money management strategy in place.

Your losses must be small, your wins must be moderate and consistent. Don't try for "home run" swing trades of many points, if you're up with decent profit, then sell and rotate your capital into the next, higher-potential trade that presents itself.

## Module Four

### Swing Trading Strategies

◀ PREVIOUS NEXT ▶

- Making the transition from swing trading into day trading, and vice-versa

Back to  
MODULE 4

#### ● Main Points:

- Decide whether your trade is a day or swing trade Before you get into it. You are not allowed to rationalize and let a losing daytrade become a "swing trade" and hope it goes up again someday.
- You may at some point in your trading life want to spend more time with one type of trading than another, or, do both types of trading.
- I recommend that you use a low-cost online broker (like datek.com or interactivebrokers.com etc) for swing trades and a DAT (direct-access trading) broker for daytrading. Have Two Separate Accounts, one for your daytrading, the other for your swing trades. That's what I do (cyber for daytrading, datek for swing trades).
- If you are unsuccessful in your current trading efforts, remember to 1) trade the market the way it's trading, eg don't go long in downtrends, or expect big runs in choppy trading times like summer 2) be flexible and try a different trading style, using papertrading and/or small 100-share trades to test out your approach.
- Be patient with yourself, making the transition from one trading style to another is time-consuming and takes hard work, patience, consistency and discipline on your part.
- People who have been unsuccessful at day trading can be highly successful swing traders, and vice versa... it depends on your personal trading style, equipment/tools, and other factors. That's why it's important to experiment with different trading styles until you find one that works for you - that's why I'm including this lesson, to help you with some ideas for trying out a different style.

Going from Day Trading to Swingtrading:



In changing (or adding) **swing trading** to your arsenal of trading styles, you take on added risk and potential added reward as well.

Your timing does not have to be as precise, as you are shooting to enter towards the lower end of a trading range (or a breakout above resistance), and sell at the high end of a trading range.

Your stops should be wider, and the size of your trades should be smaller (eg 100-300 shares).

Here are some of the things to do keep in mind to help you adopt swing trading as a personal trading style:

Trading Signals to Watch:	Equipment Needed:	Trade Sizes/Picks:	Personality:
<ul style="list-style-type: none"> <li>MA crossovers, eg 20MA, 50/100/200 MAs</li> <li>10- and 30-day trading range support and resistance levels and trendlines</li> <li>earnings release dates</li> <li>news-related gaps, either direction (up/down) on the open</li> <li>buying/selling pressure in the entire sector the stock belongs to over a 10- day period, eg \$GIN chart for internets, \$SOX for semi's etc.</li> <li>Seasonal fluctuations, eg retailers, energy strong in the fall/winter season etc.</li> <li>Candlestick reversals (1-day charts).</li> </ul>	<ul style="list-style-type: none"> <li>A single PC monitor, slow 56K modem and online brokerage account is fine for swing trades.</li> <li>You do not need to invest in the commission load of a daytrading broker and data feed if you're solely swing trading.</li> </ul>	<ul style="list-style-type: none"> <li>Recommend that you trade a "basket" of 3 to 5 stocks simultaneously with small shares, eg 100 - 200 share trades for your swing trades. Remember that bad news can cut a stock in half, so you want to minimize your risk exposure for the multiple overnight holds you'll be trading.</li> <li>Picks can be "dead cat bounces", eg buying ICGX DCLK or others that have sold off and consolidated for awhile at a key support level, or breakouts. Good companies who have had overreactions to news and whose price has attracted buyers would be good trades to enter (eg open gaps down, just like daytrades, but with a longer holding time horizon).</li> </ul>	<ul style="list-style-type: none"> <li>Ahh, this is fun. The swing traders' personality needs to be a bit more relaxed than the daytraders, eg you can't panic if the stock loses 1/2 point.</li> <li>Conservative, deliberate, patient, analytical personality types do well with swing trading. Those who are impatient will stop out of their swing trades prematurely. It takes patience to "let the winners run" and not take profits too early.</li> </ul>



**Swingtraders think**

Ok, I'm in now, I'll let the trade work itself out this week - let me study the chart pattern and see where it goes. This is an occasional trading style, may look at realtime quotes on occasion during the trading day..

**Going from Swingtrading to Day Trading:**

If you are like me and are impatient, waiting a few days or a week for a trade to pay off can seem like an eternity, and you'd rather play the market like a video game, taking fast profits based on a complex set of indicators that you depend on to help you navigate your trades.

Daytrading requires iron discipline and a more sophisticated set of trading tools and knowledge than swingtrading does. . Making the transition involves gradually increasing your trade size to where you can trade blocks of 500-1000 shares in short timeframes, almost exclusively under 20 minute round trip trades. It's like racing on a track, you need to know what you're doing.

Trading Signals to Watch:	Equipment Needed:	Trade Sizes/Picks:	Personality:
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- Gap fills on the open, eg bounces off of major gaps down or short open gaps up
- Stochastics and RSI, sector strength, \$TRINQ/\$TICK/COMPQ and nas futures/spoos.
- Breakout chart patterns on 1, 2, 3 5 and/or 15 minute charts.
- Momentum runs, eg IPOs and breakouts early in the day (9:40, sell at 10; 10:30, sell at 11, 3:40 eod short covers etc)...
- Minimum of two monitors is Required not optional for daytrading.
- Must have a 550+Mhz PC w/at least 256 megs ram.
- Minimum 128K ISP internet connection, eg ISDN/ADSL/cablemodem/T1/T3.
- Must have a pay data feed service (eg esignal or quote.com or RTIII)
- Must have Level 2 and time & sales access.
- Must have a DAT broker
- Note: if you do not have this equipment setup than please do not daytrade, it's financial suicide. Don't race against my Ferrari with your 73 Pinto. It doesn't work. Really. Don't throw your money at the market by not having the proper tools to do the job.
- You can still make handsome profits with 100-share trades on stocks w/3-5 intraday point trading ranges (eg PHCM MRVC DCLK ISLD), but in general we want to trade 300 to 1000 share lots. Add to and build/subtract from your position, scale in and out to manage risk dynamically.
- We are always monitoring the realtime financial newwires for breaking stories we can profit from. We also monitor the realtime days' gainers/losers to play off the retracements.
- We play picks that are making new highs or lows, we play the extremes.
- We keep extremely tight stops and use L2/time & sales resistance and support to enter & exit positions. Precision micro-trading for fast money.
- "Balls of steel" and "iron discipline" are helpful.
- Decisive, knowledgeable, willing to cut a stock loose in an instant is needed.
- People with attention-deficit disorder are probably at an advantage in daytrading.
- Extreme impatience is a virtue.
- Believe it or not, experienced video game players (like myself) do well at trading, as we are accustomed to rapidly responding to signals we see on computer screens. Think about playing rapid-fire games on your pc. I even like games like Tetris, builds quick decision-making reflexes.
- If you have to mull over decisions, like what to order off the menu when you're at a restaurant, you probably won't do well as a daytrader. You can learn to be fast and decisive, it takes practice.



Daytraders think

Do I BUY here this minute? .....or, Do I SELL here this minute?

Over and over and over, several times each day.

#### TIPS FOR MAKING THE TRANSITION FROM ONE TRADING STYLE TO ANOTHER:

Here's a few more tips I'd thought might be helpful in guiding you to make a successful transition if you want to try a different trading style:

- It's a good idea to have a brief written-out trade plan to refer to as you try a new trading style. See the worksheets and activities in Modules 1-4 for handouts and fill-in-the-blanks type resources you can use.
- Paper trade your plan at first to work out the details and gain consistency.
- You must decide for yourself which type of trading is best for you, give it a month or so to see how it goes.
- Whatever you do, do Not switch trading styles mid stream, unless you have a significant profit in the position. If you buy off 40 support looking to exit 43ish, don't sell at 40 1/2 just because you have an open profit, instead just put in a loose trailing stop per your trade plan and stick with it.
- Recognize that any transition is stressful and takes patience and discipline on your part. You should make a brief list of your personal trading strengths and weaknesses, based on the information in the two sections above, and work diligently to improve the areas you feel need work. Hang in there, it just takes time. Preserve your capital and be persistent in your efforts.
- Whatever you do, do not let the market take big money from you - fight like hell for every 1/4 point and make sure to not be afraid to take small losses, no matter what your trading style is. Keeping your money in Your pocket is your primary goal, using your trading techniques and plan to minimize losses and take gains from the marketplace. It's a tough, competitive game and you need to be on the right side of "the street" and pros, not with the the paper/dumb money.
- I find that the financial news tv is generally worthless to watch and avoid it this year. Instead, I focus my energy on playing stocks whose price movements I become familiar with (like DCLK) and tune out the "noise" that tv shows tend to generate. The tv show information is usually a contrary indicator, you should be suspicious, as it's paid for by the pro money - their goal is to take your money, so avoid listening to it, in my opinion. Listen to the charts, the time & sales, the breakouts and gaps - that's what you need to pay attention to.
- You may find that you did better at your old trading style, that's fine too - the main thing is to keep an open mind and attitude towards your trading from a learning perspective - you should always be trying and testing new trading methods to develop a style that works for you personally most of the time for the short list of stocks that you like to play.

- **How to Make a Living by Swing Trading Stocks: a Professional Traders' Advice**

● **Main Points:**

- Eventually, you may get to a point where you wish to trade stocks professionally, for a living.
- As with any career change, becoming a trader takes a lot of training & education, practice and commitment. It is not easy.
- This lesson gives you a step-by-step plan for making a transition into trading as a career. It is recommended that you establish your trading skills as a swing trader prior to moving to day trading, particularly if you wish to make a career change. It's like becoming a race car driver by starting with a sports car before jumping into a pro racecar on the circuit.
- Those who are impulsive and unskilled will lose their money to those who have a trade plan that is skillfully and professionally executed. The difference between "playing the market like a gambler for fun" (and mostly losing over time) versus trading professionally requires your hard work and disciplined trading skills, executed without emotions, since it is your business that you use to pay the rent and support your family. Those of us who trade for a living honestly look at it as our livelihood - we cannot afford to trade ignorantly, foolishly, in an uninformed manner. Learning professional technical analysis and trade/risk management skills is critical. Being deadly serious about our trades is what gives us the ability to succeed where others fail.
- In transitioning to trading as a career, you'll want to start by mapping out a timeline for each phase of the change. This should be a 24-month calendar outlining your goals and expectations for each quarters' (3 months) progress.
- No, you can't become a professional trader in 6 months. Any career change, including trading, requires a thoughtful plan with resources, timing and milestones. If you were to change into any other career, how long would you expect it to take? Probably at least a year or two, right? Trading is no different. In fact, it is much more difficult than other career choices.
- Based on conversations with hundreds of traders, I can tell you that most are woefully underprepared to be trading with real money.  
**For example:** Are you still using a 56K internet connection? Do you want to race against my Formula 1 with your hyundai? I hope not (well at least for daytrading...you can swing trade with aol/datek I suppose). How many trading books do you read per month? You should be reading at least 3-4 books per month, just like a college degree program. What's your net P&L average per trade? What's your average stop loss over your last 10 trades? Your average profit? I hope you are keeping track of this. It's your businesses' profit and loss/balance sheet.
- Why do most traders fail? They are not serious businesspeople who expect to make a living at it. They treat it like gambling and guessing. I hope all the things we've covered in these 4 modules gives you some insight into the discipline and hard work it takes to trade. Money is not free - you must earn it, particularly in the markets. I get frustrated at the amateurish expectations of traders who want to "win money" without work. This is a serious, deep game that takes a lot of skill and time to get good at. Anyone who tells you differently is trying to sell you something. lol.
- Let's take a look at a transition plan I've put together to help give you some specific, actionable ideas for how you might want to approach making a transition into trading for a living. Sure, it can be done. Expect it to take a couple of years. No big deal, if you want to do it, then get serious and Do It.

There are 10 major phases that I'd recommend you consider planning for when making the transition to professional trading. If you were working as a floor broker at one of the major firms they would have a similar process, with the significant added benefit of having on-the-job mentors and training to help you and correct your errors.

These steps should take roughly two years to progress through:

- **Phase One - MARKET BASICS:** Trading Education & Financial Market Awareness
- **Phase Two - METRICS:** Learn all the financial measures related to trading (dozens of metrics)
- **Phase Three - PRICE PATTERNS:** Learning Technical Analysis of Charts
- **Phase Four - TRADING SKILLS:** Order entry types, managing trades, risk management
- **Phase Five - PAPERTRADING:** Using a trading plan to simulate trades, build skills
- **Phase Six - LIVE SWING TRADING:** Limited-risk live swing trades, 1-5 stocks at a time.
- **Phase Seven - INITIAL EVALUATION:** Use of metrics to assess progress in trading to date

- **Phase Eight - START-UP BUSINESS PLAN DEVELOPMENT:** After the education and initial (pilot) trading has been done, it's time to develop a business plan w/capital reqmts & goals
- **Phase Nine - CONSISTENT TRADE IMPLEMENTATION:** Make a defined number of trades each week, using metrics and trading skills developed to date for a six-month period
- **Phase Ten - QUITTING YOUR DAY JOB:** If and when you can consistently trade profitably for at least six months of part-time trading, you can make a choice to leave your 'day job'. Since you will have developed a healthy egg nest (at least 4-6 months' living expenses) from your six months' part time successful trading at this point, you will be ready to trade full time at this point.

Yes, this is the degree of detail and work that's needed to even consider trading for a living. It's not a "I got lucky in a bull market gambling for a couple months let me go trade fulltime now" type of thing. I hope some of you will consider putting the detailed workplan into place that's needed to trade the markets professionally. I never said it would be easy, did I?

For each phase, you need to allocate resources and timing, along with developing specific measurable goals.

DTU's "ROADMAP TO TRADING FOR A LIVING" (c) 2000:

### Market Basics

Understanding how the markets work is useful for your trading. A good example is arbitrage plays, eg when a company buys another company (eg if WMT buys KM), then the acquiring company's stock will decrease due to lower earnings in the following quarter due to acquisition costs etc. Many people do not know the difference between the various market indexes and futures, even though you need to know this stuff. A good overview of the fundamentals is needed to help you understand financial forces at work, and how to profit from them. It's not the most important thing for short-term traders to know, but it should not be overlooked. It's one of the prerequisites to do well in your trading.



### Metrics

To be able to trade for a living, you must develop a detailed plan with key measures, or metrics, attached to each step in the process. These measures include your personal trading outcomes, eg profit and loss, stops, average profit per trade etc., as well as market measures that are important, such as 52 week hi/lows, the float for specific stocks, option overhang, volume patterns, fibo numbers and other TA-related metrics, fair value and the impact on opening buying vs selling etc etc. These metrics are core to your understanding of the market, don't trade without knowing key financial metrics & their impact on short-term trades.

### Price Patterns

Pattern recognition is probably the single most important skill to learn in short-term trades. By this, I mean both chart patterns, market patterns, time&sales and level 2 patterns and more. You are buying and selling peoples' reactions and beliefs in the market, you're playing people, so you need to know the 'crowd psychology' as reflected in patterns that you see. Learning price and momentum patterns, pullbacks, average trading ranges, time-of-day effects and other market patterns will help you spot high-potential trading opportunities that you should be involved in. Technical analysis is important, I do not use all of the indicators, but knowing several key ones well helps.



### Trading Skills

You must remember that your goal is to become a good trader. What is a trader? Someone who buys at one price and sells at a more favorable price, pocketing a profit. Take some time to think about what this means, other than 'buy low sell high'...there's more to it than that. A trader knows bluffs, when to hold and fold, and more. In stock trading, we need to master how to use different order entry types, how to manage trades, handle risks and run our trading like any successful business.

### Papertrading

The next step in your development as a professional trader involves practice trading, called paper trading. This is not enough - you don't get the emotions of real trading with paper trades, so instead use time papertrading to mostly learn how you would take small stops. This is the most important skill you need as a trader, in addition to technical analysis and stock pattern recognition. An extension of this is to trade with very small shares (50-100 shares at a time) to get a feel for how to enter and exit trades. Papertrading is a useful activity, to help you figure out how you would trade without risking capital. Its use is limited, though, since it misses much of the excitement and genuine trading reactions you get from real trading.



### Live Swing Trading

After papertrading, you'll want to do some live swing trading, again with small shares in relatively inexpensive stocks, from \$15-\$50/share. Avoid cheap stocks, under \$15, and the expensive ones for now. Live swing trading should be done for around three months, with an average of 3-5 trades per week, to get the initial experience you need to begin considering trading for a living. This is all preparatory activity, by the way.

### Initial Evaluation

After live trading (and after your initial papertrades too, for that matter), you need to evaluate your trading progress. Did you a) make money or b) lose money? That's the bottom line. Also evaluate your trade skills, such as risk management, percentage of stops and profits taken correctly, and other measures. At this point, if you are not making at least 20% return on investment in 3 months of trading you should go back to the first steps and repeat. Do not progress past this point until you are at least 20% ROI in 3 months. Example: you started with \$20K on July 1st live swing trading, it's now Oct. 1, you should have at least \$24K.



### Business Plan

At this point, with some consistent trade skills under your belt, you're ready to start looking at trading like a business. You will now put together a business plan like any business would, except instead of marketing, labor and other costs you have costs such as training and education (books/videos etc), high-speed internet access, higher commissions for direct access brokers (if you're daytrading), equipment such as multiple monitors and a fast PC, perhaps a larger apartment or house so you can dedicate a room to trading, etc. Your business plan must include start-up costs, metrics for profit and loss expectations, and other areas as applicable. Developing a written business plan for your trading will help you treat it like a business. Keep the plan visible in your work area once it's been developed. Especially the measures.

### Consistent Trade Implementation

Your goal in becoming a professional trader is to make consistent profits. That's it. Homerun trades and favorable gaps are nice, but professionals make their money by shorting, playing long, and all the other trading skills that are available out there to get favorable prices. Your goal at this point should be to make consistent profits in your swing trades while still maintaining a primary occupation for a six month time period. If you can earn 40% in 6 months on your capital by swing trading (and not just in a bull market either!), then you may be prepared to trade for a living. You alone must make the decision and accept the responsibility involved in such a major life event. If you can trade "pretty well most of the time, and lose only a little when you lose", and you feel that you want to do this 5 days a week for years, then you may be ready to trade. Or, you may stay part-time - the choice is yours.



### Quitting Your Day Job

With corporate downsizings and mergers, personnel problems and office politics always a threat, it seems that at least being able to take care of yourself financially if you have to is an important skill to develop. Let's say that you have an "okay" job but you're making more trading stocks, and you have been for the last 6 months, in a choppy market (like the first half of 2000). If you feel ready, then you may be able to resign from your full-time current job to trade for a living.

Any major decision requires careful thought, I'd encourage you to prove to yourself and your family that you can make a consistent living at trading before giving up a steady paycheck. And, you need to ask yourself if you can work by yourself...that is my biggest personal challenge, I am used to being a trainer and consultant and like people. The financial freedom to live where you want and to spend more time with your family is great, though...it is true that "nobody ever got rich working for someone else" and if you remember the amway and tony robbins presentations there's a lot of truth to that. Being financially self-secure is still hard work, but of a different nature. You do get more freedom and resources, but a lot more responsibility. The best parallel is running your own small business - if you've ever been a small business owner you know the hours and dedication that's needed, trading is the same, but probably more difficult.

I have been self-employed for over 5 years in Hawaii and am having the best time of my life. I miss my co-workers in my corporate life at Ford, Rockwell and McDonnell Douglas, (those staff meetings and coffee) but I enjoy the time with my family and the ability to travel and live in Hawaii much more.

I hope you find the results you are looking for in your trading and professional life, and that this page has given you some "food for thought" regarding trading lifestyles and independence.

**Worksheets**

**Module Four: Worksheet 1- Trading Sectors and Market Indexes: Swing Trading Big Patterns**



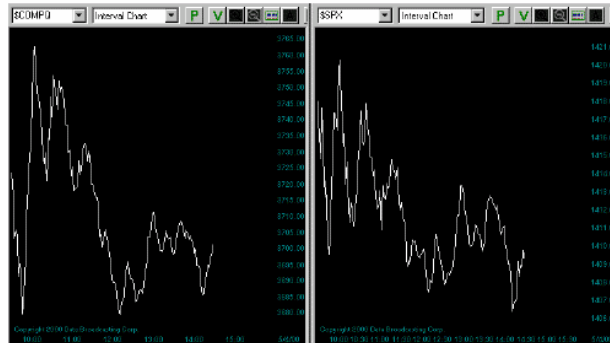
- The Powerpoint worksheet below can help you learn how to select and enter/exit stocks for Swing Trading based on Relative Sector Strength and Weakness using sector index charts
- You should complete this whenever you are considering entering a new Swing Trade position

An important thing to keep in mind is the **relative sector strength** of a group of stocks before buying or selling. For example, on one day the internet (\$GIN sector) may be up and the retailers (\$RLX) may be down. Use the relative strength to help you sell into strength and buy off of bottom bounces and into new breakout plays.

Look at these examples. The overall market has sold off a bit and is consolidating, as you can tell from the black charts to the right. \$COMPQ-Nasdaq Composite and \$SPX S&P.

Now, look at the bottom three sector green charts below, \$GIN - Internet, \$RLX, Retailers, \$IXBT, Biotech. Which of these three is the strongest? (\$IXBT) Which is weakest? (\$RLX).

How do you trade them? Well, I'd look for strength in a biotech stock (eg MLNM HGSI DNA GENE) to see if there's any more momentum left. I wouldn't be trading internet or retailers today.



**You should use this worksheet (or a similar one you make yourself) to help you map out a game plan to enter and/or exit swing trades based on relative sector strength.**

**Directions:**

1. Print out a copy of the worksheet below and fill it out for 3 different sectors you want to trade. A good first activity would be to go research and find all the sector indexes, then 2-3 stocks within each sector that you are interested in trading.
2. Use this worksheet to help you identify relative strength patterns and when you should enter/exit your positions:

## Swing Trading Major Sectors Worksheet

Goal: Be able to capitalize on different sector strength

### Step One: Identify Three Sectors You Want to Play

In the space below, take a minute to define three sectors (eg internet, semis, retailers, telecom, software etc) that you will be playing stocks within. Write down the symbol of each sector so you can track it on your charts (note: there's a link to a listing of all indexes on the members home page):

SECTOR	Symbol:	SECTOR	Symbol:	SECTOR	Symbol:
<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>

Now, identify 2-5 stocks within each sector that you will keep an eye on each day for trading opportunities. Example, in the internet sector (symbol \$GIGI), you might want to watch AOL, YHOO, EBAY, DCLK, CMGI.

Stocks I will watch/trade in this sector (enter symbols):	Stocks I will watch/trade in this sector (enter symbols):	Stocks I will watch/trade in this sector (enter symbols):
<input type="text"/>	<input type="text"/>	<input type="text"/>

### Step Two: Play Relative Strength Patterns

Now that you've defined the sectors and stocks within each sector you want to play, make a check mark next to the type of pattern you will be watching for to help you enter your trade. Use a sheet like this one daily or weekly to help you map out a game plan for entries and exits. Remember to sell into strength when you have a decent profit, and to exit quickly when your stock loses a key support level.

Which of the three sectors is strongest Today? What's my play within this sector? (check one)

- Bottom Fish/Bounce
- In a Trading Range
- Buying Breakout

## Module Four

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### Worksheets

#### Module Four: Worksheet 2- 5-Day and 10-Day Swing Trading Patterns



- The Powerpoint worksheet below is designed to help you track and trade 5- and 10-day swing trading patterns more successfully.
- Complete it as either a 'papertrading' exercise or whenever you enter and exit actual trades.

One of the things I want to encourage you to develop is a mental "library of chart patterns" that you use to help figure out when to buy and sell stocks for swing trades. Once you've established that, you need to then keep track of which of these are more effective for you than others.

For example, you may be great at buying breakouts above trading ranges but not so good at correctly buying 'bottoms'. You need to trade at what you do a good job of, so use this worksheet to identify which trading patterns you're currently using and which ones you're good at.

You must stop trading chart patterns that you have mixed or unsuccessful results with. If you're bad at picking bottoms, then don't do it anymore, for instance (or do it less).

Go where you're getting the best results. It takes discipline to stop trading like you have in the past, but if it's costing you money then look at some alternative ways to trade...

Explore with new stocks, new strategies until you find something that works for you consistently. Each trader must develop their own style, based on their individual temperament and skills.





- **The Powerpoint worksheet below can help you learn how to decide when to buy a stock for a swing trade, to develop better timing skills.**
- **You should complete this worksheet when you are considering entering a new Swing Trade position.**
- **A previous worksheet helped you decide on sectors and type of play, this one will help you decide on number of shares to buy and the timeframe and profit target/stop loss you will plan for this swing trade.**

- One thing you need to get in the habit of doing regularly is to develop a trade plan prior to entering any trade. This should be brief, easy to use notes to yourself that you use to help you define the parameters of your trades.
- For some reason, having things written down in front of me always gives me a lot more discipline to keep stops and take decent profits than I would have if I were just trying to keep everything in my memory.
- Also, if you are playing several stocks at once (I currently have 14 open swing positions, for example), it becomes next to impossible to keep everything straight from memory alone.
- A few well-placed notes, whether done on a spreadsheet or the simple Windows notepad.exe (my favorite, just put a shortcut to notepad.exe on your desktop), can significantly help your trading results.
- Gaining a good sense of timing is a key trading skill. I'd encourage anyone who's new to trading, or those trying to get back in the game after losing, to swing trade 100 shares at a time for a 2-day to 10-day timeframe. In fact, I think everyone should have at least one active swing trade open at all times, so you know the emotions of being 'in a trade'. Also, I'd discourage people to do short swing trades until after you're experienced and consistent in your trading.

**You should use this worksheet (or a similar one you make yourself) to help you develop specific trade entry timing information for swing trades.**

**Directions:**

- 1. Print out a copy of the worksheet below and use it to help you define better timing for your swing trades.**
2. You can also use this worksheet for your day trades, adjusting the timing down to intraday periods vs days.



## Swing Trading Timing Worksheet

Goal: Be able to improve your timing for swing trade entries and exits

Complete this worksheet for each new position you are swing trading.

<p>Stock Symbol:</p>	Trading Range Analysis:		Stop Loss and Profit Target:
<p>Time "Stop Loss": How long will you wait (max) before selling this stock if it has not reached your profit target? (rec. = 3 wks)</p>	10-Day High for this stock:	3-month High for this stock:	Profit target right under previous high is:
	10-Day Low for this stock:	3-month Low for this stock:	Stop Loss right under previous low is:

### TIMING SWING TRADE IMPROVEMENT PLAN

Let's put together a plan to improve our timing for our swing trades. Below are the different factors you want to define prior to getting into a swing trade:

**Main factors:**

- Min/Max Time in Trade
- # Shares Traded
- Profit/Loss Per Trade
- Optimum Trade Entry
- Optimum Trade Exit

**Timing Entries:** Should be based on one of the 3 patterns we've looked at. For each of your next 3 trades, identify what the reason was, from a timing perspective, for you to enter the trade at the time you did:

- 
- 
- 

**Timing Exits:** Should be based on the stock taking out a trailing stop that you've placed on the trade, or the stock has stopped advancing in the time period you're trading (eg it went from 20 1/2 to 23 and has stayed flat for 3 days). Identify why you exited your next 3 trades in the space below:

- 
- 
- 

**Module Four**

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**Worksheets**

Module Four: Worksheet 4- Portfolio Management: Balancing Your Swing Positions



- The Powerpoint worksheet below is designed to help you balance multiple open swing trade positions.
- You should complete this worksheet when you are considering maintaining several open swing trades at a time.
- After trading for awhile, you will see multiple swing trade opportunities present themselves. You will not want to limit yourself to single trades at this point, and will want to manage a small portfolio of open swing trades simultaneously, as your capital and experience grow.
- Note that this is different from the bad habit of keeping a "dog pound" of losing trades that tie up capital and energy. Make sure to have 'time stops' on all your trades and exit positions that aren't performing within a reasonable time frame.
- You can (and should) eventually use a combined trading style in which you have a percentage of your portfolio in low-risk long term growth mutual funds/index funds, a percentage allocated to swing trading, and a percentage allocated for day trading.



Activities

Module Four: Activity 1 - "Swing Trading Research: Picking 12 Stocks for Swing Trades"



- This activity is designed to help you research and choose 12 stocks that you think would be good for swing trading.
- Refer to [Module 4 Lesson 4](#) first.
- Papertrade a portfolio of swing trade stocks, identifying the entry, exit, trading range, shares you would trade, and stops.

The GOAL for this activity is for you to be able to wisely choose 12 stocks that make for good swing trading candidates.

**Directions:**

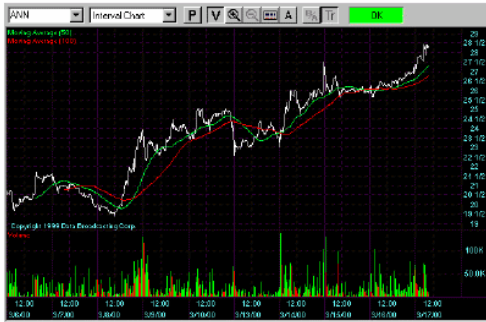
1. Take some time to do research on anywhere from 70-100 stocks and narrow the list down to a dozen or so that would be good for swing trading. I like stocks like WMT T F HRL HET VISX HAS ANN BBI and many others.
2. Include both Nasdaq as well as NYSE-listed stocks in your group. Remember, NYSE listed stocks are generally less volatile than Nasdaq stocks, and make for 'safer' swing trades, in general.
3. Make sure your stocks have decent analyst ratings (best ones are less 1.5 rated), maybe check IBD for 80/80 AAA type stocks as well.
4. Write down the following:
  - stock's 10-day support and resistance
  - type of trade it is (bottom fish, buy on breakout, uptrend, etc.)
  - how many shares you would buy (100-300)
  - how long you expect to be in the trade for
  - analysts rating for the stock
  - 2 reasons why you personally think you should buy the stock here

5. Now, papertrade these 12 stocks over the next 2 weeks and see how you'd do. Remember, you can easily be profitable even if you're only 50% right, as long as you manage your stops and exits correctly. Where you sell is more important than where you buy.

6. Choose one of the stocks that you should have had a "time stop" for...which one is it? Would you really have sold at this stop, or would you continue to hold on to it indefinitely "til it came back up"? Be honest. Work through these things to help yourself become a more skilled swing trader.

Hint: week of April 17th is probably a "bottom fishing" type week :)

Look at the 10-day charts below. Which of them would be good to buy here? Which would be good to sell? Remember, you want to trade with the trend and the crowd, if it "looks overbought" to you, others probably feel the same way, so it may be a good sell/short point.



Each chart could be traded profitably, somehow... the key is to know when to go long, when to short, when to cover and when to sell. We'll look more at technical analysis for swing trades soon.

## Module Four

## Swing Trading Strategies

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### Activities

#### Module Four: Activity 2 - "Bottom Fishing on Small Shares"



- This activity is designed to help you learn how to make "bottom fish" plays on reversals after a stock has consolidated in a low range, or on a pivot on an extreme oversold condition.
- Remember that "buying bottoms" is the most risky of all types of plays, and you must use small shares (100-200) and a tight stops (under the most recent bottom) to succeed using this trading style.
- I am never able to pick the exact bottom or sell the exact top, nobody is...remember, as a profitable trader all you want is a "piece of the action" in your direction, after you've identified a high-probability chart setup.
- Remember, if the stock loses the support level that you bought at and starts to head down, Never hold it overnight...sell it and buy again either the next day or when buyers come back into the stock, whichever occurs first. Overnight holds on downtrending stocks are asking for an opening gap down, which will be much more costly than the stop you had wanted to use. Only hold bottom fish plays overnight for a swing when the close of the day is higher than what you paid for the stock. Please Remember this and use Discipline for these plays.

**The GOAL for this activity is for you to learn how to bottom-fish swing trades relatively safely with minimum downside risk.**

**Directions:**

1. **Start by looking at several dozen 3-month charts for stocks that have sold off in recent weeks. Determine what the cause of the selling is:** was it due to bad earnings, bad news, or random sell pressure? Rarely should you buy a dip on bad earnings, they usually have further to fall (I speak from personal experience here!)... wait for a 2nd or 3rd bottom to form, then buyers to come in, before buying a stock that gaps down on the open on bad earnings news. Review recent headlines for a clue as to why people have been selling the stock.
2. Look for either a **reversal** (fast pivot off a >15% selloff) in the price and/or a **breakout above a consolidation** in price. That is, if the stock has sold off, has stayed flat for a few days or even weeks, and has now started to come back up through the resistance level.
3. **Do Not pick stocks that have been slowly selling off in a long downtrend**...the best bottom bounces are reversals off of volatile stocks...some examples include RIMM RNWK DCLK SPLS, you want volatility, stocks that have recently attracted both buyers and sellers, as seen by a choppy up and down trading pattern. Don't buy stocks whose 3-month chart looks like ETYS, for example (Jan-May 2000). No buyers have emerged, only steady selling...that's not bottom-fishing, that's called "throwing good money into a loser".
4. **Your activity here is to papertrade with 100-share lots of 12 stocks that you are choosing for "bottom fish" swing plays.** You only want to use 100 shares in this because of the risk involved in bottom fishing...if a position goes against you 2-3 points it won't damage your capital too bad...if you're trading 300-1000 shares and get a 2-point gap down that would cost you \$600 - \$2000...not a pretty picture. Your #1 goal is to preserve capital from the pros and other traders who want to take it from you.
5. Carefully identify and write down the following:
  - **The trading range:** 3-month and 5-day support and resistance levels for these stocks,
  - **Your entry price**
  - **Number of shares** you bought (100) for each trade
  - **Your stop loss** that you will hold to (the most important part of your trade), and
  - **Your profit target**, which should be right under the previous major resistance level.

**Notes:** Hold these papertrades no longer than 3 weeks, and evaluate your progress, using "paper money"...evaluate your trading record...when during the 3 weeks did you sell each of the positions? What profit or loss did you take on each of the 12 trades?

I find that holding yourself to a 3 week time frame is useful because it forces you to look for a good exit point, and to take a stop more effectively than if you are saying to yourself "well I'll just keep it til it comes back up, no matter how long it takes"... You need to put your capital to work for you, not tied up in an underperforming stock.

### Swing Traders' Keys to Bottom Fishing Success:

- 1) **Wait for a breakout above consolidation area/trading range**
- 2) **Look for pivot off extreme oversold conditions (>15% on the day)**
- 3) **Put your stop loss in right under the support/previous low**
- 4) **Use buying volume as an indicator as to "how right" you are on the long side**
- 5) **Never take home a losing first-day position, if it drops from where you bought on day 1 then take the stop and look for a better re-entry on a following day.**
- 6) **Don't chase a swing trade, look to enter before llam, or in the last hour of the day**
- 7) **Set your profit target right under a previous resistance level.**

Remember that swing trading is much more dependent on correct technical analysis than is daytrading, in which reading Time & Sales and your Level 2 chart are important.

Learning how to correctly identify breakouts, trends and support/resistance lines is critical to becoming a successful swing trader.

Candlestick charting also helps in swing trading TA.



**Module Four: Activity 3 - "Trading Breakouts and Uptrends"**

- This activity will help you practice entering and exiting swing trades when buying strength has caused the price to increase.
- As in any swing trade, knowing the key 10-day and 3- or 6-month support and resistance levels is helpful, as you can better determine when the stock will "look overbought" or "look oversold" to other traders. Using support/resistance with 20/50/200 MA lines helps in this as well.
- Also be sure to look for fluctuations in the volume of the stock over time, eg at what price points does the volume of the stock increase dramatically? Can you predict when the pivots/reversals are based on volume patterns?
- One of the important keys to success in swing trading is to properly identify support and resistance lines using your chart software, and being able to keep stops and exit with decent profits based on your careful analyses.
- Remember, the stock market seems largely random at times, so it's important to keep stops and take profits when they are there.

**The GOAL for this activity is for you to learn how to swing trade breakout patterns and uptrends effectively.**

**Directions:**

1. **Look at the chart patterns below, showing both uptrends (SPLS) and breakouts (VISX). How would you play these stocks from this moment on? Is there any trade potential left in either one?**
2. Scan your own 10-day stock charts and look for stocks that trade on decent volume (over 500K shares/day) with similar movement (eg at least 15-20% movement in the trend or breakout). Choose Five (5) of your own stocks to follow, and print out the charts, labeling them either Uptrend or Breakout, based on the pattern you see.
3. Next, draw trendlines, support and resistance levels for these stock charts using a ruler.
4. How would you trade each of them from this point forward? For each of your charts, identify the following:
  - **Major and minor support levels**
  - **Major and minor resistance levels**
  - **An optimal entry point for each of the stocks: would you wait for a pullback or buy sooner?**
  - **Where a stop loss should be set if the trade were to be entered on the next trading day.**
  - **Where your profit would be taken - what's your exit target?**
  - **Other notes that you want to make.**

This activity should help you develop an eye for uptrends and breakout patterns.

Papertrade the stocks for the next 10 days, using just 100-share lots, and see which of them would be winning vs losing trades.

Be sure to document your money management practices for these stocks as well, eg where would you have taken a stop loss, and where would you take profits, for each of your 10 stocks?

At the end of the 10 days, calculate your net profit/loss, and jot down your 'lessons learned' - what would you do differently next time? What did you do effectively?

### Uptrend patterns: SPLS

You can see that SPLS made a cup and handle pattern from 6/5 through 6/8, with a breakout and subsequent uptrend starting on 6/9.

The trade entry would be on the breakout, at 15 1/2, on 6/9, and using trailing stops throughout the uptrend pattern.

We look to exit the position right under decade resistance at 20, so we take some profit here in the 18s, and use a trailing stop at 18 for the rest of the position.



### Breakout pattern: VISX

Here, you can see that the stock was in a choppy trading range for several days, finally breaking out above resistance at 22 1/2.

The trade entry would be at 22 1/2, with a stop at 22.

The exit would be right under 'decade' resistance, or 30. This stock could be just an overnight hold, or could be held for additional longer-term gains.



**Activities****Module Four: Activity 4 - "Playing Positive News and Earning Release Trades"**

- This activity will help you practice entering and exiting swing trades in response to favorable and negative news and earnings reports that are made public
- As in daytrading, you wouldn't, for example, buy an open gap up on positive earnings or news, a good recent example is CSCO, it gapped up and sold off on positive earnings recently.
- In swing trading, our goal is to enter at a favorable price in a trend, a channel, or an 'oversold' condition, selling to buyers who entered later than you did, for a profit, several days or weeks later
- We'll have you practice swing papertrading both earnings and news plays in this activity.
- In general, stocks tend to selloff after earnings releases more often than they gap up, so I never hold overnight into an earnings release.
- Unless you have a realtime news feed and can jump on a news-release related trade within 1/2 point of the news release, do not chase it, a good example is XING in the week of August 28th, it ran from 12 to 23 then back down to 14 the next day...
- It's tough to play positive news releases unless (and it's a perfectly valid trade method too, by the way), you keep a realtime news ticker open and buy a stock within a minute (or less) of a favorable story breaking the news wires. You need to buy a realtime news feed for this
- Buyers haven't been coming in to scoop up oversold stocks as much this year, so dead cat bounce plays are tougher, again wait for volume buying signals before entering a trade off the bottom (or what you think is a bottom).
- In earnings releases, you should look to sell open gaps up and buy gaps down, again though this needs to be done with a finely-tuned set of market indicators (eg stochastics, RSI etc) for the intraday charts you're using, don't attempt these trades if you don't have a professional rig set up (eg 2 monitors, L2, time&sales 1 to 3-minute intraday charts on esignal or RTIII etc)...Why? Because you'd be trading at a disadvantage, against those of us who invest in those toolsets.
- Also in this category are **Upgrades and Downgrades**: a secret tip : look to buy stocks in the same sector that selloff in sympathy with a stock that's been downgraded, eg if you're playing the retail sector and YHOO gets 2 downgrades, the whole sector may take a hit, buy one of the other (good) stocks in the sector (eg EBAY) that also gets taken down that day... the downgrade had the effect of "throwing out the baby with the bathwater", so you want to buy a quality stock that got sold off "in sympathy with" the stock that got downgraded (this is usually best for either a scalp daytrade or a swing trade, if the sympathy selloff is >5-7%).
- Papertrade a handful of these as well, it's easy to look at the day's winners/losers about 20 minutes into the trading day...or, look at the most active on ISLD premarket around 9am... see what the crowd's reaction is, in a trend, to the news that causes a stock to sell off before the open, are they buying yet, or still selling? Then prepare to trade:

**The GOAL for this activity is for you to learn how to successfully trade News and Earnings Release plays.**

**Directions - EARNINGS RELEASE PLAYS:**

1. **Look at an [earnings release calendar](#) (click link) to see what companies are releasing earnings in the next few days. Pick 3 that you're familiar with to watch.**
2. **Look at the 10-day and 6-month charts** for this stock a day or two before the release is due, using [bigcharts.com](#) You want to identify the same information as you usually do:
  - **Major and minor support levels**
  - **Major and minor resistance levels**
  - **Average intraday trading range (eg BVSX has a 2-point range)**

Papertrade the stocks into the earnings release - note that stocks will often run up (or down) in anticipation of earnings for 5-10 days prior to the actual release, at which time they often retrace to where they were at earlier (making new 52-week lows for bad earnings, or gapping up (seldom) on good earnings).



**Two type of earnings release trades to look for:** 1) **jump on the trend** going into the earnings release, eg AMZN is going to release earnings on September 30th, watch the stock price carefully from Sept. 21st to the 30th to look for a trend.... or 2) after the earnings release comes out, **buy a bounce if it tanks and then gets buyers** (eg AMZN is 42 prior to earnings release, they miss by a penny, it opens up the next day at 36 1/2... look to buy it if it breaks over 37 before lunchtime etc..)

3. Ok, now see how you do on playing the earnings release for several stocks, and document your lessons learned: which strategy would've been the right one? Did you play that one or the opposite one? Most importantly, how did you manage your risk and trade sizes throughout the trade? If you were wrong, did you get out fast vs. hope for a turnaround? ok

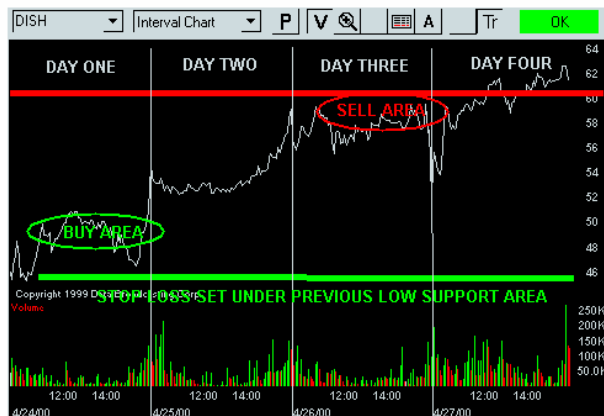
#### **Directions - NEWS PLAYS (little known trading tips in here, read it):**

1. Be careful with these, they are very difficult, they are more suited for daytrading than swing trading.
2. #1 Mistake to Avoid: Let's say SBUX announces that they've been chosen as a key supplier for a major retailers' coffee shops. They release this information Wednesday at 4:30 pm. The stock had been trading at 37... after hours it runs to 42. Thursday morning it has settled down to 41 to open. You do Not buy the gap up at 41. Dont do it. Wait til at least 10:15 or so to see if it still gets even more buyers... more likely, it would sell down to 40, consolidate around there for awhile, maybe go back up to 41 by the end of the day.... the only time you would buy a gap up is if it keeps running on good volume for at least 20 minutes or so early in the morning... usually the gap has "satisfied the buying urge" of the public and sellers/shorters will appear, selling into the momentum until the stock reverses at 10am... again these are general patterns.. but they happen more often than not. The point? Do not buy gaps up unless the stock takes out a new high on heavy volume...be careful with these.
3. How to play news: let's say you've got [www.theflyonthewall.com](http://www.theflyonthewall.com) or [www.jagnotes.com](http://www.jagnotes.com) or another service... and, most importantly, you've got a realtime news feed that gives you headline news releases throughout the trading day. Here's what to do:
4. The instant a headline comes out that has Major Financial Impact on a stocks' price (eg announced new strategic partnership, wins major contract, releases new product/service, has major drug/technology patent approved) then pull up your 1-minute chart and time and sales window. You do not yet know what impact this news will have on the share price. Much of the news that comes out has no effect on stock prices, you're waiting to cherry pick a headline that has a major financial impact on a company.
5. Buy the stock as soon as it makes a new High for the day after the earnings release. Why wait? Because what you think is good news may, for other reasons, be seen as a negative by the analysts following the stock, who will issue sell program orders, selling the stock off... so, wait to make the buyers prove to you that there's buying interest in the stock.
6. For shorting, almost the opposite is true... if you see a "Firetire Recall" news headline then you may be able to get a short off... because of the uptick rule, however, it's much more difficult to get a short sale off for bad news, the stock price will plummet, so short sellers need to respond immediately to negative news headlines and fire off a short as soon as possible (eg within 15-30 seconds after the news hits the wire), you can't wait for a new low of day, since you may not get an uptick to short on... you might, it's just not as easy.
7. Okay, papertrade the news releases with your realtime news feed too. Are you a swing trader? That's why you're reading this, right? Well, news releases can still be played profitably from a swing trading perspective, the key to look for "unresponded to" news... eg if theres a release that has genuinely positive financial impact on a company, but for some reason the stock hasn't gone up, you might want to buy into it and see if it goes up during the next 10 trading days or so. I've personally seen many stocks, usually the cheap ones (eg \$10-\$20) that aren't heavily traded, pop up 2-3 days after the news has come out. They aren't as closely watched, so the fund managers who pour money into the stocks may take a couple of days to decide to buy in. This is a good buy opportunity, before the big money comes in. Of course, if the news comes out and the stock is still flat 2 weeks later, then sell and move on.

Activities

**Module Four: Activity 5 - "Scaling In and Out of Your Swing Trade Positions"**

- This activity will help you practice adding to and selling off positions you have in a single stock.
- It's wise to use what might be called a size scaling approach to manage your swing trades. You initiate a position with a certain number of shares, then add to (or subtract from/sell) the position based on profits you're taking and major swing support and resistance levels.
- A good guideline is: add to winning positions, not to losing positions (eg don't average down, or do so only for stocks that keep price support off a bottom of a well-defined 1-2 month trading range)
- Also, a 'reverse pyramid' as previously mentioned is a good strategy, eg buy 500 shares DELL at 32, add another 300 at 34 and a final 200 at 35 1/2.... sell 500 at 37, sell 300 at 36 3/4, sell the final 200 at 35 7/8 on the way back down as it sells etc... like a rollercoaster, you want to add the most weight to your position at what you think the bottom is, then add a bit more as it keeps going up, then sell out a major piece with a good profit as the "trade potential" decreases and selling is more likely, then fade out the rest of your position on the way down, locking in profits.
- This technique is useful, I've added and subtracted as few as 50-100 shares at a time (for expensive stocks eg PHCM)... to manage your risk and "hedge" as the price moves for or against your position. It does generate more commissions, but that's generally insignificant... you shouldn't be constantly churning your swing trades, eg 1-2 buys or sells per day per stock at most... usually I'll buy a position, maybe add to it if it gets over a key breakout area, put a trailing stop at the breakout point, sell some of the initial position if it looks like it's teetering on the edge of selling off, etc...
- Some of the types of stocks that are ok for swing trading are ROST BBI SCCC SPLS NOVL WMT T etc... ones with a fairly steady trading range that you can get in and out of relatively safely... remember you probably should trade slower-moving stocks for swing trades if you're a newer trader, don't swing trade an EXDS ISLD etc unless you're experienced in risk and trade management.
- Take a look at this chart below, which you saw earlier in [Module 4 Lesson 6](#). How would you do a "scaled position swing trade" in this stock, DISH? (eg buy 500 DISH at 46 1/2.... then what ...??)



The GOAL for this Next activity is for you to learn how to successfully Scale in and Out of swing trading positions during a 1- to 3 week time horizon.

Directions - Papertrading a SCALED-IN/SCALED-OUT SWING TRADE:

1. Choose a stock whose 10-day chart has at least a 10% trading range.... eg a \$50 stock with a \$5 range (it's traded in a range or trend from 48 to 53)..

2. Paper-trade how you would manage a trade entry and exit, varying the size of your position such that you enter the trade with the largest size, and add to it if the stock is going in your direction. Of course, you need to also identify where you would stop out, this should be the "fastest stop" you take in the position, as it is the largest position size you take, eg 300-500 shares, don't let it go more than 1/2 point against you... wait to rebuy later...
3. Ahead of time, identify where key support and resistance areas are, and at what price point and level you'd sell your stock out at... where will you sell the most shares? Where will you keep that last 100-200 to see if it retests a breakout point?
4. This takes a lot of practice, and is a very important skill to master. Many new traders, myself included at first, make their trades as "all-or-nothing" trades, eg I'll buy 500 shares and sell 500 shares. That's it. ... The better approach is to work like a market maker does, eg start with a 300-share position, add another 100 to it if it keeps going up, add a final 100 if it's making new highs, then sell 300 when the momentum starts to fade etc... this can be an extremely powerful swing and daytrading technique and I encourage everyone to learn to master it.

**A few more signals you should also be looking for when scaling in and out of a trade:**

- **Volume patterns:** keep a very very close eye on relative volume during a short term trend, either swing or daytrades... volume = voting... so, if you see a lot of selling volume, then you should also be a seller, quickly... if you see buying volume then don't chase, enter on a pullback if it looks right to you.
- **Earnings releases:** make sure in all swing trades that you are aware of when earnings will be released... I generally sell my positions off the day before earnings release and re-enter on a pullback (or tank) the morning after earnings are released, if volume reversal buying is apparent. There are occasional favorable gaps up on earnings releases, but I've found this does not occur nearly as often as a "why did it tank on good earnings" type play. I'd be more inclined to short into earnings releases than go long, particularly for stocks whose month over month earnings have been declining. (see [www.bigeasyinvestor.com](http://www.bigeasyinvestor.com) for summarized table of monthly earnings and share price / volume changes at the bottom of the "screen")
- **Market and Sector relative strength or weakness:** be sure to keep an eye on sector charts like \$GIN \$SOX \$RLX etc as well as the overall market to capitalize on strong or weak sectors, look at these charts in comparison with each other (and the "lead stocks" within each sector) as well as the specific stocks you are following.

- **Introduction to Shorting: DTU Short Trading Rules & Tips**

● **Main Points:**

- If you're like most traders, you're uncomfortable with the idea of shorting. Traditional stock investors are trained to think that "if I buy a stock and hold it long enough it'll surely go up". If you bought and held from the last few months of 1999 til now you're in the red.
- You may be reading this thinking to yourself, "well I'll read what he has to say but I probably won't ever short anything". Right?
- By the time you're done with this module, I hope you'll learn to recognize and see the profitable opportunities that are available to you by adding short selling to your arsenal of trading techniques.
- There is very little out there on shorting, only 1-2 books, an audio and a video. That's it. Yet professionals are always used to selling short. So should you. It's like "working an order the other way around". Uncomfortable at first, but it still works. I'll give you what you need to know.
- Here's an example (from my mgmt. training days): I want you to cross your arms, folded across your chest, right now as you're reading this. Go ahead. Ok, now unfold them and cross them the other way, putting your right forearm across your left one. It's uncomfortable, right? But, both ways are equally successful at keeping your arms folded on your chest. Change is uncomfortable for many, but necessary. Shorting is the same.
- If you've ever bought stock long on margin, you're doing the same thing a short seller does... borrowing something you don't have, with the intention of paying for it later.
- Shorting is for more experienced traders, eg at least 6 months to a year full-time experience, or 2 years + occasional swing trading experience.
- I will show you the best ways to short stocks in this module, using current examples, and information not available anywhere else.
- Take a look at our Short Trading Rules to Live By below, and memorize them if you plan on shorting. They should help you immensely, in learning how to trade the short side.
- Do not underestimate the value of shorting, or avoid it merely because it's not what you're used to. That's like not trying Chinese food because you've never eaten it before. Expand your menu of trading choices to include shorting as a common and viable way of trading.
- If you're wrong in a stock going long, consider not only stopping out but reversing your position into a short at the right time as well... same thing for winning long positions that are reversing, you can sell it out at a profit, then enter a short and ride it down to an intraday support level, covering to make another nice profit.
- Don't just ride the curve up, make money on the selling too... why not? Once you become more familiar with it, shorting is a handy way to make a lot of money. If you had shorted all the January tops you'd be much wealthier than losing buy-n-holders are, who are sitting in red positions waiting for a bounce. Right?

**Short Selling quick intro:**

**What is shorting?** Shorting is simply selling a stock first, then buying. You're borrowing the shares from your broker to sell to someone else at one price, in the expectation that the stock's price will decline from where you bought it. You then buy the stock on the open market later, so you can repay the broker the shares you borrowed from him.

**What's different about shorting?** We'll cover the "uptick rule" in the next lesson, basically it means you've got to enter your order (to sell) only when the stock's price has just had a positive transaction, eg the arrow in your stock minder shows a green up arrow, not a red down arrow. This means you may have to try to enter a short order several times to catch the uptick.

**Isn't shorting dangerous and risky?** The only risk is that if the stock price goes up there's a lot of possible risk if you can't keep a stop loss. A long trade of 100 RNWK bought at 41 means you have a \$4100 investment at stake, it could conceivably drop to zero, in which case you'd lose \$4100. If you shorted RNWK at 41 it could run to 210, and you'd owe your broker the difference, or  $(210-41=169)$  or \$16900. If you're not good about taking stops, then you shouldn't ever short. Or go long, for that matter. Taking stop losses is especially important in shorting.

## **DTU's SHORT SELLING 'RULES TO LIVE BY':**

### **Rule #1: Never hold short positions overnight**

Why this rule? Because I want to minimize your risk to upside overnight gaps. If good

news comes out, or the futures are way up, causing a lot of gaps up, your short could cost you a lot of money.

I recommend only intraday shorting, never ever "swing short" in my opinion. The risk:reward may not be as good. Of course, many traders do just fine with 1-2 week short positions, but it's not a trading style I'm comfortable with, I wouldn't be able to sleep, wondering if good news will cause my short to gap up against me the next morning.

Look at stocks like CIEN CNXT etc. with recent large gaps. Shorts would be in a bad position if they held shorts overnight.

The rule of "never take home a losing position" is especially true of shorts. If the stock goes out strong, it's likely to gap up or have a next strong day, so, don't take it home short. It just isn't worth the risk.

## **Rule #2: The best time to short is on an open gap up of over 8%**

We will cover this with many chart screensnaps and video clips in the later part of the module. Open gaps up are the best short candidates, just as open gaps down are the best long candidates, if it happens on strong volume and you see sellers begin to appear.

The larger the gap up is, the more likely a retracement back down will happen. Think about it, if you had a position in KLAC from 53 and it gapped up to 62, wouldn't you want to sell it on the open? Most other people would too, so this is an idea time to sell stock as well, shorting it, then covering at the fibonacci retracements, eg down 38% from the high, roughly a third down.

If you see a stock gap up over 40-50% (rare, but it happens), look to short it as well. This is one of the valuable parts of looking at the "Day's Gainers" lists early in the morning... even as late as 10:00... look for the stock to begin selling off into the gap up and fire off a short, using a stop at the previous high for the day.

## **Rule #3: The next best time to short is after a stock has lost a key support level and is making a new low for the day**

If a stock is in a technical downtrend, eg a series of lower lows and lower highs, you will want to short the next lower high after it's lost a key support level, particularly a decade number.

For example, if RNWK loses 40, you'd look to short at 39 3/4, with a cover stop loss at 40 1/4 or so. You'd have an exit target of 37-38 1/2.

This play is good for the first trading hour in the morning, as well as lunch and afternoon selling pressure. Look to short the second time a new low of day is hit. We'll show lots of annotated chart example in future lessons. Use a two-day chart here too, eg always look to short a new 2-day low, and buy a new 2-day high. Many professionals use this technique as well. I always use 2-day 3min candle, intraday 1-min stochastic, and 10day 15 min candle charts to trade.

**Always pay attention to the sector and broad market indexes: short stocks on weak days, buy stock on strong days. Do not fade (try to outguess a reversal in) the overall market trend! Buy strong stocks, sell/short weak stocks.**

## **Rule #4: Other good times to short are the 10am reversal of an uptrend and at 12:00 on lunch weakness**

**10am tops reversal shorts:** This is your chance to profit from the classic "gap and trap" play that market makers like to do. On stocks that put in a 10am high (that is Not a 2-day high), you may want to short it if it starts to get selling in a "microdowntrend". This one is a bit riskier, so be sure to put a cover stop loss at the immediate previous high.

**Lunch weakness shorts:** A slightly better time to short is when the market starts to drift downwards during the 11:30 to 1:30 slow lunchtime, since this is when many market makers like to bully stocks down so they can get a low of day price to sell back into afternoon buyers. So, shorting a stock that's making a new low of the day at around 12:00 is usually a good time to short.

### **Rule #5: It is too dangerous to try and "catch a rising knife" and short a momentum stock's top.**

Okay, yes up - how many of you have been cut trying to catch a bottom for a stock you think is going to bounce up? We've all done it. Shorting momentum stocks is the same exact thing, in reverse.

Do not ever, repeat ever! try to predict the top of a strong stock that has a lot of buyers in it. When demand exceeds supply, price goes up. It is difficult to nail the exact top of stocks that rise, say, 5-10% in 20 minutes on a hot news story.

This, unfortunately, is how many traders try to get started with shorting, and they get burned more often than they correctly guess the top. We want to use technical analysis, LII and other indicators to trade, not guessing.

Once you understand true market dynamics, you'll realize that you don't want to try and guess a top for a hot stock. You may get a short off on a wiggle, right before the stock explodes to a new high. Shorts are often "squeezed" here, as everyone rushes to cover their short positions. The market makers step off, and the price runs. These are good opportunities to get long, when a new high is made. Do not try to short momentum stocks unless you're very fast, have very tight scalping-type stops (eg 1/4 point absolute max, 1/8 better). An exception might be if the stock is up a ridiculous amount for the day, say over 80%. eg I nailed the XING top at +92%, but those are very rare times. 99% of the time you'll want to avoid shorting momentum runners.

### **Rule #6: Use a cover stop loss at the most recent intraday reversal price**

Let's say you short CSCO after it loses 60 support, making a new low for the day. You get the short off at 59 3/4. It wiggles up a bit to 59 7/8, drops down to 59 1/4, then runs back up to 60, then goes to 60 1/4 and beyond.

What's the proper way to have managed this trade? Your cover stop loss should be a bit over at the support level that the stock lost that caused you to enter the short in the first place. If you shorted because you think 60 was a key support level that was lost, and your reason for entering the trade is proved wrong, eg they take it back up over the 60, then you'd want to cover right over 60, at 60 1/4 max.

### **Rule #7: As with all daytrading stocks, make sure to only short stocks trading over 800K average daily volume. Check that your broker has stock available to short ahead of time.**

These should be common sense, but they're worth noting nonetheless. As with all intraday trading you, **volume is your insurance**, and helps you take your stops quickly and at a good price. Only trade stocks with an average daily volume of over 800,000 shares.

If you're trading a thin stock, you may not get filled til way past your stop, costing you more than you wanted to spend, in the event that you're wrong about the price direction.

A second note: check with your broker to make sure shares are available to short. You don't want to correctly identify where to short, then try to enter the order and get a "shares not available" message. Also note that all shorts are done in your margin account, and that stocks that are non-marginable are not shortable either (including under-\$5 stocks).

Okay, let's move on to some chart patterns and examples...

● **Main Points:**

- Shorting stocks that **have a large gap up** on the open on news are often profitable. You want to avoid shorting good earnings release gaps and buyout gaps though.
- You should look to short overreactions to news (eg gaps up over 15%) on high volume (eg over 30K shares premarket) within the first 10 minutes or so of the market open.
- The other way to short gaps is to short a stock that makes a **small gap down premarket and continues selling after the open**, eg 1/4-1/2 point, and loses a 2-day support level, making new lows. (eg ALTR closes at 48 3/4 near the low of the day, the next day's premarket trading at 48 1/4, it loses 47 3/4 on the open at 9:30, short it here with a cover stop at 48 and an exit target of 5/8 to 1 1/2 points etc.)
- As always, it's a good idea to place a close short cover stop loss right above the exact open price as well, in case buyers keep coming into the stock.
- In general, you want to see a bit of a downtrend on the gap occurs from where the stock was trading premarket. For example, if it closed at 36 1/2 the night before but gapped to 40 3/4 premarket the following day on news of a new contract being won, then sells down to 39 7/8 by the time the market opens at 9:30, you'd want to consider firing off a short on the open (using a cover stop loss at 40 1/8) and an exit target of roughly 1/3 the retracement, at 38 1/2.
- You can also short minor gaps down, as well as major gaps up, as follows:
- Let's say a stock closed at 28... near it's low of the day. Then the next day it gaps down a bit to 27 3/4. You might want to fire off a short at the market open (9:30-9:35) with a cover stop loss at 28 1/8. You might look to cover it near a 10-day support level, or, use a trailing cover stop about 1/4 behind where the stock is currently trading at.
- Do not short major gaps down on the open. They tend to attract buyers.
- You could short a major gap down stock if it's still selling off as of 10:15 am or so... just don't try to short big gap down stock... the "trade potential" is largely gone on the short side, as people who were short from earlier will probably look to cover their shorts (these are the "dead cat bounces" that you can scalp on the long side oftentimes).
- Take a minute to review [Mod1Lesson10](#) and the next lesson as well, [click here](#), for some basic gap info as well.
- Let's look at a few charts here to look at examples of shorting on the open. Again, don't short premarket... but, look for short opportunities within the first 5-10 minutes from 9:30-9:40, for these chart patterns below:

**How to Trade Open Shorts**

Here's a perfect example of an open short play, for a stock called GALT that gapped up over 30% premarket on Oct. 17th.

The 2-day chart to the right shows the stock closed at night over 30, and doesn't trade on much volume. After a positive news story came out, the stock gapped up to 43 premarket on high volume (over 100K shares had traded before 9:30am on 10/17).

**You do Not short stocks that gap up on good earnings**, in general, eg MSFT gapped up over 10% and kept going up after the open. Be selective, and first **"wait for the stock to lose a key support level before shorting it on the open"**. This is the most important thing to realize about open shorts. You do Not just short it because it's up 30%, it could run to +42% before topping. Let the chart tell you the story, short only after it loses a support level.

In our [Trading the Open](#) live trading room, I advised traders to **"Short GALT if it loses**



**40 support, say at 39 3/4** (exact quote). I advised them to cover around 36 or so (fibonacci retracement). This was a great trade! Hope this makes sense. 40 (decade number) is where I pegged support. It could have reversed above 36, so that's where we covered (it's ok that we didn't get the full range of the short, we're happy to take almost 4 sticks (points) on a \$40 stock!

Let's look at some more examples...

**Ebay had ran up to 60** and consolidated the day before here (Oct 17, 2000), right before the close. It ran up a bit more on the open here, consolidated a bit more for the first half hour, then lost 60 support (twice, a double bottom).

We would have been stopped out for a - 3/8 or so loss the first time, but on our re-short (2nd time it lost 60), we are in for a nice win as it dropped to 59, consolidated, and sold off down to 55, where we cover, for a + 4 3/4 win.

Note the key when we're wrong, if it "shakes us out", like it did the first time, is to keep the cover stop loss small, say 3/8 to 1/2 point max.

This example shows you about breakdowns below consolidation (choppy undecided) trading zones that last for 5-10 minutes before the trend is re-established one way or the other, on open gaps up.

	10:00	11:00
10/16/00	10/17/00	



**Here's Oct. 17th KLAC**, a semiconductor company - notice we could have got an open short off at 32 on the open, if we were fast... however I like to wait til it loses a key support level, my favorites are decade numbers since level 2 tends to get thicker there, as the market makers have a lot of stop buy and sell limit orders there from the public investors that they have to fill.

So, we see a bit of consolidation before the downwards march continues, we fire off our short right under 30, at 29 3/4 (with a cover stop at 30). We cover 1/2 the position at 29 (trailing stop at 29 1/2) and the balance at 27 1/2, for another 2 1/4 points win.

Remember, you can add to and sell off your positions in pieces, a common pro trading technique, eg short 400 at 29 3/4, cover 200 at 29, wait and cover the remaining 200 at 27 1/2. Your trades do not need to be "all or nothing", rather use dynamic position sizing depending on the price action to get the best overall trade. This is how market makers trade, you should try it out yourself as well.



### More Tips & Guidelines on How to Make Winning OPEN SHORT Trades:

**Keep these pro techniques in mind for playing open shorts:**



- Keep in mind the **reason** for the open short (why did they gap it up?). Be more cautious about shorting earnings plays than you are about shorting news-type plays.
- Always always keep **tight stops** on your shorts. Because of the effect of "**short squeezes**", eg shorts trying to cover in a panic if the price starts to go up, you need to be prepared to cover quickly. Never short without a DAT broker (don't daytrade w/o a DAT broker, for that matter). Cover with market buy orders (or SOES limit/ISLD).
- **The higher the open gap is, the more likely it is to attract sellers**, which makes for a better short play. **Don't short a stock that gaps up 3-5%**, for example (we look to play these on the long side, if they make a new 2-day high or are making a cup pattern). Watch your "daily % gainers" list and look to short stocks that are trading over 400K volume or so that have gapped up over 15-30%. If a stock has gapped up over 50% it will almost always attract sellers, so it's a matter of "when not if" to short it, if shares are available to short. Check with your broker ahead of time that morning to see if they have shares to short. **If your broker has a lousy (small) list of stocks that are available to short, switch brokers.**
- **Use Level II and Time & Sales to help time your entries for shorts more than for longs.** We are still chart-pattern based trading using technical analyses, of course, but because of the uptick rule and the dynamics involved in shorting you should pay **closer attention to level 2 support/resistance** for shorts than for longs. The t&s is more important of course, that's your navigation for the trade (the "tradewinds").
- **Use Fibonacci retracements to help you identify your targets for where you should cover** your open short trades. In the GALT example above, we don't expect more than 36 out of the trade since that's near a fibo line. Your open gaps up will almost never close the entire gap, I look to get out at 1/3 to 1/2 of the retracement range.

## Module Five

## Shorting Skills for Active Traders:

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Time of day patterns for best short selling: finding the best trading opportunities

Back to  
MODULE 5

### ● Main Points:

- Becoming successful at timing your trades is important to your success.
- In this lesson, we will look at some of the time of day patterns that you should be aware of to short stocks effectively.
- By gaining familiarity with the time-of-day patterns that set themselves up for good short opportunities, you can become more effective in "timing your trades" to be in sync with the professional money flow.
- Remember to keep an eye on the broad market indicators as always, an eye on the Nasdaq TRIN, the COMPQ, and your sector charts, to confirm the reversals and time-of-day pivots as they occur in the market each day.
- In time, you will hopefully become more practiced, more "on time" with the market's many pivots and become better able to navigate the directional changes as they occur.
- Your primary goal by the time you complete this lesson is to be able to a) anticipate time of day patterns that yield profitable short trades b) be able to recognize these time-based pivots and reversals when they occur and c) be able to execute short trades more successfully as a result of now "knowing what to look for" in your short trades.
- Remember that timing takes much practice, and is both difficult to learn and time-consuming to practice. This is why market-watching a core basket of 5-8 key stocks for weeks, months on end, during at least the first 2 hours of each trading day, is so critical to your development as a trader.
- As a new trader, I used to enter trades late, still looking for good movement after the first, most powerful move, had been made. In time, I learned to jump on the first move more consistently and accurately. This takes a lot of time to develop; the more 1-minute charts you watch, the better you should get at this crucial trading skill.
- Each trading day is a mini-world in itself, you need to not apply blanket rules or your expectations to any one day, rather, you need to be flexible and trade "what the market is telling you" for each separate session.

- Paper trading, or trading 100-share trades, for many months, is a great way to learn the intricacies of trading without exposing your capital to much risk. This is a good way to learn shorting, by paper shorting at least 6 months initially before doing live trades.
- Let's take a look at some of the timing patterns I've discovered that help uncover what should become consistent, profitable trading opportunities.

## Time of Day Patterns for Shorting Nasdaq Stocks

Here's a brief summary, we will illustrate all of these with recent chart patterns, from Feb 2001, below:

**EARLY PLAYS:** We've already discussed the "short an open gap up" when there's a bear cup reversal that you can see premarket. The other early play is a bear cup reversal occurring after the open.

**LUNCH PLAYS:** Market makers often take a lunch break (hey, they're only human too, contrary to popular perception :). And stocks often drift down from 11:30 til 12:45 or so. Leisurely shorts can often be entered in this time frame as well.

**LATE SESSION PLAYS:** Although I rarely or never play the afternoon session, you can look for short opportunities late in the trading day on days where a) the compq is making new 2-day lows after 2pm or b) the market has run up considerably until 3pm, and profit-taking is happening.

### Bear Cup Breakdowns on the Open:

In shorting bear cups right after 9:30, as with open gaps up, you look for an arch, eg the stock gets buyers on the open at 9:30, goes up to meet resistance, and starts to fall. The key is, you don't guess at the top, you wait til it makes a new low of the day, and short under the breakdown.

These are best if they are making a new 2-day low as well (in this example, let's say ORCL traded 30-31 1/2 on the previous day... today, it opened at 29 3/4 on the open, traded to 30 decade resistance, then sold off again, the short is at 29 5/8.

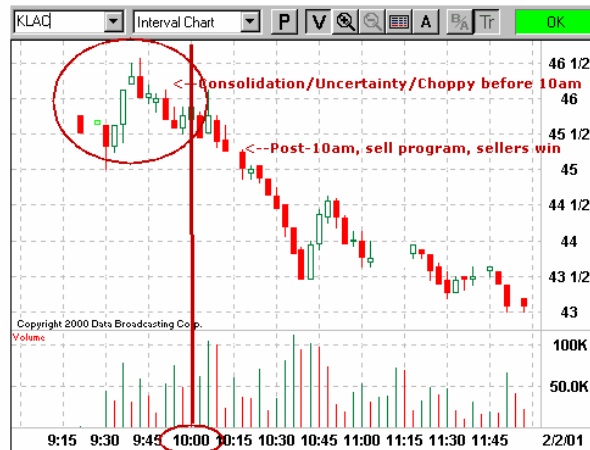


### Patterns for 10am Shorts:

Sometimes a stock will chop around til around 10am, at which time it makes a breakout to the downside (or upside).

For shorts, we can look to 10am as a good time; often the traders in a stock will decide whether to bid it up or sell it off at around 10am.

This is a good time to look for short entries, at right before 10am, to prepare to short a breakdown.



As you can see from this example, the stock broke down early at 9:50 or so, then got a 10am bounce, before continuing down.

This illustrates the need to always keep tight stop losses; eg if we short at 29 5/8 or so, and it drops to 29 3/4 then starts to bounce, we cover soon with a small 1/2 point profit or so, we don't wait for the stock to go back up to our original short entry point.

In the current market, trading wins over 5/8 point on \$20-\$60 stocks are fine to take, they are the "base hits" that are our bread and butter... of course the home run + 1 1/4 type trades are great to get as well.



### Shorting Lunch Weakness with the mms:

Oftentimes it is good to look to enter new short positions from around 11:30 or noon until 1pm or later, as stocks will often drift downwards over the lunch hour, until the mms return from lunch and volume/volatility returns to the market. These are longer daytrades, usually taking 15 minutes to an hour or more to complete round trip.

Here's a perfect short example: AMAT is stairstepping down in a classic downtrend: lower lows and lower highs throughout the morning.



### Late Session End of Day Shorts:

Finally, we can look at late end-of-day selling. There's two time zones to be aware of, one is from 2-3:30 or so, the other is during the close, from 3:30 til 4pm.

The best is to look for bear cup breakdowns during 2-3:30, as selling continues.

Often you'll see some volatility at 3pm when the bond market closes; also, you may see end of day tanking Or short covering, so, careful holding any short positions post-3:30pm.



## Module Five

### Shorting Skills for Active Traders:

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- Premarket indications for shorting opportunities: chart patterns, news/earning

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MODULE 5

#### ● Main Points:

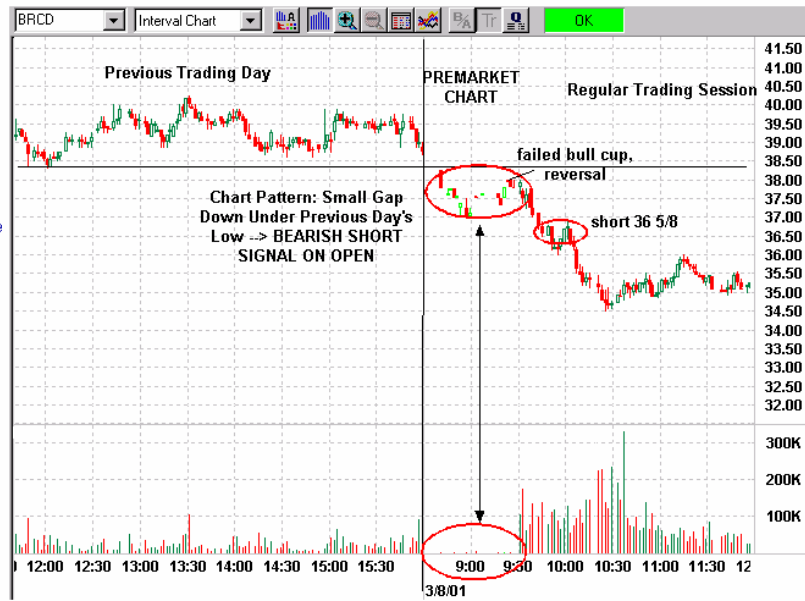
- We've already discussed how to look for large premarket gaps up, over 8-15%, that are getting selling on the open (bear cups) as being the best short opportunity. Now let's look at a few more.
- Premarket activity is a good leading indicator about the overall strength/weakness of a stock when the gap activity is less than 5%.
- I've pulled together a handful of example charts for this lesson to help you see how to use premarket charting to correctly identify short candidates.
- You need to have a charting software data feed service (like esignal.com :) that has premarket chart ability in order to daytrade effectively. There's no reason to be "blind" each morning in the premarket, when you can have charts to help you see double tops, cup breakouts and reversals.
- We do not ever enter new positions in the premarket. This is because our volume is very low. Speaking of volume, you only want to screen for stocks that have over 20-30K minimum volume by around 9:10 am. If a stock has gapped up a lot or down on just 12-15K volume, for instance, you don't want to touch it - yet.
- We are looking for continuations & reversals on the open from premarket chart patterns. The stock will do one of three things: stay flat, go up, or go down, right? We want to see if there's significant movement up or down through a good technical entry point.
- I tend to like to short stocks that are making new 2-day lows at around 5/8 below the whole number that was the previous low/support level. You will see this in the charts below.
- Charts let you see the impact of news, earnings releases, and anything else, so we use chart patterns to trade with. We do not guess at what news/earnings will mean for the price of the stock - ever. If we did that, we'd be investors. (perish the thought!)

## Small Premarket Gap Down Under Previous Day's Low

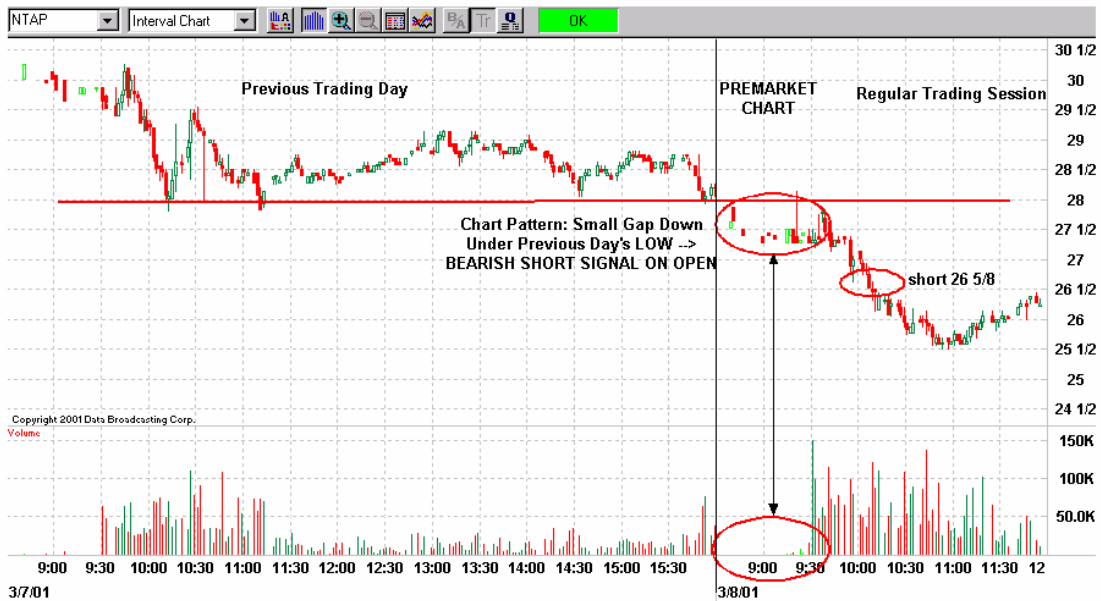
Here's a good example of a premarket double top failure in BRCD that continues on down.

Note that we do not short on the open, we instead wait for the premarket pattern to make a new low, and enter the short at 36 5/8.

This is a classic "short the 2-day low breakdown" after a weak opening in the stock.



Below in NTAP - what do you see? I always draw the technical low/high/2-day lines to help you see what I'm looking at as well. In NTAP we see support at 28 in the previous trading day, a weak open with a small gap down, and a breakdown later in the morning on heavy selling volume. We short in the area of 26 5/8 (under the 27 whole number support) and cover out in the high 25s as our cover stop gets taken out on the way up after 11 am.



## Larger Premarket Gaps Down Under Previous Day's Low

Remember we typically start looking for bounces in stocks that gap down more than 8-15%, right?

One exception to this is if the stock gaps down to retest the immediate day prior's low, in this case to the right, TXCC, that was under 20, at the 19 3/4.

One good thing about these shorts is that you can easily see where your cover stop loss would be, eg the 19 3/4 line.

So, a short on the open, around 19 5/8, would let you cover as low as 18 5/8 or so before a bounce takes out our trailing cover stop.

For these types of patterns, make sure you have confirming indicators that shorting is the right move, eg your sector charts all gap down a bit on the open, the COMPQ is making or near a 2-day low, or is selling off after a large gap up, etc.



Finally, we have SUNW, a stock like INTC MSFT I rarely trade since volatility is low.

We do have a good pattern to work with today, a "failed bull cup" in the premarket, you can see the price tested 21 3/4 a couple of times before losing it, we short on a breakdown, new low Under the Premarket Low (that's important, make note of it) that's also under the previous day's low.

In this case, we could nibble +1/2 on a short under the 21 1/2 short on the open, cover around 21.



Types of short plays: lunch weakness shorts, morning top shorts, momentum shorts.

● **Main Points:**

- We are covering a number of different types of short plays in the lessons in this module so that you can become completely familiar with where the entries are.
- There are many short opportunities in each trading day, and you are encouraged to learn how to play these as well as our long plays.
- Most traders never short - this is a mistake.
- New traders try to short momentum runners - this is also a mistake.
- Learn to short 2-day breakdown lows using bear cup patterns etc. as we mention in other lessons as well.
- Pattern recognition is one key to successful daytrading.
- By showing you many examples of annotated chart patterns for these short plays, I am hopeful that you can learn which shorts are likely to work out, and which types to avoid, based on your trading experience.
- For example, new traders [less than 1 year fulltime experience] should never go against the trend and try to short tops, or momentum runners.
- It is always important to remember to use a cover stop loss on shorts, just as in long trades... eg if you're wrong, get out with no greater than a -3/8 loss, ever.
- In general, I like to short under a whole number, say at the 3/4 or 5/8, and use the whole number above my short entry as the max stop loss exit to cover.

**Major Types of Short Daytrading Plays**

Here's a brief summary, we will illustrate all of these with recent chart patterns, below:

**(reminder) 2-DAY LOW BREAKDOWN SHORTS:** These are the best shorts, the inverse of our long 2-day breakout high plays. Simply look for a stock to be making a new low below the previous days low, and short under the whole number below this area.

**LUNCH WEAKNESS SHORTS:** As we mentioned, look for weakness after 11:30-noon, til around 1 or 2... stocks will often sell down during this time frame, making for good shorts. Beware of 12:30 and 2pm long reversals, on rare occasions.

**MORNING TOP SHORTS:** Often you will see stocks put in a top at around 10am. This is a good time to look for reversals and enter shorts for experienced traders, as the stock makes a bear cup.

**MOMENTUM SHORTS:** For experienced traders only, these are worth learning as well - you need to be very experienced in reading time & sales to even consider these. These are following multipoint runs up, and are shorts initiated after selling below a whole number has occurred, eg you see a "bear cup" pattern and have a t&s confirmation. The opposite of "catching a falling knife", these are generally not recommended... at least, not unless you're skilled at spotting reversals..

**2-day Low Breakdown Short**

As a brief reminder, these are the best shorts to look for, in the order of "likelihood of them working out correctly" for you. I am mentioning the other types below to broaden your vocabulary. Remember, losing a 2-day support level usually works out for a short. In this case, we'd take a stop even on the first attempt at 10, and made a good 1-point run on the lunch 2-day breakdown as indicated below:



## Lunch Weakness Short

Here's another examples of a lunch weakness short on an intraday chart, PWER losing support at 35.

We enter the short at, say the 34 5/8, and trail a cover stop down til we're out at the 33 1/4 or so, for a +1 3/8 on it.

Lunchtime seldom gets new buyers, the market is often choppy and/or weak.

If it's just chopping around in a tight consolidation, or trading range, then do not trade it.

If, however, the stock loses a key support level during lunch (again, preferably a 2-day support), then you can look to enter a short, again with a 3/8 max stop loss in it, and look to cover with profits by 1-2pm.



## Shorting the Morning 10am Top

CAUTION: Experienced traders only

This is for experienced traders only.

You can look to catch a reversal at around 10am, where many stocks put in a day's high (or at least, the morning high), on weak or choppy days.

Of course, you would not short at 10am if the whole market is running, making new 2-day highs, the TRINQ is under 1 etc etc... use common sense.

The 10am time frame is important to the morning session, and is when the first strong trend develops, after the market's chopped around in it's 9:30-10 and 10-minute reversals.

Look to exit open longs near 10am at the first sign of weakness, using a close trailing stop (eg 1/8 to 1/4) if in long, and possible reverse to short on any weakness and bear cup pattern.





## Shorting Momentum Runners (Not Advised for most traders)

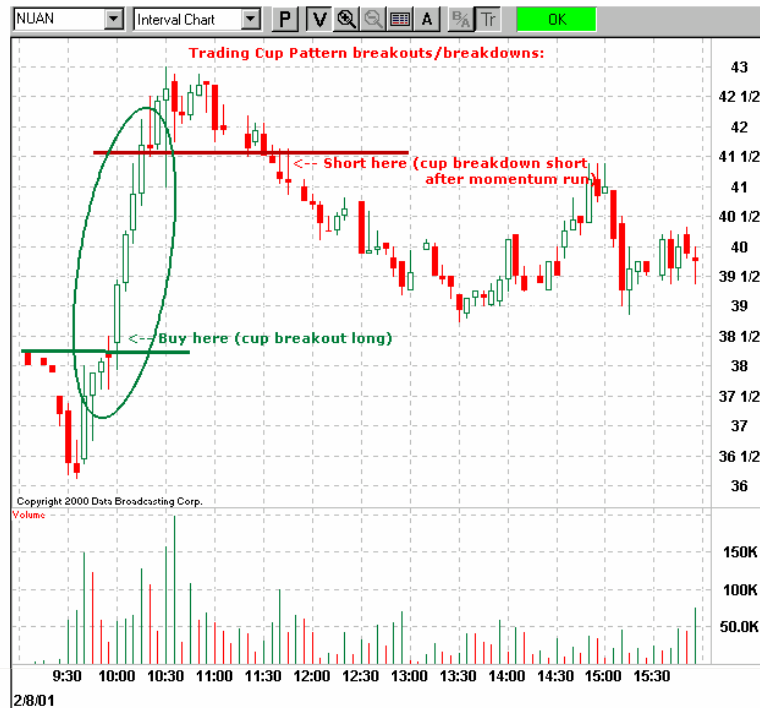
CAUTION: Experienced traders only

Finally, we will look at the type of trade I don't recommend for most traders... which is looking to short momentum runners... in fact I've spoken against this type of trade, since it is how most new traders get burned.

We can see a long buy on a bull cup breakout early in the stock... in this chart we'll look at the short entry off the top.

How would you ever know it wouldn't run to say 45 or 47??

That's the problem with this type of trade, same as the inverse, in buying long stocks that are tanking. A clue is a) multipoint run up b) high volume in the consolidation zone at 10:30, telling us a lot of stock is changing hands.. c) bear cup forming from 10:15-11:15 and d) finally, most important, a bear cup breakdown under the 41 1/2 at 11:30 into lunch weakness.... several factors telling us it may finally be time to consider shorting this one. Careful on these, and don't do them unless you're fast and good w/t&s.



### Module Five

### Shorting Skills for Active Traders:

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- TA for Shorting #1: Basic Short Chart Patterns: Identifying Intraday Sell Patterns

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MODULE 5

#### ● Main Points:

- As with your long trades, being able to recognize successful shorting chart pattern setups can help you profit if you learn them.
- We will share patterns you will not see elsewhere, using high-percentage, easy to enter trading patterns.
- Remember to trade in the direction of the market, eg resist the temptation to short when the market is in a daily uptrend; short when things are "feeling down, like there's no buyers around", early enough though to avoid shorting at a bottom. TA and chart patterns are the key to doing this successfully.
- There are a number of correct short chart patterns illustrated and explained below. Please take a look at them and compare them to your core basket of trading stocks.
- Remember, we strongly suggest that you "get to know" from 5-30 stocks and their intraday patterns fairly well to be a successful day or swing trader.
- Do not jump into trades on stocks you've never heard of, unless you're experienced and successful with your core basket of trading stocks first... also avoid trading stocks under 800K average daily trading volume.
- Pattern recognition, eg "hey it's losing a 2-day support level here" is the key to effective shorting, along with keeping effective cover stop losses and using trailing stops.

### How to Short Using 2-Day Support & Resistance Levels

Let's start with a big picture view. Once you've established that the market, the futures and your sector seem to have more sellers than buyers, eg the prices are in a technical downtrend, we want to focus on 2-day chart patterns.

The very first pattern I want you to learn is how to look at 2-day support and resistance levels. Remember, we buy 2-day breakouts, right? Well, the reverse is certainly true when it comes to selling, and shorting stock. You should enter a short when a stock is making a new 2-day low (except for shorting the bottom of a stock that's tanked already premarket, of course - that's an open gap down, for which we'd expect a bit of buying). Again, these are intraday plays, eg you're entering the short in the early part of the second day... you use 2-day charts for your intraday trading.

**ALTR Short:** Lost 2-day support level at 9:45

To the right we see an ALTR 2-day chart 10/5-10/6/2000.

First of all, what's the support level on 10/5/00 trading day? It was roughly **47**.

So you say to yourself, ok I'll look for a short in ALTR on 10/6 if it loses 47. Sure enough, the stock opened flat and started selling. The first short here could be near the open. (Note: typically I would enter shorts on the open (more for open gap up shorts) or around 10am).

Here, we see it got a bit of buying from 10-10:15, but couldn't get over 47 support (now resistance). This is a confirmation, and we have a successful short. Our cover stop loss? At right over 47, of course, say 47 1/4 or 47 3/8.



Where do we cover ALTR? I typically like to look to cover around 10:30, since I expect bounces, but in ALTR's case no buyers emerged. An initial short profit of 4-45 1/4 or + 1 3/4 could be had for a morning short, covering at 10:30, or, if you're patient you could have waited until 3:30 end of day short covers and covered around 43, for a +4 point gain on the short. (Note: we even called this short on the morning of 10/6 in our live tradingtheopen.com room beta test).

**Traders' Plays - What to look for in 2-day support and resistance level short trades:**

- Identify the 2-day low/support level for the stock
- Look to enter a short from 9:45-10am when the stock is making a new 2-day low.
- Look to make your initial cover at around 10:30 or so, be cautious about staying short at this time.
- Use trailing stops to lock in profits, and look to cover shorts quickly, so you do not get stuck in a "short squeeze"... which means, make sure you're already set up with a fast order routing method, eg ISLD ecn or SOES limit buy order.

**Self-Test: Using two-day support for an intraday EBAY short:**

- Identify the 2-day low/support level for EBAY
- What's your "short signal" on 10/6/00?
- Where should your cover stop loss be located?
- Where would you look to exit with profit in this trade (hint: always always cover shorts before 3:30, since you will have an end of day short cover rally most of the time).



Answer: EBAY made a new 2-day low when it started tanking on 10/6 and lost 62 1/2. Covering by 10:30 or so at 58

1/2 would give you a +4 point profit on this short. Covering towards the end of the day at 56 or so would give a +6 point profit. (11% in one trade).

## Cup and Handle Breakdowns: High Percentage Chart Pattern

Here we see the opposite our cup and handle breakout on the open, a cup and handle breakdown. Actually, this is more of just a cup... imaging a coffee cup turned upside down, for the price action that you see in the initial part of the trading day. When it loses it's opening price, I look to fire off a a short trade. Let's take a look at an example here with CMCSK:

**CMCSK Short:** Lost opening price level of 44 1/4 at 10:45am.

2-day support level broken down at 9:45

Our sell/short signal is where we indicate it in the chart to the right. In this case, it would be tough to get a short off if there weren't many upticks to short into. The key is to keep hitting the short button til the tick reverses and you can get your short off. You may have to keep trying to short, punching the short button for 30 seconds or so, until an uptick is made that you can short into.

In this case, since the short signal occurred after 10:30, we can stay in the trade for a bit longer, til right before lunch.



**INTC Short:** Lost opening price level of 41 at 10:45am.

2-day support level broken when it lost 41.

You'd look to cover the short right over decade support, in this case right over 40.

Again, notice how the stock got some buyers early in the session (you could have traded the cup and handle breakout long on the open, a fast trade til 9:45), then sold off for the rest of the day.

Notice too that the stock is in a technical downtrend, eg lower lows and lower highs. Trade (and in this case, short), with the trend.



## Momentum Short Entries: Tanking on Open

Much as with momentum long plays, we tend to avoid these, but, you should be aware of them as one style of shorting that some traders like. (Why do I tend to avoid these? I want a reason other than "the crowd is selling it here" to enter a short, eg losing a 2-day support level lets me know where to put a cover stop loss more easily.

Momentum shorts are more difficult than longs, since you need an uptick to short into. The time to do this is on a "pause", when the initial rush of sellers is taking a breather and the stock is waiting before selling off some more. In the ATHM example below, this pause was at 11 1/8. Do you see it below? We missed the 12 to 11 tank, but getting onboard with the 11 1/8 to 10 3/8 was a bit easier.

**ATHM Short:** Selling from the open, no buyers in sight.

After an initial pause at 9:40, ATHM kept selling down from 11 3/4 to 11 1/8, paused for a bit longer, then kept selling off to around 10 support. As with longs, you look to find reversals near decade numbers, eg 10 20 30 etc.

Quick self-test: where is the micro-resistance level from the timeframe of 11 am til 3 pm at?

Answer: microresistance at 10 3/4... notice it couldn't break over that point though it tested it 3 times during the day.



**VERT Short:** Here's a more dramatic example. VERT opened up right under 30 and sold off all the way down to 22 and so.

There were three good short entry signals to watch for here:

- 1) It couldn't make a high above the opening price near 9:30-9:45
- 2) It was right under 30 decade resistance, a great place to short
- 3) A second short opportunity came when it bounced at 10am and kept going down from there.

We'd look to cover somewhere before 20 support level, in this case we got strong support all day long at around 21 1/2...scalps off this support level would be ok too, later in the day.



**Homework Assignment:** Okay, now you know what to look for - these are the signals professionals use. You won't find them in anyone else's book or website. Homework: I recommend that you use a chart software package, or website like bigcharts.com with 5-day charts, for some of the stocks that you like to trade, and look for similar patterns.

Look for these pro shorting patterns in the stocks that you trade. Notice that NONE of these examples tell you to short stocks that are running up - a common new trader MISTAKE. You want to Sell Weak Stocks and Buy Strong Stocks. Do NOT try to short a shooting star, or buy a falling knife.

These patterns are to help you sell weak stocks at the proper time, for highest short profits. Good trading!

- TA for Shorting #2: More Chart Patterns for Shorting: Volatility and Volume Tracks

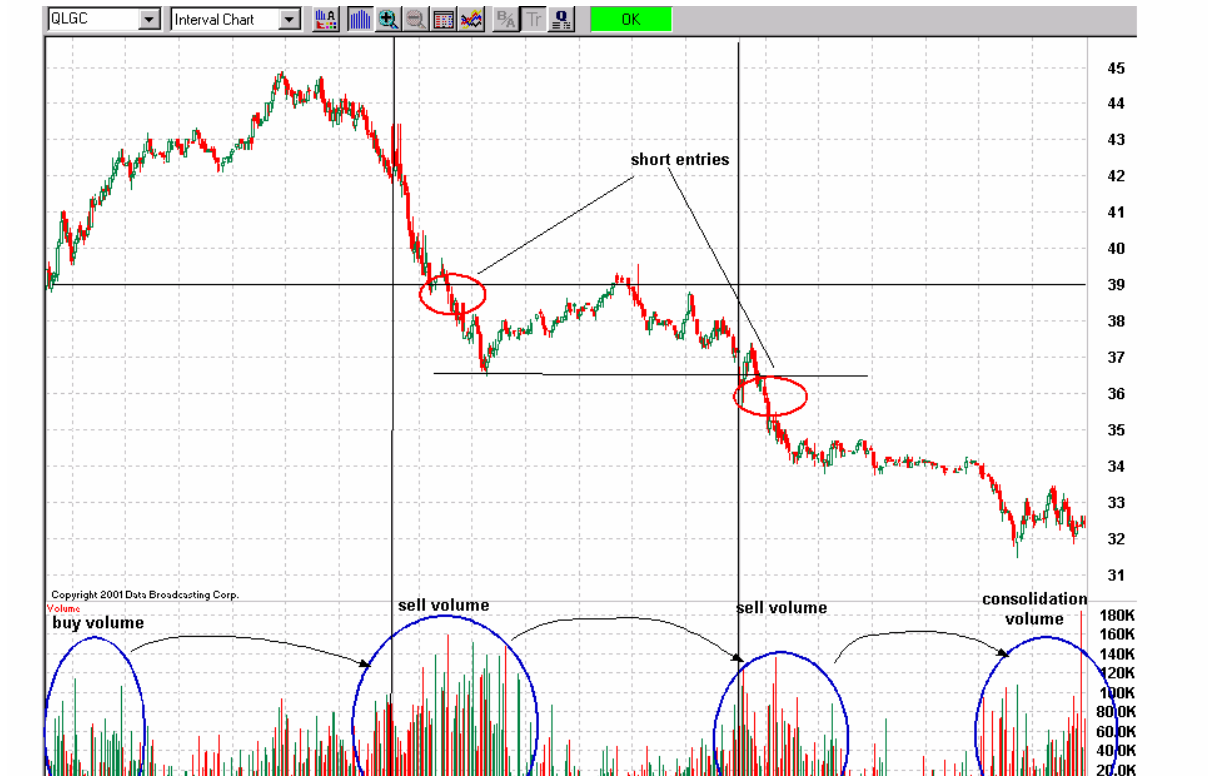
● **Main Points:**

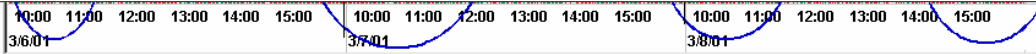
- In psychology, there is a saying that "past behavior is the best predictor of future behavior". In the stock market, we say "bears win, bulls win, pigs become bacon".
- When it comes to repeatable patterns, there are very few, in stock price movements, beyond an initial retest and failure/breakthrough of specific support/resistance areas.
- One thing that does tend to repeat and hold is volume patterns, as in the examples in this lesson. A good example is in the QLGC chart immediately below, the volume is heaviest at the open/close, and thins down from 12-2 daily.
- How do you use this to profit? Buy on similar patterns day to day, eg retest and bounces, or short new breakdowns/buy new breakthroughs, particularly when this volume propels the stock price through a 2-day high or low.
- Be a detective - look for clues in the stock charts, using all your technical knowledge from previous DTU lessons and other books out there.
- Volatility is important as well - see if a stock is exceeding or near it's 2-day trading range, eg if you know KLAC has a 2-3 point trading range and it's already moved 2 1/2 points in one direction on this day, you wouldn't enter in the same direction, unless there's a very (rare) compelling technical breakout.
- Put the probabilities in your favor - make sure to know your stocks, the behavior of the traders in it, as measured by volume and volatility "tracks in the sand" that the stock leaves for you in the previous trading session.

**USING VOLUME TRACKS:  
Repeatable Early/Late Day High Volume Patterns**

Let's look at several days of QLGC in the chart below here. You can see the high volume at the start of each trading day, right? On the first day below, it was all buy volume- a great time to go long. When this started to reverse, we saw short entries. Note that we didn't "guess a top" on the first day, and we didn't short the last third of the range down (from 39-41) on the open of the second day, we instead wait for it to lose the previous day's low, and shorted 38 5/8. The second short entry, on the third day, is again when it loses the previous day's low, short 35 5/8.

What you want to learn here is how to study the charts like this and see what I'm seeing: that "most of the action" occurs on high volume in the first hour or so of the trading day for this stock. This, we know that a short on the third day is likely to continue on downwards, given the volume pattern and 2-day low breakdown. Make sense?





Here's another example to the right (AMGN), that shows us a good short entry under the decade 70 support, on the open of the current trading day, under 69 5/8.

Why? Heavy sell volume on the open drags the price down, and our profits go up, as we short the 69 5/8 on the open, under the two-day low, on heavy volume.

We look to cover (and possibly reverse to a long) once sell volume starts to lighten up, and a cup pattern reversal on heavier volume starts to form. That's our "cover the short" signal, and we're out at 67 3/4 or so for a nice 1 7/8 short profit.



**EXTR Short:** Here's an excerpt of 3 trading days in EXTR.

Let's scan it for major patterns first:

Support line at the 21.

Heavy volume sellers on each of the two openings shown here.

We short on the start of the third day, as we get our new low, under the 21 and again under the 20.

You see heavy volume on the open of each day, right?

You also see heavy sell volume on the close of the first day, right?

This tells us the market is in a "sell this stock" mode... so, we nab two good short entries on 3/8/01 on the way down.



Finally, we have CMRC - you can see the first entry was a bit tough to catch, as we want a new low, under a whole number, meaning our short entry is at the 15 5/8.

It consolidates for awhile, then sells off on down to 13.5, never once stopping us out.

This is a good short, good for multiple points.

One clue is the volume, it's much higher on the sell side on 3/8/01 than it was on 3/7/01.

Also, you can see CMRC sold on the open of the previous day as well, another hint that this is a "stock to short".



## Module Five

## Shorting Skills for Active Traders:

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- TA for Shorting #3: Using Stochastic Reversals to identify short opportunities

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MODULE 5

### ● Main Points:

- Remember that we use several types of indicators in daytrading: those called "OSCILLATORS" (eg stochastics, futures, \$COMPQ) and "TREND" indicators (individual intraday 1-min. candlestick charts, nas composite, sector charts)
- As an "oscillator" type indicator, remember that stochastics give relatively FAST trade signals and we use them, like all oscillators, to indicate REVERSALS and PIVOTS: when to enter a long trade on a bounce, or when to sell a profitable open position as it starts to drop
- IMPORTANT: Note that using stochastics for shorting stocks that have shown recent strength is ONLY for experienced traders. In general we want to short stocks that are losing key support levels vs. shorting these stochastic reversal "tops", which is more risky. **Experienced traders only should use this method**, others are advised to short stocks that are losing 2-day support levels using your 1-minute candlestick chart patterns.
- HOW to READ Stochastics: the only time you pay attention to stochastics are when the two lines, %K and %D, are **crossing over each other either above 90** on a downturn, **or below 10** on an upturn. So, they've either gone above 90% and are now headed downwards, having just crossed over each other (time to sell/short), or have dropped to below 10 and are just now crossing over and headed back up above 10 (time to cover short/buy long).
- Drawback to stochastics: more than other indicators, they may give false buy/sell signals, since they move relatively fast. You can experiment with stochastic settings, I like 15/5 (use 15, slow stochastics, in esignal.com, as below). So, you use them as a secondary, confirming indicator in your trades, along with other things like the \$TRINQ, time & sales, level 2 and chart pattern prior to entering or exiting a trade.

## How to Short Using Intraday 1-Minute Stochastic Reversals

For shorts that you enter early in the session, either 9:30am open gap shorts or shorts during the morning's 10-minute reversals, we may get a stochastic crossover early enough to help us, as in the chart below. When you see the stochastic lines both go up strongly with the stock price and then start to reverse, we can look to enter a short, once the stock price has started to head down. Always have a close cover stop loss, no more than 1/4 point.

**BVSN Short:** Looking at the stochastics here, we see they gave us an "overbought" pop signal where the pink line is, they are over 90% and crossed over. The stock price made a top right after this and headed back down.

You would wait until the stock has lost a key support level, eg 29, and enter the short at say 28 3/4 after it's made it's first peak. You would watch carefully to see if there was support at 28 whole number, possible cover there and reshoot once it loses 27 3/4... repeat the short until the stock price consolidates & stabilizes in a range to cover.

Stochastic pops are used to define "overbought" conditions in the stock price.



What is the key chart pattern we use? Cup breakouts. In the case above, we see the stock made a "bear cup" from 28 to 29 1/2 and back down to lose 28 (short signal right under 28), a conservative entry.

Experienced traders would short the stochastic reversal pop looking for it to lose 29, after the first stochastic top, and short at 28 3/4. Both strategies worked in this example, for +1 gains.

### Traders' Plays - What to look for in stochastic short trades:

- Practice identifying when the stochastics indicate "overbought" (>90%) and "oversold" (<10%). If you see too many wiggles up and down past these points, readjust your software til you get clean signals, eg the %K and %D settings, on a one-minute candlestick intraday chart.
- You look to short the reversals in stochastics that get over 90%, also using whole number resistance to your advantage, in combination with Level II, to time your entries.

**Trader's Pop Quiz:** Using this ALTR chart, identify where you would enter short trades. Use a piece of paper held over the chart (slide it from left to right) to simulate the trading day... When do the stochastics indicate overbought/oversold?

- Where would you first look to go short?
- How would you manage the trade? What order routing option are you most likely to use? Pull up a level II window and look at the participants on the inside bid, who & how would you route a sell/short to them?
- Where would your cover





stop loss be for each trade entry? What's the key support/resistance levels you will use?

In the chart above, note that we have a sharp spike in the stochastic, as with any sudden move in an indicator, it is prone to a fast reversal. Also, notice that sometimes the stoch's can lag and not be as helpful, as in the "late crossover/short signal" we have in the second stochastic rise above.

## Using Stochastics with Other Indicators: What's Most Important?

Do you get confused by how to use all the indicators together in a system, properly? I get many questions on this topic - with so many indicators, how do we judge the relative importance of each in our trade decisions, and how do we use them as a system? This area will help you, in using stochastics properly.

**AAPL Open Short:** Lost opening price level of 21 1/2 at 9:45am. Note that it would be very difficult to get an uptick to short into if you waited until the stock started to break down in this case. The solution? Be ready to keep hitting your 'sell/short' button repeatedly until you get an uptick, say 10-15 times, spaced a few seconds apart each time (don't chase though).

Relative importance of indicators: as an oscillator, you **give stochastics secondary importance** (unless you're a scalper, in which case they're very important)... in determining whether or not to enter a trade.

The main thing to look at is the chart pattern, the \$TRINQ, the sector indexes, and the time & sales for your stock.

The stochastic and level II is always of secondary importance. This does not mean you do not use it, on the contrary, you want to see the stochastics reverse to the downside over 90% for a short entry if you're shorting a top. You're looking to have as many indicators tell you the trade is a good one as possible, and react before "the crowd" does.

I find you usually do have at least a couple minutes to get a good trade off before the crowd catches up. Part of this is my using 1-minute charts. If you're using chart support/resistance patterns and time & sales correctly, you do not, contrary to what some people say, have too much noise.

In fact, I depend on having more information, faster, than other traders, to help me make winning trades consistently. I know how to mentally filter out non-important information, so, I like the 1-minute charts. U



### Using Stochastics Like a Professional:

1. Make sure to experiment with your %K/%D settings on your 1-minute chart to get an optimum setting. Different stocks are best traded with different settings at times. My default is 15/5.
2. Practice integrating signals from your stochastics with your chart pattern and market indexes, like the \$COMPQ and \$TRINQ.
3. Be decisive on acting as soon as you get a confirming 10/90 crossover signal from the stochastics. They move fast, and as an oscillating indicator your goal as a trader is to use them to rapidly help you fire off correct trades.
4. Be fast to take stop losses when you are wrong, we always advocate 2-3 spread stops for daytrading, usually 1/4 to 3/8 point.
5. I use stochastics primarily as exit criteria vs entrance criteria for longs, eg when the stochastics start to go over 90 then head downwards, I will be likely to sell out a profitable long position and look to enter a short if it's right under a key resistance (eg whole number/decade number) level.

Practice using stochastics as part of your trade setup. I put them on my large intraday (1/2-day 9am - 12noon) chart, only. Do not put stochastics, volume and other TA indicators on a lot of small thumbnail charts, it clutters them. Focus in on a specific trade by putting the ticker in a large, full-monitor size intraday chart, that has all your technical indicators on it. Good trading with it!

● **Main Points:**

- You know from previous lessons how important it is to look at broad market indicators like the COMPQ and TRINQ, along with sector charts, to **identify relative strength and weakness among sectors** that are diverging each day.
- In this lesson, we will look at how you can **use the divergence in sector charts to recognize good short trading opportunities**, as some sectors are always weaker than others each day.
- I follow the \$GIN (Internets) \$SOX (semis) \$GHA (hardware) \$GSO (software) \$GIP (networkers) \$IXTC (telecoms) and \$RLX (retailers), \$IXBT (biotechs), for example.
- Learn to recognize variation in chart patterns among these sector charts. You should use **1-minute 1/2 day close line charts** to follow the various sectors. At first, choose only 2-3 sectors to watch, say the \$GIN \$SOX and \$GSO/
- **By variation in chart patterns**, I mean look for the following: a) one sector chart making a faster bear cup than another chart b) sector chart percentages lower for one sector than another for the trading session so far c) chart pattern weakness and strength, as seen by "how high are the bounces compared across sector charts" as they map out during the morning, from 9:30 on.
- After you **train yourself to recognize the variation**, we look to trade based on relative strength and weakness. You know, of course, to be following the tier 1 "Lead" stocks within each sector, at least 2-3 per sectors (eg \$GIN: EBAY YHOO, \$GSO: MSFT ADBE \$SOX: INTC) etc.
- **We look to short stocks that are in the weakest sectors each morning**, in realtime, as we see them being traded. If the whole market is pretty much flat (eg sector charts within a 1% trading range) but the telecoms \$IXTC are weak, we go look to short stocks in that weak sector, eg WCOM and other telcos.
- You **trade based on what the market is telling you**; if it's saying "there's no buyers in this sector, everyone's dumping it and rolling their money into another sector" etc, then you can look to short stocks in that sector, during the initial selling.

**Sector Shorting: Using Variation in \$GIN \$SOX and others to ID short sectors**

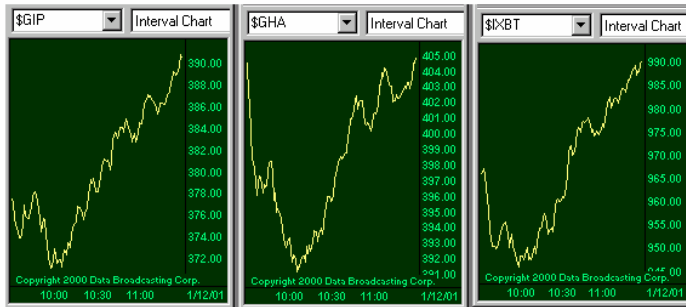
You should have at least 2-3 1-minute 1/2 day close line sector charts open in your trading station so you can follow the relative strength of the various sectors, as illustrated below.

These sector charts show roughly equal weakness, telling us that it's a "short any sector"-type day.



**Sector Chart Variation**

Many days, however, you will see variation among the sector charts, and some will appear weaker than others. An example is found below. These are 3 relatively strong charts, none of which we would short stocks within. However, one sector is weaker than the other two: which is it? And Why? (this is important for you to understand)



Answer: the \$GHA sector is weaker than the other two, as it is just now testing it's high of the day, just now completing a bull cup, while the other two \$GIP and \$IXBT sectors made bull cup breakouts much earlier in the session, at 10:30. Can you see this? What does it tell you?

That stocks in the \$GHA (hardware, eg DELL, AAPL) sector are weaker than other sectors, and would thus be more likely short candidates when the market reverses to the downside. Of course, the best days to short are like those found in the 5 sector charts above, where the broad market is selling off.

Go with the overall trend, using sector chart variation to 'lead the way', and alert you to the best groups of stocks to look for shorting.

### Sector Percent Change: Watch This!

It's very important that you make this a regular part of your toolkit: a small quote box that has only the COMPQ and major sector percentages in it.

This gives you a very useful, handy reference for which sectors are under- and over-performing the COMPQ, and what their relative ranking is, minute by minute throughout the trading day. Powerful - use it.

This chart tells us that internets are the weakest today, down 7% (wow), while retailers were off 2.3%.

Symbol	Pct
\$GIN	-7.0%
\$SOX	-5.4%
\$GSO	-5.4%
\$GIP	-5.3%
\$IXTC	-4.6%
\$COMPQ	-4.4%
\$GHA	-3.6%
\$IXBT	-2.3%
\$RLX	-2.3%

### Lead Stocks within Each Sector Provide an Early Indicator

Following the "lead stocks" in each sector is important, as they get the bulk of the money earlier than others do within the sector, and can be thought of as sector-specific futures (almost!), as lead indicators.

What this means to you is, you may watch a lead stock like EBAY or YHOO (tier 1) and trade a tier 2, smaller cap stock like PSFT DCLK RNWK in the same sector, based on what the "lead stocks" in the sector are doing.

This is an important trading concept to "get right" as well. In shorting, we look for 2-day breakdowns after 9:40 as a key entry point, also after 10am tops are put in and again near 10:30 (where we'd cover on down days, or at least, tighten up our trailing stops).



### 2-Day New Low in the COMPQ = Great Time to Short

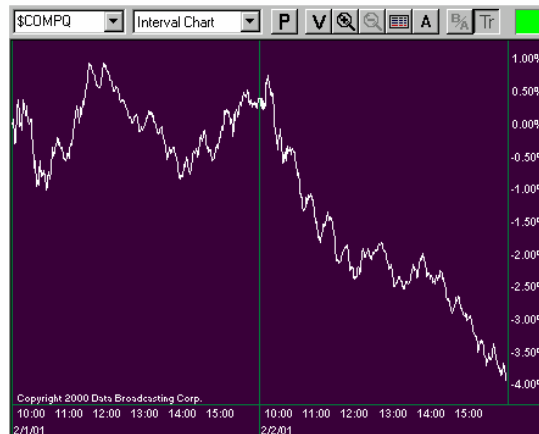
OT the trend's your friend, right? Well, just as we seek to buy 2-day breakouts to the upside for new long positions, we also look to:

Short stocks when the COMPQ is making a new 2-day low. This occurred right after 10:10 or so on the 2-day chart to the right, on 2/2/01.

After lunchtime choppiness (expected), the market continued selling down throughout the rest of the session.

Food for thought: what would you have done if the COMPQ started to head back up through its two-day low in the afternoon session, if you were trading at that timeframe?

Answer: look for long bounce plays, of course, especially from within sectors that did not sell down as hard as the others.



● **Main Points:**

- There's several shorting errors that new traders are prone to make that I want to show you how to avoid.
- As you go through the examples, look for things that would separate the professional traders from amateurs, both in their use of proper risk management and in using the chart patterns.
- Shorting is primarily for more experienced traders, and is not recommending for first-year traders to try.
- This is not to say you should ignore shorting, it's important that you eventually be able to short as well as go long, so you are making money on both sides of the mountains, the valleys, that occur in stock trading.
- If you make mistakes in your trades, be sure to document the chart pattern and 'what went wrong'.
- If you take a small stop, eg less than 3/8 of a point, that's normal. If you take a large stop, over 1/2 point, something's wrong, and you need to pause and evaluate why.
- Much of what you find in the way of errors are simple mistakes, eg not trading the chart patterns correctly.
- Other mistakes may be due to order routing errors, eg trying to short via SNET when only ECNs are bidding.
- Also, you want to use level 2 in your shorting, but again, not as the primary decision making tool. Your chart patterns are what you use in all trading, level 2 is used to help manage cover stops and order routing, that's it.
- Learning how to use time & sales effectively is also key to good trading, as it shows you the trade-by-trade sentiment in the stock.
- Being too slow is also a common enough error that new traders make. Daytrading is a fast game, you need to hone your reflexes for it. That's why I say shorting is for experienced traders only, as you need to get both shorting into the uptick correct, as well as your chart analysis and risk management.
- Here's a few common errors and mistakes you want to check yourself for prior to trading short:

**Avoiding Common Shorting Errors & Mistakes**

**Error #1 To Avoid:  
Failing to Observe the Technical Signals.  
Example: Shorting an Open Gap Down**

Remember our basic trading guidelines - you want to play off extremes.

Buying gaps down, on confirmation of buyers, is the right play. I'm much more leery of shorting a huge gap down, eg over 8-15% down on the open, as it will often attract buyers.

So, you do not short an open gap down, that's as bad as buying an open gap up, for a gap and trap.

You need to look for cup pattern reversals following a gap, and play the trade according to the major trend for that day, since the stock opened.

In our live trading room, we nailed this one long over 36 3/8 for good profits. ( a competitor's room had their traders take a 3 point loss telling their traders to short the gap down!).

Professionals trade early, with the trend, on confirmation signals, as I teach you to do.



**Error #2 To Avoid:  
Going Against the Primary Trend  
Example: Shorting a Momentum Runner**

This is the same as trying to catch a bottom, a falling knife, without any reversal confirmations.

New traders will say "It looks expensive here at 32, it already ran up 2 points", only to see it go up another point and a half, as in this GSPN example.

Remember, we need technical signals for all trades. Trying to 'catch the top' of a momentum runner is poor trading.

Good traders will wait for it to consolidate a bit, then lose a key support level, before firing off a short.

Do not guess where the top of a big runner is for shorting. Wait for a confirmation pattern on these.

And, these should only be attempted by very experienced traders. It's much better to short a new 2-day low on the way down than it is to try and short the top of a stock that's just ran up a lot.



**Error #3 To Avoid:  
Failing to Short a 2-day Breakdown  
Example: Watching vs Shorting a 2-day low**

Remember to not get 'paralysis analysis' if you see a solid entry on a technical signal like this one.

The stock, JDSU, is making a 2-day low breakdown under 37. We short it at 36 5/8, and look to cover around 34 for a nice profit.

2-day breakdowns are good to short into, generally speaking, so be prepared to recognize and trade these powerful short patterns when they are available for you.



## Short Daytrading Basket Trading Worksheet

Instructions: Scan for stocks each day, and weekly, that fall into each of the three categories below. Use this to improve your ability to execute winning short trades.

Goal: Be able to Scan and select stocks that are good for intraday shorting

### Open Short Example Types:

#### **Stocks that Are Making New 2-day lows:**

These are the best types of shorts: look to short stocks that are making new lows, under the previous day's low, after 9:45am or so. Short under whole number resistance, eg at 3/4.

#### **Open Gap Up Shorts >15% w/volume >40K:**

Slightly riskier, look to short stocks that make a reverse cup pattern on an open gap up of over 15%, short around 9:40-10am.

#### **Shorting the reverse side of a momentum runner:**

These are generally **not** recommended, for very experienced traders only, short a stock that is in a mini technical downtrend after running up over 12-15% during the first hour of the trading day and is now reversing. Note that it has to be making a lower low/lower high pattern after making a top. Use close 1/4 point stop cover loss max on these.

### Stocks Meeting This Criteria:

Papertrading Results for Each Type: Your Net Profit/Loss

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## Finding Support and Resistance for Shorts

*Goal: Be able to improve your trading entry and exits by correctly using support and resistance levels*

Complete this worksheet to help you identify chart pattern support/resistance levels for shorts.

Example 1:  
RNWK



On the RNWK chart to your left, draw in the following:

- 1) Early morning consolidation area (circle it)
- 2) Support level in the morning (horizontal line)
- 3) Correct short entry
- 4) Correct short cover area

Example 2:  
EXDS



On the EXDS chart to your left, draw in the following:

- 1) Early morning consolidation area (circle it)
- 2) Support level in the morning (horizontal line)
- 3) Correct short entry
- 4) Correct 1st short cover area
- 5) Second support area (horizontal line), and 2nd short

Example 3:  
SUNW



On the SUNW chart to your left, draw in the following:

- 1) 2 day support and resistance areas (horiz. lines)
- 2) Correct short entry (intraday, horiz. line)
- 3) Correct short cover area (above 2-day support)

## Putting it All Together: Your Shorting Trading Plan & Skillbuilding

### Your Daytrading Short Game Plan:

**What stocks** will you plan on looking for shorts in, on a regular basis (your "core shorting basket")?

**Tickers:**

**What types of short trades** do you think you'll try to do, primarily? (circle)

- Losing 2-day support (best)
- Intraday range shorts (ok)
- Shorting momentum tops (risky, for pros only)
- Other: \_\_\_\_\_

Notes:

### Short Risk/Trade Management Plan:

**What stop losses will you use, Maximum, per trade (circle)?**

- 1/8th - 1/4 point (close trading, scalping-style)
- 1/4 point (two-spread cover stops)
- 3/8 - 1/2 point (wider stops)
- 1/2 point or more (do NOT do this!) Keep all stops < 1/2max

**How Many Shares Will you Short in each trade (circle) ?**

- 100 shares (best for new traders, and for learning)
- 200-300 shares (after you've got some practice and are doing >50%)
- 300-500 shares (average daytrading size, after you're doing well)
- >500 shares (for experienced, pro traders only)

**Which of these Shorting MISTAKES will you AVOID (circle) ?**

- Trying to guess tops and short momentum runners making new highs (only highly experienced traders should attempt these types of shorts)
- Shorting too many shares at first, over 300/trade, in your first 50 trades
- Trying to short stocks that your broker doesn't have short shares for
- Shorting without clearly understanding the best Order Routing choices for you to cover with (I prefer ISLD and SOES limit orders)

**Module  
Five**

Shorting Skills for Active Traders:

Back to  
MODULE 5

Activities

### Module Five: Activity 1 - "Your First 10 Open Shorts"

- This activity will help you learn to correctly identify which stocks are good for open short plays.
- Remember, **open short** means it's a stock that you enter a short sell trade for from **9:30-9:45** or so.
- Use a link like [this one](#) to see the day's %gappers. Your "screen" should be for stocks that have **gapped up over 20-30% on premarket volume of 40K shares or more**, and are starting to sell off on the open. A cover stop loss should be no more than 2-3 spreads up from your entry.
- You can also look to **short % gainers at around 10am** or so, look for stocks with at least 500K volume that are up over 20-30% on the day for these.
- The other "screen" is for stocks that have **gapped down 3-5% on the open and are making new 2-day lows**.
- You will soon learn that setting your stop losses and profitable exit targets is the Most Important part about shorting, just as with any trade.
- For this open short practice activity, I want you to **keep track of your profits and losses** on the 10 trades so you can see how you'd do in a live trading situation.
- Please note that I have a reason for setting the criteria I do - **do not make exceptions** on the rules (eg do not consider an open short on thin volume, eg under 10K volume, to be significant) ... Try my techniques with discipline and see how well they work for you.

Stochastic reversals are also helpful in looking for timing open short opportunities.

Look at WCOM here, the stochastic peaked and reversed, along with WCOM's price... the short signal was when it lost 23.... a cover right over 22.



**The GOAL for this activity is for you to learn how to successfully IDENTIFY GOOD OPEN SHORT trading opportunities, using current examples.**

**Directions - Papertrading 10 OPEN SHORT trades:**

1. **Over the next 10 trading days, I want you to look for a total of 10 "open short" plays that meet our criteria for practice trading. (you may find 2 on one day, 3 on another, none on another etc).**
2. Paper-trade how you would enter and exit these "open short" plays based on the guidelines that we have presented here.
3. Open shorts are typically entered around 9:35-9:45 and covered by 10am or 10:15am at the latest. Remember the first 60minutes makes reversals every 10-15 minutes and you want to be on the right side of these in both your long and short plays.
4. Your cover stop losses can never ever be higher than the opening price was at. In the WCOM example above, thats at 24 1/4... Eg you enter the short at 23 3/4 and have a cover stop at 24 or so...
5. **Keep track of your open short profit/loss for the 10 trading days** that you are papertrading these open shorts on.
6. Most importantly, make a brief list of what went right for your profitable open shorts and what you should have done differently for the ones that you lost on. What changes will you make in your personal trading style based on what you've learned?

**Module  
Five**

Shorting Skills for Active Traders:

[Back to  
MODULE 5](#)



**Module Five: Activity 2 - "Making Shorts a Regular Part of your Trading Activity"**

- This activity will help you learn to **gain confidence and familiarity with the whole idea of shorting**, and help structure several practice activities that should help you become more skilled at it.
- The first thing to do, of course, is to heavily practice it, with a simulator, like the excellent cybertrader.com simulators. If you have an account with them, you just use "demo logon" and still practice trading with live data. If you're not a customer, you can practice with practice data. Or, use whatever simulator you feel comfortable with, just practice.
- Let's look at how to get started on the path to shorting stocks.

**First, you must realize the Value, the Benefits of shorting stocks.**

This RIMM chart is a great example. One of our TTO traders told us about the long run, I had us wait, and short it on the way down, at 38.7, to cover for a nice +1 gain.

Ever miss a "run up" in a stocks? For experienced traders, you can short a pivot on the way down, like this RIMM trade. **New traders, short weak stocks making 2-day lows.**

**Second, you need to get familiar with the uptick rule**, and look for short opportunities based on the chart pattern and time & sales.

**Finally, you need to practice**, practice, practice, til shorting becomes second nature. Papertrade extensively.

It's the "other half of the action" and you shouldn't miss out on it, once you've been successfully trading long for awhile.

Give it a try!



**The GOAL for this activity is for you to gain CONFIDENCE and FAMILIARITY for shorting opportunities, using current examples.**

**Directions - Papertrading Shorts for 4 weeks during the first 2 hours of the market:**

1. Over the next 20 trading days, I want you to decide on **4 stocks** that you will follow and look for shorting opportunities in for the **10am til 11:30am (only) timeframe**.
2. **Next, practice shorting** only stocks making new 2-day lows. These are the best opportunities for new traders to focus in on. If you're more experienced at reading time & sales, you can try pivot shorts like the RIMM example above.
3. Paper-trade how you would enter and exit these short trades. Make sure that you see an uptick in your L2 box prior to entering a specific practice short entry, since you must have an uptick to short into.
4. **Keep track of your practice short trades (how much did you profit/stop out on) and the total profit/loss for the 20 trading days** that you are papertrading these shorts on.
5. Finally, print out the charts of the winning shorts that were good for the most profit, and make a brief list of "what went right" for these shorts. Examples can include: weak market, COMPQ making 2-day low, you shorted a weak stock in a weak sector that day, time of day was good for a short, stock was making a new 2-day low etc.
6. To gain confidence, practice until you are consistently making winning trades. Take several months to do this, do not be impatient. Like all trading skills, this one takes time to master - Best wishes!

## Module Five

### Shorting Skills for Active Traders:

Click on each link for a new daytrading lesson. Be sure to complete the trading worksheets and activities for each module.

[Back to  
DTU CAMPUS MAP](#)

Click on each line for daytrading lessons from the list below. An underlined link means the content is now available. **Note: click on your browser's "reload" button to make sure you see the latest modules posted as they become available.** Remember to set your screen resolution to at least 1024x768 to enjoy DTU.



#### Trading Lessons

 = Updated pages w/in last week.

#### DTU Module 5 Lessons:

- [Introduction to Shorting - DTU's Short Selling "Rules to Live By"](#)
- Understanding the differences between shorting and trading long: uptick rule & order routing
- [Open Shorts: The easiest and best short play](#)
- [Time of day patterns for best short selling: finding the best trading opportunities](#)
- Types of stocks to sell short: from low to high risk shorting
- [Premarket indications for shorting opportunities: chart patterns, news/earnings](#)
- [Types of short plays: momentum shorts, morning top shorts, lunch weakness shorts](#)
- Avoiding dangerous shorting situations: staying away from "short squeezes"
- Shorting and Nasdaq Level II: What to look for in your Level II box for shorts
- [TA for Shorting #1: Basic Short Chart Patterns - Identifying Intraday Sell Patterns](#)
- [TA for Shorting #2: More Chart Patterns for Shorting: Volatility and Volume Tracks](#)
- [TA for Shorting #3: Using Stochastic Reversals to identify short opportunities](#)
- [Sector Shorting: Identifying Weak Stocks in Weak Sectors, Using lead/follow stocks](#)
- Using the Market Indexes: shorting based on sector indexes, \$COMPQ and \$TRINQ patterns
- Risk Management in Short Positions: Where to Cover for Profit and Where to Use Cover Stops
- [Avoiding Common Shorting Errors and Mistakes](#)
- The Mental Game of Shorting: 5 Steps to Become Comfortable with the Whole Idea of Shorting
- Additional insights into Shorting Stocks using Nasdaq Level 2 and Chart Patterns





## Worksheets

[Click here for Powerpoint viewer program](#)

[Click here for MSWord view program \(3.5Megs\)](#)



- [Your Short Stock Trading Basket](#)
- [Short Trading Journal](#)
- [Finding Support & Resistance for Shorts](#)
- [Putting it All Together: Your Shorting Trade Plan and Skillbuilding](#)



## Activities



- [Your First 10 Open Shorts](#)
- Shorting the Lunch Weakness and Last 2 Hours' shorts
- Level II and Chart Shorting Activity
- [Making Shorts a Regular Part of Your Trading Skills - \*New!\*](#)

● **Main Points:**

- Many of you may have started off daytrading by trying to buy dips, buy bounces, and ride it on the way up for profits. This works, if you're using a cup reversal pattern etc, but the best trades are buying breakouts - not bounces.
- This lesson is designed to help you learn how to recognize 2-day breakout patterns for stocks by looking many different examples from mid-Jan 2001.
- The guidelines are simple, and they work. Here they are:
  1. Use a 2-day 2-minute chart to identify the previous high of the stock. By a 2-day chart, I mean look at yesterday and today so far. So, if today is Tuesday, set your chart to look at Monday's data and today. Trade with both a 2-day and 1/2 day intraday chart active.
  2. Draw a horizontal trendline straight across from the stocks' previous high. In the ITWO example below, that's about 57. whole number up from the previous day's high. In this case, that's "buy TXCC if it gets over 57 3/8".
  4. Your stop loss is at the whole number, so you never risk more than 3/8 on any trade. You trail a stop to lock in profits.
- The same strategy works (in reverse) for shorts, you simply identify the previous day's low, and set a short entry at below the whole number underneath this value. Say ORCL traded yesterday with a high of 40 and a low of 38 1/2. You would short ORCL when it loses 38, say at 37 5/8, on a breakdown.
- Why are these patterns so very important to recognize? Simple: because that's where many professionals (like myself) look to enter stocks, and this creates buying momentum.
- You can enter exactly over the previous day's high, but I prefer to wait just a bit to make sure the stock is safely over the whole number rounded up from the previous day's high. This is the same reasoning behind why we don't buy a stock at, say 39 5/8... it's right under 40 decade number resistance. Same with the 2-day plays, we want to time our entry to be rounded up over a whole number above the previous day's high.
- Some of the best strategies in trading are the simplest, repeatable ones that work time and time again. This is such a technique - it works very well, and is my #1 preferred entry on stock trades. Particularly when it's
- For an audio discussion of this and other techniques I've developed, [click this link](#) and then click the interview next to my name, Ken Calhoun, Daytrading University.

**Buying 2-Day Highs:  
Breakout Chart Patterns Made Easy**

These trades are best done during my favorite time of day to trade, from 9:40am til 11am, our "primetime" for daytraders.

**ITWO EXAMPLE:**

On the right, we see ITWO 2-day chart. The buy is right after the open, over the 57 from the previous day's high. You could have done this one twice, once for a quick trade on the open 57 3/8 to 58, the next time from the 57 3/8 on up to 60.



**EBAY EXAMPLE:**

Again, we see that a buy on the open at right over 52 3/8 or so would be fine.

Since we always trail a stop of about 3/8 (the same as our max. stop loss), we would be out from 52 3/8 up near 53 1/2 for this trade.

You could enter again over a cup breakout above the 54, say at 54 3/8, for a second trade in this strong stock.

Do not be afraid to "buy high" - your reason for buying is because you believe others are also buying, and will continue to buy, so you can sell to them later, for a profit.



**KLAC EXAMPLE:**

Here we see a breakout on the open over 44 3/4 or so. We'd enter at right over the 45, say at 45 3/8 on this trade.

Note that you can enter exactly over the previous day's high (where the 'buy here' arrow shows), we like to usually wait til over the previous whole number up over the high, which would be over the 45. Either entry is good.



**CMRC EXAMPLE:**

Alright, on this 2-day chart you can see consolidation towards the end of the first day, right under 32 resistance.

On the second day, we trade a breakout over 32 3/8 or so. We'd be out roughly even on the first attempt (stopped out even), and in for a good run on the second buy, which topped up over 34.

In our live trading room, we called this one for 3 separate profitable entries this morning on the way up to the 34 1/2 high in the morning session.





**EXTR EXAMPLE:**

Here's a final long example, EXTR. Our high is at the 48, a buy alert over the 48 3/8. It ran up a total of 4 points over this alert.

Trader's tip: if you miss out on the first entry, try a new entry one point up - say in this case you didn't get in at 48 3/8, you could enter again over 49 3/8 or the 50 3/8.

These two-day breakout cup patterns are very powerful and you should learn to master them in order to become a successful Nasdaq daytrader.



**Shorting 2-Day Lows:  
Using Breakdown Chart Patterns**

Here's the inverse of the above, learning how to short 2-day breakdowns. They are effective for the same reasons as the long plays, eg professional money moves a stock based on it making a breakout/breakdown over or under the previous day's high/low.

**TXCC EXAMPLE:**

On the right, we see TXCC 2-day chart in a breakdown pattern. The short is after an initial bear cup after the open, under the 50 decade support level.

Short TXCC under 49 5/8, trail a stop at 3/8 or so up from your original short entry.

This one would be covered initially at around 48 1/2 for + 1 1/8. If you are patient, or wanted to re-enter the position short later, you could make up to 3 points on it that day.



#### TQNT EXAMPLE:

Here's a nice volatile stock with good volume and short trading possibilities.

We see here that it bounced a number of times off of 38 support before finally breaking down to a low of 34 1/2.

The short entry is at 37 5/8, with a cover at 37 or so, for a +5/8 trade. You could short the afternoon breakdown as well, for a 36 5/8 to 35 short, another + 1 5/8 on it.



## Module Six

## Advanced Chart Patterns & TA

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MODULE 6



- Time of Day Reversals and Pivots

### • Main Points:

- To become skilled at day trading, you need to be able to anticipate time of day effects in the market.
- What this means is, you know already not to trade during the lunch dead time right? From 11 or 11:30 til 1pm is a slow time in the market, most often, and is a bad time to trade. What else do you need to know about time of day effects? Let's look at reversals.
- There are several phases of each market day. Let's look at the 3 that I focus on the most from 8:30 til 11:30 or so.
- Premarket: 8:30 til 9:30. Look for premarket gaps and overall breadth in the premarket trend. Are the sector leaders (MSFT CSCO INTC SUNW etc) getting buying, getting sold, or staying flat?
- **First Half Hour Reversals:** From 9:30 til 10, the COMPQ often reverses 2-3 times, usually around every 10 minutes or so, at 9:40, at 9:50 and again near 10am (give or take several minutes).
- 10:00-10:30am - Major trend is getting established by now. We also anticipate a reversal around 10:30 many times, particularly if the market's been selling, drifting down all morning, it will attract buyers frequently around 10:30 (also 12:30) for a "bounce".
- 11, 12:30, 2, 2:30 3, 3:30 ... all are also times where the market frequently pivots, or changes broad market direction.
- Watch the COMPQ, TRINQ and sector charts closely, eg SOX GIN GHA GSO etc to spot whether specific sectors are stronger than others, if there's convergence (agreement) or divergence among sectors, etc.



## Time of Day Reversals and Pivots You Should Know About

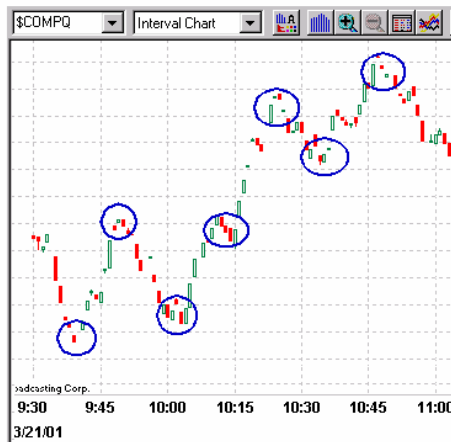
This lesson has many different index charts with the pivot / reversal times circled in blue for you to see.

The goal is to prepare you for trading "within the reversals" in the live market.

You need to prepare, for example, to enter and exit positions in a 5 to 8 minute round trip window for trades that you do from 9:30 til 10am daily.

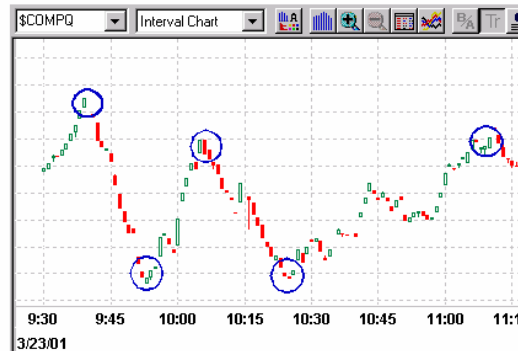
After 10:00 am, your trades may last a bit longer, as long as 15 minutes or so.

Let's take a look at the charts to the right. In this **first COMPQ half day chart**, you can see reversals at **9:40 9:50 10am**, followed by a pause/continuation up til **10:30**, then selling right before **11am**. Getting to learn this "pacing" is important, to help you from getting stopped out, or getting into trades too late into a given direction.



For example, if the market's been getting buyers from 9:30 til 9:38 straight, you probably are too late to get in for another long, over the 9:40-9:50 timeframe, unless the charts are making new highs etc. Plan your trades accordingly.

Here to the right is a **second COMPQ chart**, with our reversals spotted for you at **9:40, 9:50, 10:05**, and right before **10:30** again.



As you can see, you need to trade relatively fast if you trade the first half hour. The 9:30 to 10am timeframe is generally best left to more experienced traders (eg over a year experience).

There are plenty of profitable opportunities from 10-11, the next major wave in the market, and these should be looked at for continuation breakouts and bounce reversals to trade.

### \$GIN EXAMPLE:

In addition to the composite index, the \$COMPQ, you need to track at least 2-3 sector charts, such as the Goldman Sachs Internet Index, the \$GIN.

Again, you can see reversals follow the broad market, at the 9:40, 9:50 10:05 and right before 10:30.

**What should you look for on the sector charts?**

**Divergence, relative strength/weakness from one sector to another.**

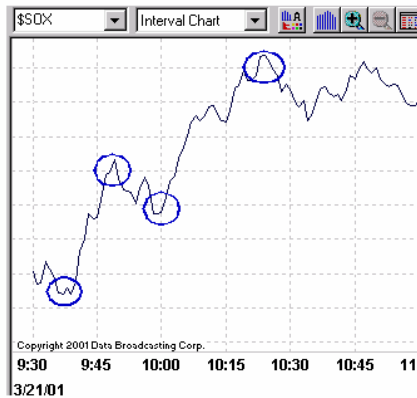
You want to see where the big money is moving: say out of internets and into semiconductors, the \$SOX... by spotting divergence across sectors, you'll be able to uncover trading opportunities that otherwise would remain hidden from view.



The sector charts are your first way to spot this. If for example the \$SOX is up +3.1% and the \$GIN is only up +1.8% on the day so far, at 10am, you would look for semiconductors to buy, eg KLAC VTSS XLNX, before you'd be shopping for internet stocks.

In the \$SOX chart to the right, you can see reversals, in the context of an overall uptrend. If you were looking to choose between nets and semis, using the \$GIN above and the \$SOX to the right, you'd be buying semis on any new breakout high, as they are stronger on the day.

If the biotechs, \$NBI, were say down -0.8% on the day, you might look to be shorting them on any sign of a market reversal downwards.



**Another \$COMPQ EXAMPLE:**

Here's another example, for the Nasdaq Composite, the COMPQ, to the right.

What do you notice about this chart?

We got initial buying in the morning, up to a top around 11am, followed by selling down into the fibonacci/50% retracement range.

How often does it reverse in a major swing direction from 10-11 vs from 11-15:00(3pm)?

You should notice that the volatility and reversals are fastest and strongest in the early part of the day, where most if not all of your trading should be done.



Let's look at this next example to the right. **What's different about its reversals,** from 9:30 to 12 noon, compare to the one right above it?

The selling is as strong as, or stronger than, the buying is, on the reversals. You can see this in the length of the downtrends after each wave of buying.

This should tip you off to the potential (which occurred) of more selling later in the day.

When looking at your reversals, take close note of the relative strength/weakness of the buying vs selling on each leg of the chart pattern.

Look for "which is dominant - buyers or sellers?". If the answer comes back "none-it's a choppy day" - then of course you know to trade more lightly, or not at all.

Your trading opportunities are more profitable when there's a strong trend in the market.



Finally, let's look at using the TRINQ reversals.

I often make note that the TRINQ is a very useful inverse indicator for spotting net buy vs selling strength, and for spotting market reversals a bit earlier than you see on the sector charts and composite index chart.

**\$TRINQ EXAMPLE:**

Although the TRINQ is useful say only 60-70% of the days for spotting reversals, it is always good for evaluating the net buying/selling strength in the market.

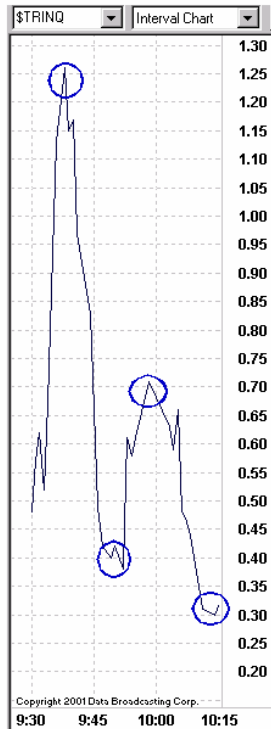
A TRINQ of 1 is "neutral", eg buy volume and advancers is the same as sell volume and decliners.

A TRINQ of 1-2 is modestly bearish, a TRINQ over 2 is very bearish, showing many sellers in the market.

A TRINQ of 0-1 is modestly bullish, staying down at zero to 1 etc shows buyers are in the market.

One advantage to the TRINQ is that it tends to move in pronounced levels, easier to spot big changes than in the sectors and COMPQ, on many days.

This makes it somewhat easier to spot if there are more buyers vs sellers in the market, and you should incorporate using the nasdaq trin, the \$TRINQ, into your trading efforts.



**Module Six**

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- Using Fibonacci Retracements for Intraday Range Trading

**Main Points:**

- Fibonacci retracements are useful to help you learn how to trade "bounces" and for managing trailing bounce play stops... they help you know "how much to expect out of a trade before it pivots". They are rough guides only, as every trade is unique.
- The basic idea is this: prices will tend to retrace only a portion of their first initial large move... not recover the entire movement. Eg VTSS may go from 40 at 9:35am down to 36 by 9:50am and bounce back to 38 by 10:15am, for example (not 40). This is a 50% retracement.
- Fibonacci values are useful in that they can provide rough estimates of where a price may move to, eg the support and resistance levels within a range.
- I use Fibonacci retracements ("fibos") as rough estimates to help me know when to start tightening up a trailing stop on an open bounce play, or, where to enter an open gap trade.
- Note that in time you should be able to "eyeball the chart" and see where the fibo values are. The primary ones are the 38%, 50%, and 62%, or, roughly 1/3 1/2 and 2/3 of the range.
- You can use Rick LaPoint's excellent "FibCalc" free program ([download here](#)) to help you identify specific fibo values within a trading range.
- Also, remember that bounce plays and retracements are lower - percentage trades than are 2-day high breakouts and 2-day low short breakdowns.

Here's what the FibCalc program looks like, I highly recommend it.

Symbol	Retrace	24%	38%	50%	62%	79%
AMGN	BOUNCE	52.49	51.25	50.25	49.25	47.82
LOW	T 24%	54.50	53.26	52.26	51.25	49.83
	A 38%	55.74	54.50	53.50	52.49	51.07
46	R 50%	56.74	55.50	54.50	53.50	52.07
	G 62%	57.75	56.51	55.50	54.50	53.07
HIGH	E 79%	59.18	57.93	56.93	55.93	54.50
	T 100%	60.99	59.75	58.75	57.75	56.32

**How to Daytrade using Fibonacci Retracements**

Here we see how to buy a bounce, and exit before it's "too late", for open profits.

Look at the fibcalc screen cap to the above right, I entered the initial values of 46 and 54.5 in it, you can see that the 50% retrace (the most important fibo to learn), is at 50.25, right near where it did, in fact, stop getting buying on the way up.

A classic textbook fibo bounce example.

**AMGN EXAMPLE (3/22/01):**

In this AMGN trade, we shorted all the way down to 46 in the TTO room, bought the long bounce starting at 46 1/2, and sold on the way up (twice) to under 50, where we closed out open longs.

See how the 50 price level is 1/2 the range of the 46 to 54 1/2? This is the most we expect from an initial long bounce. What it means is, you shouldn't be entering new longs close to the 38% or 50% after a stock has already been bouncing up, as it's likely to start turning down again.

The fact that it had bounced to near half the range on the way down was the exit target, eg the "max we expect from a bounce" on the initial bounce off a bottom.



**AMAT EXAMPLE:**

I want you to get used to thinking in terms of range retracements, as we see here in AMAT.

Stocks often make a major multipoint move, then retrace (go in the opposite direction) for up to half the initial range, before a reversal or consolidation occurs.

In AMAT here, you can see it ran from 46 to 47 3/4 (initial large run, almost 2 points), then retraced to 46 3/4, roughly half the range, before getting buyers back.

How does this help you? You need to learn the fibo ranges and pivots to manage your trades and get ready for new breakouts, and to trail close stops to lock in profits, on open trades that are "in the money"



**MLNM EXAMPLE:**

Here's another example, in the other direction, MLNM sells off, then bounces to roughly half the range, before consolidation, running out of buyers.

What this type of pattern means is:

- 1) The next time you look for a bounce play, you do not enter if it's already retraced 1/3 or 1/2 of it's range. In this example, you could have bounce 27 3/8, sell up near 27 3/4 or 28. You would not be a buyer at say 27 3/4 or 28, as it's "too late" for a bounce entry.
- 2) Once in the bounce early, you trail closer and closer stops the nearer you get to 1/3 or 1/2 of the range on the upside. So, if you're in from 27 3/8 and it gets to 27 7/8 here, then starts to fade back to the 3/4, you can go ahead and exit, to take your 1/2 point on the trade.



**Bonus Play: Open Gap Retracements**

Remember how we said that large (over 8-15%) premarket gaps are good plays on retracements?

Here's an example to cover how to use fibo ranges with the gaps.

**GMST EXAMPLE:**

On the right, we see GMST 2-day chart in an open gap up selloff pattern.

A short on the open, say at the 34 5/8, is covered before we get to the midrange. In fact, we tighten up our stops as soon as we get to 1/3 of the range... in this chart, that's near 33 5/8 or so.

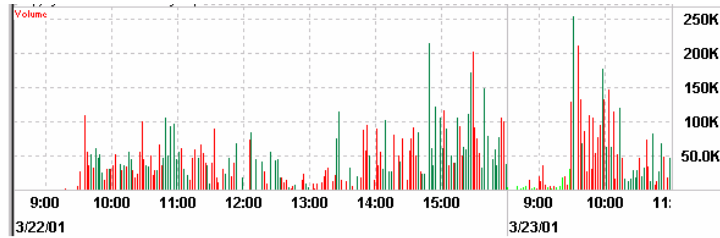
Covering out near the 33 1/4 yields a +1 1/4 point trade.

We do not expect it to sell all the



way back down to the previous day's close, eg at the 29 1/2, we look to cover as it approaches the midrange, at around 32 1/2 to 33.

You can see that GMST bounced a couple of times off this 50% fibo retrace area, at 32 1/2.



## Using Fibo Retracements with the \$COMPQ, \$GIN \$SOX etc...

Finally, let's look at how to use fibo retracements, expectancies, pivot areas, with our indexes and broad market indicators, like the sector charts (\$SOX \$GIN) and the Nas composite, \$COMPQ.

### \$COMPQ EXAMPLE:

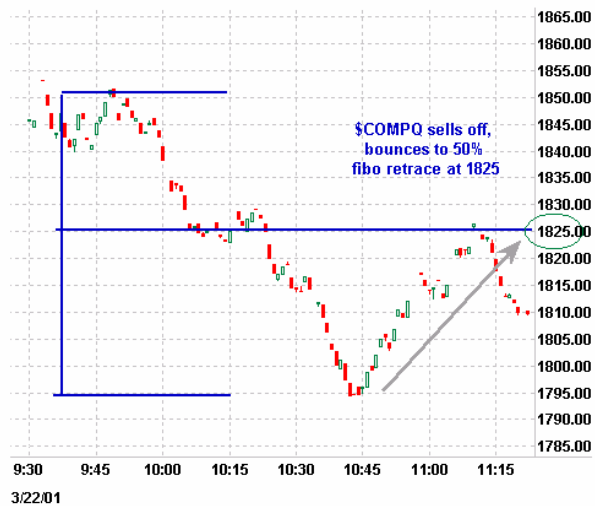
As always, the main point of using fibo retracements is to help us map out likely areas where a bounce or drop will retrace, after a large initial move.

In this \$COMPQ example, you can see the index dropped from 1850 down to 1895, then bounced back up to roughly half the range, at 1825.

How to trade with this? It tells you a couple of things:

1) Don't enter new longs if you're close to the midrange on the bounce, as it's likely to stall out here.

2) If you're in on long bounce trades, look to trail closer stops and exit with an open profit as you reach the 38%/50% fibo retracement areas.



### Closing Comments: Fibonacci Retracement-Based Trading

Think of stock prices like a spring, that has a certain "stretch" to it, then bounces. Or, a ball that drops, bounces to a part of it's former height, then drops again.

In using Fibonacci retracements, you should be aware that the price will always double back on itself, always make pivots, at some point in time.

My primary use of fibos is to help me get out of bounces before they turn back against me, and to identify rough areas where I should begin tightening up my trailing stops to lock in profits. They also help me avoid poor entries, as I will not enter if it's already near a fibo retracement area... eg I would probably not enter new long positions if the COMPQ was at 1820, right under the 1825 previous consolidation/fibo retrace area.

Best wishes, and remember - bounce plays are Lower Percentage trades than are 2-day high breakouts, so, trade them carefully.





• **Main Points:**

- I've put together a solid comprehensive reference of the most important bullish long candlestick chart patterns you should learn in this lesson.
- The primary value of candlesticks to the daytrader is to be able to spot when reversals are beginning to occur.
- Reversals, also called pivots, are important to be able to spot early, before the crowd does, for two types of trades, when trading long:
  - 1) When protecting an open profit, you want to trail a close stop, and look to exit on any sign of weakness in the chart patterns. Candlestick patterns can tell you when buyers are done, and sellers are starting to come into the stock (eg dojis and others).
  - 2) They are also good for "bottomfishing" as a second indicator, beyond cup pattern reversals and volume reversal patterns. You look for signs like hammers and dojis at the bottom of a cup, before buying the breakout over a new whole number to the upside.
- Time interval for candlesticks: since my roundtrip trades can last from 3 to 15 minutes or so, I need to use fast candlesticks, and prefer 1-minute candles. Note that you will need to limit your chart timeframe to the 8:30am til 12 noon timeframe, to be able to clearly see the candles, when using 1-minute time intervals.
- You should experiment for yourself with 2-minute and 3-minute candlesticks.
- Add stochastics, MA lines and volume to help you with your candlestick charts.
- I have not found candlesticks useful for things like risk management, other than to alert me to possible tops, for open long positions. You need to use time & sales and level 2 for close risk management. The candlesticks are used to get you into bounce trades, and to get you out of open profitable positions, when you start to see reversal patterns occurring.

**Bullish Candlestick Patterns to Go Long With**

**Bullish Candlestick Pattern #1:**

**the HAMMER**

Not the MC type, this is instead a reversal pattern, similar to the doji (to be covered below, next) that shows a possible top or bottom after a sustained run in one direction or the other.

**XLNX Example:**

You can see here the hammer I've outlined at 10:38 or so in the stock.

It looks like the letter T with a small body at the top. The inverse pattern is good for tops (and is covered in the bearish candlestick lesson).

As the name implies, it looks like a small sledgehammer. The buy here using my strategy would be buy over 42 3/8 (with a stop loss at the 42), and an initial exit at around the 43 1/8 or so.



### YHOO Example:

I've highlighted a hammer in YHOO for you on the open, right after 9:30am.

The other pattern I've highlighted is a candle (spinning top?) that looks like a doji, as the stock is reversing back to the upside.

Learn to follow the hammer as an initial indicator that buying has resumed in the stock, for the bullish hammers we've shown in these two examples.



### Bullish Candlestick Pattern #2:

#### the DOJI

A Doji is a + type pattern, and can look like one of three candles, as you can see in this EBAY example's notes to the right.

#### EBAY EXAMPLE:

The thing I want you to spot in this EBAY bounce play is the doji where I've highlighted it and drawn an arrow to it.

Do you see the small red doji at the bottom? It looks like a plus sign. Don't let the color of the candle, for dojis or hammers, make a difference, the main thing is the size and relative position of the candle to the preceding and following candles.

Here the buy is over 42 3/8 after spotting the initial doji. On dojis, remember to not buy the doji just because it looks like a doji, you need also a cup pattern and for it to clear the whole number above the doji, and also to watch volume and time & sales.

These indicators are all meant to be used together.





#### QCOM EXAMPLE:

Here you see the doji at the bottom, followed by a nice volume spike on the upside.

This is a good entry, and you can see we got to over 65 from a 63 3/8 entry before buyers slowed down.

Good example, it followed a multipoint drop and had a volume reversal to confirm the entry, after the doji appeared.

### Bullish Candlestick Pattern #3: the MORNING STAR

A morning star is a consolidation and bounce pattern using 3 different candles in a row. It's a bit tougher to spot at first, since there's a sequence of 3 candles off a bottom you're looking for.

#### ITWO EXAMPLE:

You see one red candle on the way down, a candle with higher/lower tails, followed by a bullish candlestick in green on the way up.

The entry is over the highest part of the middle (reversal, red in this example) candle, and we'd wait til it clears the 30 3/8 decade and whole number level for an entry.



## Bullish Candlestick Pattern #4:

### the BULLISH ENGULFING

Bullish engulfing patterns are easy to spot.

You are looking for a sequence of two candles in a row, one red one that is followed by a larger green one.

The green candle has to have a high and a low that is higher and lower than the red candle preceding it. In other words, the range of the bullish green (2nd) candle needs to be larger than the sell range in the red candle.

#### VRTS EXAMPLE:

Here you can see two things I've highlighted, the first is 2 doji-like candles that were Not a bottom (so we'd have to stop out on this first attempt).

The bullish engulfing pattern is following it, you can see the red candle at right after 10:30 am followed by the green, larger candle.

The correct entry on this is over the 57 3/8 previous support, over the whole number above the first 'engulfed' candle.

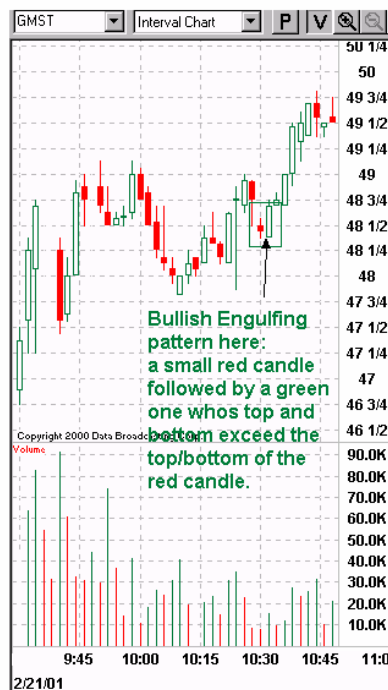


#### GMST EXAMPLE:

Here's one more bullish engulfing candle pattern to study, right after 10:30.

The small red candle is followed by a larger, engulfing green candle, showing that buyers are strongest.

In this example, I would wait for it to clear the whole number and previous high, eg buy right over 49. If time & sales is strong. However, I usually do not buy 9s, particularly under a decade number, so the best trade is to wait for it to clear the 50 3/8, later.



## New- Pattern #5: 3-LINE BREAK

The final type of bullish pattern I'm covering here for now is what's called a "three line break". This is where you have three successive green candles in a row, each one that has a higher low than the previous candles' highest high.

When you are in a profitable open long, start getting ready to sell at the top of a 3-line break, as it's a pattern other traders also look to sell the top of.

### MLNM EXAMPLE:

We see the bullish engulfing pattern here right after our 10:30 bottom. This is the buy signal, eg over the 27 3/8 or so.

The three line break you see, the second box, is great - we're in with a nice open profit. However, you look to exit at the top of a 3-line break (or sooner, of course, depending on whether your trailing stop gets taken out).

At the top of the 3-line break you see a doji-type candle occur, so we exit as it starts to grind down to the 28.

Another winning trade.



**Module Six**

## Advanced Chart Patterns & TA

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• [Bearish Candlestick Chart Patterns to Short](#)

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MODULE 6

### • Main Points:

- As with the bullish patterns for longs, here I've put together a solid comprehensive reference of the most important bearish short candlestick chart patterns you should learn.
- You will become familiar with these patterns in time, and can use them to aid you in getting out of long open positions with a profit, avoiding initiating bad new long positions, and for entering short positions.
- Thus, there are several reasons why you should learn both the long bullish and short bearish candlestick chart patterns explained in these practical lessons with recent examples.
- Experiment with different time intervals on your candlesticks, you can try 1- 2- and 3- minute candles, along with stochastics (15/5/3), volume and other indicators.
- One of the difficult tasks facing new traders is the idea of learning to interpret price data with the somewhat-intimidating or unfamiliar candlestick notation.
- Reading more about candlesticks (eg Nison et al) and comparing the patterns in your charting software will help.
- To compare what a chart looks like in bar, close line, and candlestick format, use one stock you are familiar with and switch back and forth between these different types of charting in your software.
- You will find that different data is good for different purposes, ie I use close line 1-min thumbnail charts to scan the market (as many as 20-40 open at once), and use a large (2/3 of one monitor) 1-minute candlestick chart to get more in-depth information for a specific stock I'm looking to trade. Thus, you use the different types of charts in combination with each other. See [this link](#) for my 6-monitor setup example.

## Bearish Candlestick Chart Patterns to Short

### Bearish Candlestick Pattern #1:

#### the HAMMER

A Hammer shows that traders started the stock off in the immediate prior trend, continued, then started / closed at a reversal.

#### LLTC Example:

See the hammer pattern here as the stock starts to sell down from the 42 1/2 level. This is an "early warning sign" and can be used to initiate a short or to exit a long position with profits.

It looks like an upside down letter T with a small body at the bottom. This pattern is good to help identify tops.



### Bearish Candlestick Pattern #2:

#### the DOJI

A Doji is a + type pattern, as you can see in this XLNX example to the right.

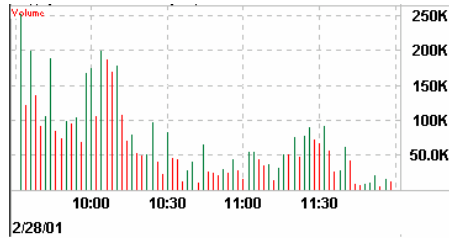
#### XLNX EXAMPLE:

See the doji where I've highlighted it and drawn an arrow - XLNX is putting in the top right under 40 decade resistance after a nice run up over a bullish cup pattern over the 38..

Do you see the small red doji at the top? It looks like a plus sign. Any open long would have a trailing stop up here near the 39 1/2, the doji may signal you to get out here. You could rebuy if it broke over 40 3/8 (it didn't) or short if it lost the 39 1/2, which it did.

Quiz: What's the pattern you see in the candles right before 11:30 in this XLNX example? (answer at bottom of page)





**BRCO EXAMPLE:**

BRCO is usually a bad stock to trade, however on this week it had good trading volatility, so we played it.

Do you see all 3 dojis where I've outlined them for you here on this intraday chart?

Important: note that dojis may not always signal a reversal, you need to use other indicators to help you manage your positions when daytrading with candlesticks. Of course the most important is to use a close stop loss, no more than 3/8 of a point ever on any single position.

In these examples, the dojis followed through nicely, showing us where the price was turning.



**Bearish Candlestick Pattern #3:**

**the BEARISH ENGULFING**

Bearish engulfing patterns look like two consecutive candles, a green one followed by a larger red one

The red candle has to have a high and a low that is higher and lower than the smaller green candle preceding it. In other words, the range of the bearish sell (2nd) candle needs to be larger than the buy range in the green candle.

**KLAC EXAMPLE:**

There's two bearish engulfing patterns in a row here on the KLAC example... our sell/short signal is when it loses the support at 38...

We enter short as soon as it loses the 37 5/8, and trail a stop down to 35 1/2 or so, for a +2 1/8 possible win.



**HGSI EXAMPLE:**

Here's a variation of the bearish engulfing pattern, a wide range candle pair at a top. It still meets our criteria, eg the sell bar is larger following the buy bar, at the top.



**AKAM EXAMPLE:**

Here's a final bearish engulfing candle pattern to study, you can see the red candle "engulfing" the previous green candle here right after 10:15.

Shorting tops like this is for experience traders only, new traders should simply learn these patterns to help you get out with a close trailing stop, to maximize your profit on each trade.

Use the candlestick reversal patterns as an early warning sign to help you close longs before they start selling down.

Experienced traders may consider selling open long profits and then shorting on an uptick following one of these patterns, provided close 3/8 stops are used.





## Bearish Candlestick Pattern #4:

### the 3-Line Break (down)

The final type of bearish pattern we'll discuss is the "three line break". This is where you have three successive red candles in a row, each one that has a lower high than the previous candles' lowest low.

#### AMAT EXAMPLE:

Here's an example of a bearish engulfing pattern right before 10:30, followed by 2 more down candles.

The stock consolidates over 43 for awhile before breaking down, the short entry signal is when it loses the 43, say at 42 5/8 or so. A trailing stop would have us cover out at 41 1/2 for + 1 1/8 profit in the trade.



#### ONIS EXAMPLE:

Here you can see a two-day chart, we have another 3-line breakdown under the 2-day low.

This is often a good confirmation that the stock will continue selling for awhile.

One challenge is getting a short off into the sellers, you may need to try several times (eg keep hitting the short button til you get a fill, don't chase more than 1/4 of a point or so).

You can see that ONIS here sold all the way down to 34 1/2 before reversing, for a nice multipoint gain.



quiz answer: bullish engulfing



**Main Points:**

- Stochastics are useful in helping primarily to determine potential pivots, or reversals, in a stock's current trend.
- They are considered of secondary importance to help decide whether or not to enter a position, as is level 2. Many new traders do not know how to "weight" the importance of the different indicators in helping make trade decisions. Remember, the chart patterns and time & sales are the 2 most important things to pay attention to. Stochastic bounces, level 2 patterns etc are of secondary importance.
- Having said that, there is still, of course, a place for stochastics (or "stochs" as professionals call them) in our trading toolkit.
- Also, you set parameters such as %K/%D in stochastics, I recommend 15 as the step (for esignal users), other programs, use 15/5/3 (15/5) for your parameters.
- We look for one of two patterns in using stochastics: "Oversold" and "Overbought."
- OVERSOLD: When looking to either a) cover shorts or b) enter long bounces, you can look to whether the two lines of the stochastic have dipped below 10-20% and have crossed over to the upside. This may be an indicator of "oversold" in the stock, and, when used with other data (eg bullish cup reversal patten, volume buying, doji candlestick, time & sales hitting the ask, etc), can indicate a potential good long entry.
- OVERBOUGHT: When looking to either a) exit a long position or b) initiate a new short, you can look to see if the stochastic lines have gone over 80-90% and are starting to crossover to the downside. Again, use other indicators, this is a TA indicator that is part of a "team" of indicators you need to use simulataneously to correctly gauge entries and exits from your positions.
- Let's take a look at quite a few good chart pattern trading examples below.

**OVERBOUGHT STOCHASTICS:  
Time to Close Open Longs,  
Possible new Short Entries**

Stochastics give us an early, almost lead-indicator type warning that a stock is about to sell back down. Remember to always use trailing stops, eg if you were in from 63 3/8 here, we'd trail a stop and be out at 64 1/8 or so on the way up for a +3/4 trade in VTSS.

**VTSS EXAMPLE:**

On the right, we see VTSS intraday chart, with two overbought stochastic crossovers clearly labeled for you.

Notice that in both cases, they go near 80-90%, a potential overbought signal, and cross over to the downside.

You should be able to clearly see the red and blue lines cross over where I've circled them in the lower part of the chart to the right, yes?

I have also circled the corresponding "tops" in the stock price chart in the



upper half, you can see the clear indication of the stoch crossovers and the resulting drop in the stock price shortly thereafter.

This is not a crystal ball indicator however, and stochastics are right maybe 50-60% of the time only, so, a word of caution to use them as a secondary indicator in your trading. They are often right enough to be worth paying attention to, but you need to integrate several buy/sell signals and trailing stops etc into your trading style to be effective... so, don't over-rely on stochastics, or level 2, to help with your trading.

**ALTR EXAMPLE:**

Here you may see another example, of ALTR, with our stochastic overbought signals circled for you to learn from

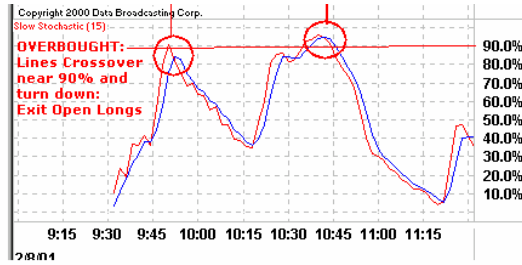
The best signal is after it rises all the way up to near 100%, and then crosses over, to the downside, right after 10:30 am.

I've also put a horizontal red line on the chart for you to see the key price level, 27 3/8, for this stock on this morning... this is the reversal line.

The first stochastic crossover, as you can see, would get you out, probably incorrectly, as it only pulled in 1/4 point before making a cup breakout to the upside, for a 3/4 point run, before our second stochastic told us the stock was overbought up here.

This is another tip to learn: I personally like to use stochastics mostly for exit signals (as I do with level 2 bands), vs. to decide to enter a stock long.

However, there are times where oversold stochastic bounces are good. Note that these are for more experienced traders, I provide some good examples in the charts below.



**OVERSOLD STOCHASTICS:  
Time to Initiate Longs, one  
signal of several to use**

Here's the inverse of the above, learning how to buy bounces on stochastic reversals. Again, these are not highly reliable if used by themselves, I prefer to buy cup breakout patterns... or, bounces off of multipoint selloffs after we get a volume bull cup reversal to the upside. The stochastic crossover can provide a key as to when to cover a short in these examples, or for new long entries.

**NXTL EXAMPLE:**

On the right, you see a bounce in NXTL off the bottom at 34 5/16.

Do you see the stochastic crossover where I've circled it in the lower half of the chart?

We see it's dipped under 20% and is reversing to the upside.

This trade could be good for up to a point from 34 3/8 to 35 3/8.



**AMAT EXAMPLE:**

Here's a good volatile example using Applied Materials, AMAT, a perennial daytrader's favorite.

This nice chart pattern yields both good examples of long stochastic bounces off an oversold bounce, as well as a "get out here" signal when it crosses over and loses the 90% after 10:30 am.

Again, we look for the signal lines, the %K/%D, to cross over under the 10/20% to the upside, as our first potential indicator that buyers are in the stock.

Rely more on the time & sales, once you see a stoch crossover, to let you know if a long play is worth trying. What's the net action in the stock - more buyers or sellers, or mixed? Stay out as long as the t&s shows a christmas tree-like green and red pattern. Instead, wait for it to move in favor of buyers, and begin to look at level 2... if there's no heavy INCA or "heavyweight mm" (MLCO MSCO SBBSH etc) selling, then you may want to consider a long entry.

These indicators create a system you should pay attention to - they are NOT meant to be used in isolation from one another. Be looking at the TRINQ, the sector charts, the COMPQ, etc when making trading decisions. And always hold yourself to 3/8 max stop losses.



**NUAN EXAMPLE:**

Here's a super strong cup breakout following a stochastic bounce to the upside in NUAN, good for a multipoint run.

NUAN is an unfamiliar ticker to me, to this day I still have no idea what they do. All I know is, it comes up on my scanner, it meets my minimum-volume requirement (eg over a few hundred K shares on the day so far etc), and I look to trade it.

This example isn't really a stochastic bounce to the upside, but it did provide a crossover signal to get over the 20% right after the open, at 9:40, so, it catches my attention.

The cup breakout pattern over 38 3/8 is a confirmation that a long trade is good, and we're off to the races on this one.

Trailing a close stop of 1/4 to 3/8 point is always a great idea, and we can either a) sell under each whole number at the 15/16 or so, sitting out the whole number resistance, re-entering right over ,at the 3/8 again, or b) use a trailing stop to keep us profitable all the way up to 41 3/4 or so from a 38 3/8 entry.

So, in summary, use stochastics as part of your trading decision criteria, and look for other indicators to help confirm your entry.



**Module Six**

**Advanced Chart Patterns & TA**

◀ PREVIOUS NEXT ▶

- Recognizing Breakouts and Breakdowns: Trading Consolidation Pattern Breaks

Back to MODULE 6

• **Main Points:**

- The most important patterns to recognize are **bull cup breakouts**. Following this, we have technical **uptrends** (higher highs, higher lows, making bull cup breakouts on the way up).
- Next, we have **consolidation breakout** and breakdown patterns. Let's start by figuring out how to spot a consolidation, and what it is.
- Consolidation: an area on a chart pattern, typically lasting from 15 minutes to several hours, where the stock is basically "flat" in a narrower-than-usual trading range.
- For example, if YHOO as a \$40 stock has a 3-point average daily trading range, say goes from 37 1/2 to 39 3/8, then trades narrowly, chops, between 39 and 39 7/8 for the next hour, we say it's "consolidating", eg no trend is seen, it's in a narrow trading range. Your goal is to trade the breakout above/below the consolidation area.
- Note that this is for a narrower-than-usual range, you need to first recognize the difference between stocks that are just chopping around in their average trading range vs. when they're in a narrow range, one that can yield good trading potential once a breakout occurs.
- First, you need to use your two-day chart and draw horizontal trendlines from the previous day's high and low.
- Next, draw trendlines to define the current narrow consolidation range the stock you're watching is in, for today's trading. The best consolidations to trade are those that are right under the 2-day high line (for breakouts) and right over the 2-day low line (for breakdowns). Do Not trade a stock that's in the middle of its two day range.
- Finally, decide where good trade entries would be. Personally, I like to buy right over a whole number breakout near the 3/8 on a new 2-day high. In the YHOO example, we'd buy once it clears the 40 3/8. The 39 7/8 is the temporary "top of the consolidation", we wait for it to get over decade resistance and a 2-day high, to buy over the 40 3/8.

## Recognizing and Trading Consolidation Breakout Patterns

First of all, let's start with the basics: I want to show you how to recognize a consolidation pattern on an intraday candlestick chart.

You are looking for a series of tops and bottoms, over a 15 minute to several-hour time frame, where you can draw consolidation lines, the trading range.

You never want to guess the direction that a breakout will occur in, it can easily go either way.

Instead, you want to prepare to enter a trade once a support/resistance level has been penetrated to the upside (for a long) or to the downside (for a short).

Your stop loss, as always, must be no greater than 3/8 of a point on any singly daytrade (regardless of the number of shares you're trading).



Itty bitty chart example: see where the upside breakout occurs above the consolidation lines I've drawn?

Tip: oftentimes, I've seen cup patterns on the open, and consolidation breakouts/downs after the lunch, in the afternoon session. Look to play cups in the morning, consolidation breakouts/breakdowns if you choose to trade the afternoon session.

### GSPN EXAMPLE:

Here you can see where I've drawn the consolidation/cup pattern lines for several distinct trading waves for this GSPN chart.

The first is roughly 30-31, the next, from 33 to 33 1/2 (nice tight range), the third is 34 1/2 to 35 1/2.

What does this tell you?

To trade in the direction of breakouts that occur once the stock has started to make it's move.

Another tip: watch volume for these plays. In the first example, you can see volume picked up right after 10:30, as the stock started to slow its upwards movement.

This change in volume tells you to exit with profits, if the stock has started moving. In the first breakout example, it could easily have dropped back to 31 1/2 or so after its initial run. At 10:45, after drawing the initial lines, you should say to yourself, "Ok it's ran up some here, I'll short it if it loses the 33 support, or go long if it gets over 33 1/2 or so".

Can you see where the consolidation ranges are? That's the most important thing I want you to take away from these examples: to be able to draw the lines where the support and resistance, congestion areas, consolidation, occur, so you can prepare to trade breakouts successfully above/below these areas.



## Shorting Consolidation Breakdown Patterns: Lunchtime and Afternoon Session Shorting Explained

Okay, here's a fairly heavily annotated VTSS chart (I like it, and XLNX KLAC ALTR NVLS etc for \$SOX semiconductor sector trading).

Don't let it scare ya, let's learn from where I've made some notes to help.

**VTSS EXAMPLE:**

On the right, you see three distinct trends in VTSS this day:

1) The initial uptrend, made an ascending triangle and a breakout over 69 1/2.... in my trading style, I'd have us buy 70 3/8.

2) For the next several hours, VTSS then traded in a consolidation range, from 71 3/4 to 72 3/4. This is where Not to trade it. Instead, you get ready to trade it once you've identified these support/resistance levels. Again, at say 14:00 hours, 2pm, we have no idea as to where it's going, only that it has a slight downside bias since it's retested the bottom of the consolidation like (a triple bottom) vs testing the topline. So, we get ready to short.

3) Finally, we have a trade in shorting VTSS once it loses 71 3/4 or so at right after 15:00, 3pm EST. It lost a point and a half, for another decent trade. We'd have our initial cover stop target at near the open breakout, at the 69 3/4.

The two black ovals show where profitable trades are executed, over the triangle breakout on the open, and a short under the consolidation area later in the session under the 71 3/4 line.



These chart patterns are daytraders' favorites, and you should learn to trade them. You should anticipate getting shaken out on wiggles initially, say the first few months, as you master order entry and stop loss management.

I've found that "good trades are usually good right from the start", so, if in doubt, get out, and always always keep losses to a minimum, even if it means stopping out once and re-entering a second time, for example, to get the winning trade.



● **Main Points:**

- Note: New traders should not day trade until after 10am. This is because we often get reversals every 8-10 minutes or so, eg at 9:40, 9:50 and again at 10am. You need to be able to execute your trades in a 5- to 8-minute round trip timeframe, which is usually too fast for new folks to keep up with.
- After you've mastered 2-day breakouts, you can attempt more advanced techniques like buying bounces on reversals and playing in the first 30 minutes of the regular session.
- This is a very volatile and active time to trade. Often you will see buyers from the premarket continue to push the price up until 9:35 or 9:40, at which time professionals are shorting, you see the stock start to sell back down, "losing steam". This is often referred to as a gap n trap, a misnomer, it is actually just the slowing down of public order flow into the open.
- One key to success in trading the first 30 minutes is being able to master order routing. Most of my trades are done via ISLD, also I'll use SOES Limit orders if there are temporarily no ecns on the inside. Since you're experienced, eg you're trading this timeframe, this should be little problem, and you know, of course, not to use your brokers "smart" order routing, instead preferring the direct control you can exert over routing your order to the exchanges.
- The basic pattern that we need to master for trading the first 30 minutes is micro-cup patterns, eg bullish cup patterns that we trade closely, tightly, using 1-minute charts and time & sales, into the open.
- We can also trade open gaps in the direction of a continuation/reversal, depending on the chart pattern.
- Both are potentially profitable for the decisive, fast, experienced trader.

**Cup Pattern Breakouts in the First 30 minutes: 9:30-10am Pattern Trading**

Cup Pattern Breakouts are excellent since they keep us away from risky "guessing" about a stocks' bottom or breakout, we have waited until buyers are definitely back into the stock before entering a new trade.

**TQNT EXAMPLE:**

Here's a cup pattern breakout; note that you Do need premarket charting ability to trade the first 30 minutes. This is one reason I like esignal.com (I think rtlll may offer it as well, you need to check).

Notice that the stock opened at right under 18 premarket, sold down to 17 3/4 at around 9:35, came back over the 18 around 9:40, and started to breakout around 9:50 or so.

The trade is to buy 18 3/8 at around 9:50, and be ready to close the position no later than 10am, or when your trailing stop (which needs to be close, 2 spreads or so on these) is hit.



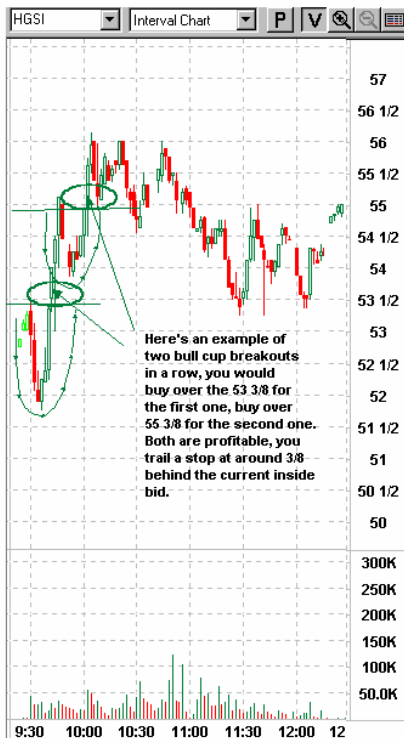


**HGSI EXAMPLE:**

Ok I've even drawn the cups for you to see in this one, it sold down and recovered two times, you could buy either breakout.

Note that the first breakout is usually the strongest, best one to buy, and that subsequent "cups" should be looked at with an increasing degree of skepticism re: follow through.

Many new traders fail to act on the first trade signal, then watch it run up, then try to get in on the 2nd, or later, lower-probability trade. This is an error. You need to be in early on good trades.



**SONS EXAMPLE:**

Here's a 2-day chart of SONS, the main thing to look at is the start of the second day, where I've annotated three trade signals that were generated.

Noting the previous day's open/high/low/close proves useful to us, as we buy the first micro-cup over a bounce over the previous day's support, at 28 1/4 or so and again over the 29 3/8 2-day high. The third trade is over the 30 3/8 decade resistance.

Can you see the patterns in the candlesticks here?

You are looking for U-shaped cup breakout patterns throughout the first 30 minutes, for fast profits.



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## Bottom Fishing in the First 30 minutes: 9:30-10am Pattern Trading Play #2

Another favorite opening play is the fast bottom bounces, on cup reversals.

### QCOM EXAMPLE:

On the right, you see QCOM making both of these trading patterns:

1) An initial bounce over 53 3/8 for a long, we look to sell out around 54 1/2 or so into the fibo 50% retracement of the selling down.

2) We also buy a new high of the day on a cup breakout, over the 56 3/8, trailing a close stop. We would be out the first time at 57 for +5/8, and out the second time at around 57 5/8 for +1 1/8 or so.

The stock gets up to 58 before getting sellers, you can see a small green doji up at the top, near 58, before QCOM heads back down.

Several good trades to be had in it.



## Open Gap Trading in the First 30 minutes: 9:30-10am Pattern Trading Play #3

Remember how I always talk about stocks that are gapping over 8-15% on volume over 20-30K premarket are worth watching for a trade?

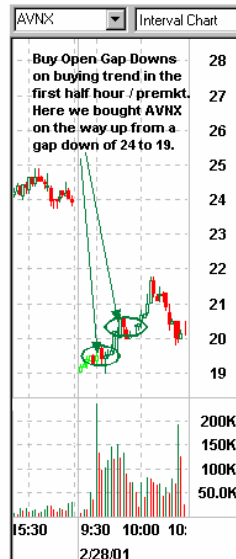
We need to remember that we usually buy gaps down and short gaps up, when they are large. But, we wait for confirmation of the reversal before getting in. As an example, QCOM gapped down, and kept selling all morning (at tradingtheopen.com we shorted it 5 times on the way down :).

Here's an example of a gap down and long recovery (we traded it twice on the way up long at tradingtheopen.com for nice profits).

### AVNX EXAMPLE:

Take a look at AVNX here, a nice large multipoint gap down, to right over 19 premarket. We buy on strength once it clears 19 3/8, and again over the 20 3/8 decade resistance, for nice long wins.

You will notice that most of the profit potential occurred from 9:30 til 10am.. this is common for gap retracement plays, so, you need to be fast to trade these.



### HGSI EXAMPLE:

Here's a good look at a gap continuation (not reversal) play: HGSI gapped up from 49 to 51, then continued on up.

We are cautious about buying a gap up (instead, usually looking for a short entry), so we set our long entry a whole point up above the gap value, at 52 3/8 for a long.

Guess what? It runs, our trailing stop keeps us in til 53 5/8, at which time we sell, taking a healthy 1 1/8 point profit long before 10am occurs.

So, we need to look for cup patterns to tell us to get in on a continuation or reversal, and play in the direction of the trend in a timeframe of up to 10 minutes max for the round trip, during trades we fill during the first 30 minutes of the trading day.



## Module Six

## Advanced Chart Patterns & TA

◀ PREVIOUS NEXT ▶

- "Hanging on a Cliff Ready to Drop" Short Chart Pattern Tips

Back to  
MODULE 6

### • Main Points:

- This is a combination of using consolidation and bear cup breakdowns, most frequently following a large rise in a stock price, as it attracts sellers.
- As this is the opposite of trying to "catch a falling knife", it's for experienced traders (over 1-2 years profitable fulltime experience) only, as we are shorting the first sign of weakness, after a breakdown technical signal.
- I have included a good number of chart pattern examples here below to help you spot these trading opportunities.
- The best time for these is, as always, following a 2-day low breakdown. The riskiest is following a multipoint run to the upside.
- If you're good, you can catch a reversal and profit on the way down, the "other side of the mountain".
- If you're not good, you can get caught in a continuing uptrend, and suffer a "short squeeze". As always, you need to know how to properly use the L2 and time & sales tools to manage these trades correctly.

## More Shorting Breakdown Patterns: DTU "Hanging on a Cliff" short plays for experienced traders only

"Hanging on a Cliff", means, the stock is approaching a breakdown under a support level. Learn to identify these, both to exit profitable longs (using trailing stops) and to enter new shorts, the subject of this lesson.

**NVLS EXAMPLE:**

On the right, we see NVLS intraday chart, with a consolidation area, very tight, from 41 1/2 to 42 for much of the trading day, after an initial run up.

Note that we'd need to try this trade twice to succeed, as we got stopped out on the initial loss of 41 1/23, around 11:20, and made the big profitable short in the afternoon, shorting right after 13:00, 1pm, EST.

Our cover target in this is right over 40 decade support, we can re-short once it loses the 40, but the best trade is to be out at say 40 3/8 from the 41 3/8 short entry.



It's usually good to choose stocks with high volatility for these plays.

**INTC EXAMPLE:**

Although INTC usually isn't volatility, it led the way in a chip selloff on Feb 13th, 2001, in the afternoon, and was a profitable short under the 34 "cliff"...

Here you see INTC breaking down and losing the 34 morning support around 1pm, 13:00, where it gave us our first short alert.

It's important to be able to identify the consolidation support/resistance levels, the "hanging on a cliff" is where it teeters, before finally giving in to selling pressure, which takes it back down.

Initial exits are always near the morning's open, if we're selling a large bear cup pattern (eg we short the right side of the cup, once it loses support).



## More Shorting Breakdown Patterns: DTU "Hanging on a Cliff" After an Open Gap Up Chart Patterns

Here's an advanced variation using both our "short open gaps on any sign of a breakdown under a bear cup pattern" and our "hanging on a cliff" rules.

### ONIS EXAMPLE:

On the right, you see a selloff on a 2-day ONIS chart... it closed at 47 1/2 and gapped all the way up to 52 premarket on the open.

We never just blindly short an open gap up, it could easily have kept running up. Instead, we wait for a couple of things to occur:

1) Since it's near a decade number, we wait for it to lose the 50, and short at say 49 5/8.

2) We want to see a downtrend, or at least a bear cup, prior to shorting it on the open. The least preferred open gap up short is one that simply gaps up and sells down with no support, as it could reverse to the upside on us quickly.

We want to see it test buyers, and continue selling off, as it does in this example, you can see it popped up to 50 1/2 a bit before continuing on down.

The first TA based cover target is the previous day's close, in this case, around 47 1/2. Nice short from 49 5/8 - almost a 2 full point winner on a \$50 stock... that's 10% profit for 2 hours patience in the short. Not too bad an ROI.



### PPRO EXAMPLE:

Here's another good volatile example using PPRO gap and bear cup, losing the cliff on the open at right under 18 3/4 for the short play.

As you can see, our cover stop is at the previous day's high (or close, whichever is highest, as in the ONIS example above).

This short yielded over 1 5/8 points profit from a \$20 stock. Again, a superb trade, executed correctly.

Where would our buy entry have been on the open? If it traded over the 20 3/8 or so, it would be a buy. It didn't, it tested 20 decade resistance and faded all the way back down to 16.

Nice movement, on heavy volume.



Let's look at one final example here:

I always advocate a "systems approach" to trading, where we combine several indicators to give us a buy/sell signal.

**AKAM EXAMPLE:**

Here's AKAM, a b2b stock I like to trade (along with ARBA CMRC etc).

We see a descending triangle on the open, and it gives us the short signal once it loses the 24 3/4 support line.

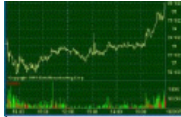
The first place to cover (and possible enter for a long bounce), is when it makes a bull cup on a volume reversal, as we can see here at 14:00, 2pm EST.

See the volume spike at the bottom? This would have us cover our short at the 24 1/4 or so, and enter long 24 3/8. In this case, it didn't bounce, so, we made a large profitable short and took a small stop losson a bounce attempt long.

The key is to have the win:loss ratio consistently profitable; by using these chart patterns you should learn how to begin trading more effectively, and nailing the winners.

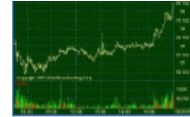
Good trading all.





## Trading Your Favorite Long Chart Patterns

Let's find out which Long Chart Patterns are the most profitable for you. I've put together this worksheet to help you keep track of the patterns that produce the most consistently profitable trades in your trading.



**Trader Instructions:** Make several copies of this worksheet and use it to track your progress for your long trades. By studying your successful trades and your stops, you should be able to find a pattern - eg the type of chart that works best for you, the time bought, the stock sector and more.

TICKER	TIME Bought	CHART TYPE (check which type of trade this was):					P&L
		2-Day High Breakout	Intrarange Long	Bounce (2-day support)	Bounce (under 2-day low)	Other (describe)	

## Advanced Risk Management: Using Trailing Stops and Stop Losses

Let's put together a stop loss game plan using this worksheet.

I want you to jot down your thoughts regarding how you plan to manage your stops the Next time you're in a live trade.

Using 1/4 point to 3/8 point Stops

In the space below, I want you to write down the stops that you take on the next three trades you make.

Stock:	Buy Price:	Stopped out:	WHY out?
example: CMRC	30 3/8	30 1/8	t&s all sellers
1.			
2.			
3.			

Exceptionally Tight Stops using Level 2:

Here's another technique: you can get in, say over a whole number at the 3/8, and get back out if the number of participants on the inside bid decreases from, say 7 to 2. This is a very tight stop loss strategy, and can also be used profitably. Say you buy YHOO 42 3/8, when there's 7 participants on the inside bid at 42 1/4... then it drops to 2 bidders, boom hit one of them and be out with a small 1/8 loss max. Try this one.

Trailing Stops to Lock in Max. Profits Per Trade:

Using trailing stops is vitally important in the choppy market we've been experiencing recently.

Let's look at a few tips for trailing stops.

In the L2 box below, let's say we've been in this trade from 22 3/8 and it's now at 23 1/2. A trailing stop at 3/8 points back from the inside means we'd sell the if it drops from 23 1/2 to 23 1/8.

You may well want to use even closer trailing stops, say at "if it starts to lose the 23 1/2 on level 2", eg if MLCO NITE disappear, you might want to sell to one of the remaining bidders, to lock in a good profit.

In the space below, jot down the SIZE of the trailing stop: you use on each of your next three trades:

--	--	--

MMID	Bid	B...	MMID	Ask	A...	
MLCO	23 1/2	10	ISLD	23 9/16	20	23 1/2 300
NITE	23 1/2	10	INCA	23 9/16	1	23 1/2 100
MADF	23 1/2	10	STRD	23 11/16	5	23 9/16 1.00K
REDI	23 1/2	4	BRUT	23 11/16	5	23 1/2 400
WASH	23 1/2	3	MSCO	23 3/4	10	23 1/2 100
OLDE	23 7/16	10	LEHM	23 3/4	1	23 9/16 400
MSCO	23 7/16	10	GSCO	23 7/8	10	23 9/16 100
SLKC	23 7/16	10	NFSC	23 7/8	1	23 5/8 1.00K
BRUT	23 7/16	1	MONT	23 7/8	1	23 5/8 1.00K
ISLD	23 3/8	10	FBCO	23 7/8	1	23 3/4 2.50K
DEAN	23 3/8	5	HRZO	23 15/16	15	23 5/8 500

## Module Six

## Advanced Chart Patterns & TA

Click on each link for a new daytrading lesson. Be sure to complete the trading worksheets and activities for each module.

[Back to DTU CAMPUS MAP](#)

Click on each line for daytrading lessons from the list below. An underlined link means the content is now available. **Note: click on your browser's "reload" button to make sure you see the latest modules posted as they become available.** Remember to set your screen resolution to at least 1024x768 to enjoy DTU.



### Trading Lessons

 = Updated pages w/in last week.

DTU Module 6 Lessons:



to play audio, click the yellow speaker icon in each lesson

- [2-day High/Low Breakout Chart Patterns Explained - \(with Audio\)](#)
- [Time of Day Reversals and Pivots you Should Know About - \(with Audio\)](#)
- [Using Fibonacci Retracements for Intraday Range Trading \(with Audio\)](#)
- Trading with Three-Point Breaks, Elliot Waves and More
- Using Nasdaq Futures/E-minis, \$TRINQ and Sector Charts: More Tips
- [Bullish Candlestick Chart Patterns to Go Long With \(with Audio\)](#)
- [Bearish Candlestick Chart Patterns to Short \(with Audio\)](#)
- Reversal Candlestick Chart Patterns: Exiting Trades based on Pattern Reversal
- [1-Minute Stochastics In Detail: Chart Setups You Should Recognize \(with Audio\)](#)
- [Recognizing Breakouts and Breakdowns: Trading Consolidation Pattern Breaks \(with Audio\)](#)
- [Patterns for Fast Traders: Chart Patterns for the First 30 minutes of the Market, 9:30-10am \(with Audio\)](#)
- ["Hanging on a Cliff Ready to Drop" Short Chart Pattern Tips \(with Audio\)](#)
- Scalp Charting Patterns: Flipping 1/4s and 1/8ths for profit later in the day
- Using multiple Advanced TA Indicators Together as a System: Examples of How a Pro Trades
- Time of Day Patterns for Trading: Knowing the "Prime Times" and Retracements/Pivots

### Worksheets

[Click here for Powerpoint viewer program](#)

[Click here for MSWord view program \(3.5Megs\)](#)



- [Trading Your Favorite Long Chart Patterns - New!](#)
- [Advanced Risk Management: Using Trailing Stops & Stop Losses](#)
- [Chart Patterns for Fast vs Slower Trading: What's the Difference Here?](#)
- [Using Multiple Advanced TA Indicators Together as a System- Worksheet](#)

### Activities

- Trading Like a Pro - What are Your Signals?
- Collecting Chart Patterns that You Win With
- Advanced TA: Applying it to Your Own Trades
- Action Plan for Improving Your Daily Trading Results



- **Scanning Basics Part 1: Choosing the Types of Stocks to Daytrade**

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● **Main Points:**

AAPL  
ADBE  
ALTR  
AMAT  
AMCC  
AMGN  
AMZN  
BEAS  
BGEN  
BRCD  
BRCM  
CHKP  
CIEN  
CMVT  
CPST  
CREE  
CSCO  
CTXS  
DELL  
DIGL

- This lesson will help you learn how to select a stocks are best for Nasdaq daytrading
- Start by quickly [reviewing the first intro module](#) page on the subject, eg avoid the most actives and those w/less than 5% intraday volatility
- With all the possible stocks out there to trade, how do you choose the best ones to focus your trading efforts on? This is what we'll answer in all of Mudule 7, starting with this lesson.
- Key criteria for choosing the right stocks to trade are illustrated with the examples below.
- A few helpful things to remember are to be patient, be skeptical of charts, be sure to trade during the best trading time of day, eg 9:30 til 11am, and be selective in choppy market.
- Stock selection for daytrading is based largely on trading ranges and chart patterns. The volume and volatility that are essential to creating profitable trading opportunities are important to learn how to read.
- Scanning through a list of stocks, like those on the left, is done each morning premarket starting at 8:30am EST, we look for premkt buying/selling/gaps and volatility as an early indication of the market trend. We also look at the COMPQ on the two day chart.
- The stocks I'm training traders to use, and trading myself, for the current market, June 2001, are in the column on the left. Many of them, eg the tier 1 sector leaders like INTC MSFT, or ones that some of the rooms trade heavily, like JNPR/CIEN, I may use only as indicators, ones I keep an eye on, while trading activity is focused more on ones like VRSN CHKP ADBE AMAT SEBL BEAS.

EBAY  
EMLX  
ERTS  
EXTR  
FLEX  
GMST  
HGSI  
IDPH  
IDTI  
INTC  
INTU  
ITWO  
JDSU  
JNPR  
KLAC  
LLTC

**KEY IDEA: Scan for "CLEAN CHART LINES" on charts with WIDE 2-4 point intraday trading ranges and volatility, stocks priced \$30-\$60 or so.**

**STEP ONE:**

Learn what stocks are in what sectors, and which ones are the "most actives" (not for trading, more to use as an indicator) vs the "trading stocks" (eg INTC the most active, we trade KLAC AMAT LLTC XLNX PMCS etc).

**Figure out what sectors and stocks to begin looking at** using a 2day 2minute candlestick chart. You do not care about the 10day or longer timeframe. Start scanning based on stocks in major [sectors](#) ([click this link to see what stocks are in what sector](#)). Also see [this link](#) midway down the page for stocks sorted in sectors.

**STEP TWO:**

Now that you are familiar with what stocks belong in what sectors, begin looking at them on two day charts each morning, (should take 1-2 minutes per chart for 20-30 charts you review each morning premarket).

Your daily morning premarket ritual should include the following:

- **What's the average intraday trading range of the stock?** Let's focus on those with a 2 to 4 point range as a starting place.
- **What's the price of the stock?** Look to trade those priced \$30-\$50 per share. The under-\$20 stocks, and to a lesser degree, the \$20-\$30 ones, have under a point (or 1 1/2 point) total intraday range, making it difficult to get +1/2 point wins or better consistently.
- **What's the chart patterns** of the stocks telling us? Look for ones that have relatively clean trading ranges and can provide decent trading liquidity.

LRCX  
MEDI  
MERQ  
MLNM  
MSFT  
MUSE  
NEWP  
NTAP  
NVLS  
NXTL  
ONIS  
OPWW  
PMCS

Compare the "good stocks" and "bad stocks" examples below - what differences do you see?

**GOOD STOCKS FOR DAYTRADING EXAMPLES:**





**Answers:** for the good stocks, above, we have good trading ranges and volume. Both are needed for successful trading. There is **strength in these charts**, in the directions of their moves, both down on 6/14 and back up off the bounce on 6/15.

**BAD STOCKS FOR DAYTRADING EXAMPLES (same trading days, 6/15/01 - 6/16/01):**





**Answers:** for the three stocks above, which I would generally not want to trade on a regular basis, each chart has a problem. CORV is too cheap, it's a sub-\$20 stock that has very little trading potential. Also note that you can't short under-\$5 stocks. The best a trader could've done is buy the exact bottom at 3.9 and sold for 4.1 ... this is bad.

MSFT doesn't have enough trading range (though a 2d breakdown short is a good technical entry, the trade potential is not high). And ELON doesn't have either sufficient volume or volatility to be worthwhile for trading.

I want you to learn how to differentiate between the various charts, and learn how to ignore/filter out all the bad charts, which are the majority, and instead learn to focus on specific trading opportunities when they exist.

which are the majority, and instead learn to focus on specific trading opportunities when they exist.

We will cover many specific scanning strategies and criteria throughout Module 7, since it's important to help you all learn what to look for in whether or not to enter a trade.

- **Scanning Basics Part 2: Identifying Signals vs "Noise" - What Should Get Your Attention?**

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● **Main Points:**

- This lesson will help you learn some of the initial criteria to use in helping tell the difference between "good trade opportunity" and "no clear signal" in the charts.
- One key to remember is that you do not want to get wiggled out, so avoid charts that have a lot of chop and churn in them. You cannot expect to "thread the eye of the needle" with some stochastic pop scalping style, this is unrealistic.
- You want to use close stops on stocks in clean, large 3/4 point type trends.
- In scanning for stocks to trade, give preference to those with "clean lines" - they are easier to trade.
- It is worth noting that it will take you some time to learn how to distinguish between the two types of charts.
- The examples here and in subsequent lessons can help give you a clear idea of what you should be looking for.
- It's good to avoid the churn in stocks that chop and oscillate too closely, as these will produce more stop losses.
- It's also important to know how far, on average, your stock will run before getting a retracement or consolidation patterns.

CHART PATTERN EXAMPLES:

**CLEAN TRADE LINE CHARTS**

**Note in the charts below that the trading follows a closer line, eg there's less "chop" and wiggles on the patterns. These are better for trading.** You do not want to trade stocks that oscillate and chop around a lot, as you will get stopped out.

These three below, EBAY BGEN ERTS illustrate "clean" trade lines:





CHART PATTERN EXAMPLES:

CHOPPY/NOISY TRADE LINE CHARTS

**Note in the charts below that the trading is choppy and indeterminate.** The moves in either direction are met by reversals more frequently, and trading is choppy. Again, these are all from the same trading day.

**These three below, CIEN DELL QCOM illustrate "choppy/noisy" trade lines, and show you the types of charts to avoid trading:**







Not surprisingly, these are also very heavily traded "most active" types of stocks. A good example of how something popular with the public crowd can be bad for daytrading.

#### Your Own Observations:

Okay, so go pull up a handful of charts and see if you can start to differentiate based on the "trade potential" in what you are looking at.

Take note of those with cleaner, easier-to-follow trade lines, on good volume, compare to those that just chop and churn.

As a trader, you should develop the ability to differentiate between these various chart patterns.

- **Scans for Percent Gainers - When Do We Look for New Longs??**

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### ● **Main Points:**

- This lesson is designed to help you learn what to look for both premarket and as each trading day begins for scanning for potential long entries.
- One key strategy to use premarket is to begin by identifying stocks that are "outliers", eg those that closed the previous day the highest percent green/red, especially when this is over 5% in magnitude.
- In the current trading day, we can play both continuations/reversals of these, as well as learn how to do real-time scans for high-potential trade setups.
- In scanning for percent gainers, we need to understand both the average intraday trading range of the stock, eg when it's extended or about to continue.
- Strong clean line charts that are reversing or continuing on high volume are excellent to learn how to scan for.
- This strategy is particularly well-suited to mixed, choppy days. You want to be able to identify those few charts that have the best potential for follow through using these techniques.
- Using a 2-day high breakout pattern in combination with correct premarket and early market scanning can produce excellent results. Let's look at a few examples:

#### THE METHODOLOGY FOR SCANNING FOR PERCENT GAIN CONTINUATION PATTERNS:

##### **1) PREMARKET WORK: RELATIVE SECTOR STRENGTH PREVIOUS DAY SCAN**

**It begins, as always, with your premarket work that you start each trading day around 8:30am EST.**

- **Set up one dedicated quote box that just tracks sector percent changes** (calculated from the open, not from the previous day's close) .

SCANNING ELEMENT ONE: **Relative Sector Strength from Previous Trading Day:** You should look for which sectors closed off the most green/red from the open in the previous trading day... eg a typical analysis might yield :

Strong prev day (NBI SOX) Weak prev day (GIN GSO) If you see that in the previous session, say NBI closed +1.8%, SOX +1.2%, GIN .0.8% and GSO -1.1%..

Ok, so now you have a 'bias' to know which sectors had the most money flow in/out in the previous trading session. This is a helpful data point for the current trading day.

##### **1) DING DING! OPENING BELL, What To Look For:**

Okay, now as the market opens, **you should be keenly focused on the sector percent change from the open as the market goes from 9:30 am til 9:38 am. You're looking to see a) whether they open mostly green/mostly red, and what trend they have, as a group and b) which 2 sectors are the strongest/weakest?** To get this you need to click on the Pct column frequently, to sort the column by which sector percentages are moving, eg once every couple of minutes.

You also have 1-minute line charts on your monitors grouped by sector, along with an index chart (see <http://www.daytradinguniversity.com/!16mon.gif> left two screens for examples, using SOX/GSO) Also note the sector percent chart in the 2nd monitor as well.

Let's walk through an example step by step, a good example is in the live room on a GENZ series of winning alerts we posted (4 in a row wins) on Feb 12, 2002. Let's say our sectors opened like this, eg at 9:45 or so the sector box may appear like this:

Symbol	Pct▼
\$NBI	+0.8%
\$COMP	+0.3%
\$GIN	-0.1%
\$GSO	-0.5%
\$SOX	-0.7%
\$GHA	-1.3%
\$GIP	-1.7%

Your question as a trader is: a) **is the market overall bullish or bearish on the opening 10-15 minutes?** (bearish, also look at the tring value to see if it's under 1 or over 1, eg <.7 bullish, >1.5 bearish)

b) **which 1-2 sectors are the most green** (Biotechs, NBI) and most red (Networkers and hardware, GIP/GHA) and **most red by 9:40am?**

Note that we usually get quick market reversals around 9:40/9:50/10am daily.

2) OK You've Identified Overall Market Bias (Long/Short) by seeing if the majority of sectors are green/red percent change from the open, and you have Identified which sectors are most green/red of the 6 or so you follow.

This is your Initial Sector Relative Strength profile, your data to work with, that you moderate all trade entries from.

You are now prepared, say it's 9:40am, and you are:

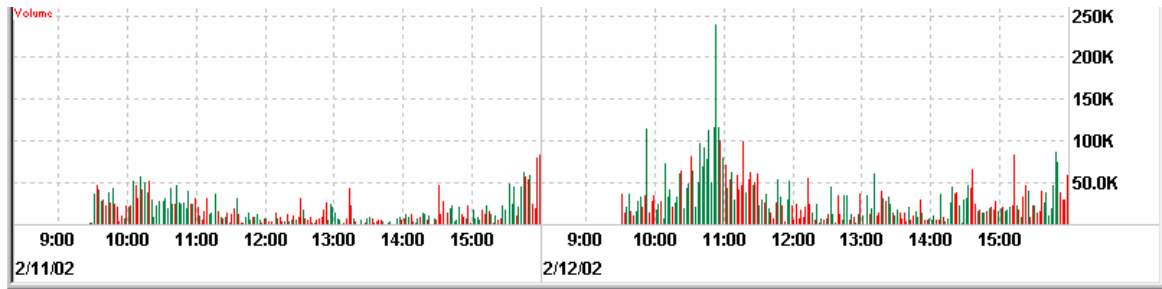
a) more skeptical of longs than shorts on an open like this (meaning you're likely to mainly try 2day high breakouts, intrarange long entries rare, in NBI sector) and

b) you will look for longs mainly in Biotech sector on this open, and short the other sectors.

Let's look at an example of live calls I made in our live training room Feb 12th 2002, using a NBI sector breakout in GENZ:

This is the 2-day chart in GENZ: Initial longs at 43.6, 44.7, 46.7 for three long wins, and a short call at 47.35- for the reversal.





Now how do I scan the market for such a nice string of wins, you may ask?

Well, we are initially biased short overall in the market, with possible longs in biotech, as they are the strong/green sector of the basket. I knew this going into the open, during our first 20 minutes or so, as biotech sector took the early lead.

I saw both volume and pace in time & sales strong in GENZ, which helped confirm our multiple entries in this powerful stock.

**Use strong stocks in the strongest relative sector on 2day high breakouts as your key, #1 most-often used long entry Nasdaq daytrading strategy.** You do Not have to wait forever for these two day highs, and if you use the time & sales and volume patterns to help you filter false breakouts/double tops, eg by making it punch through at least .2 to .4 over the high of the previous trading day, on volume, you will have learned the best trading setup I can share with you. These are Much better than intrarange or bottom fish type long entries. Test it yourself. I do, daily.

**Key learning point:** Sector percentages tend to stay relatively constant throughout the trading day, eg the "most green" and "most red" sectors at 9:35 / 9:40 will likely be the same strongest sectors throughout the day's session.

What this means is, (here's another pro tip), the "most green/most red" sector at 9:40 can lead you to a nice profitable win on an entry at 10:15 or whatever, since you know the relative sector strength pattern for the day.

Given the choppiness of the stock charts, it's very important to know this one data point, that **the rank order of sector percent changes for the outliers** usually stays relatively constant throughout the trading day. It's very unlikely for sectors that are the outliers to change their ranking/ordering throughout the trading day. Eg **if semis and software are strongest sectors at 9:50, they are very unlikely to become the weakest sectors compared to others later in the session**, they tend to flock together in the same rough ranking.

Use this powerful knowledge to help you assess specific chart patterns as they become available for entries, moderate/balance your entries and other data points off of the sector percent relative strength scan.

Here's the actual sector percent change chart from the open on Feb 12th, note that the sectors closed offat 4pm in the same rough order as they opened, with biotech's the strongest.

Symbol	Pct▼
\$NBI	+4.8%
\$COMP	+0.3%
\$GIN	-0.0%
\$GSO	-0.5%
\$SOX	-0.7%
\$GHA	-1.9%
\$GIP	-3.2%

Ok traders, test this out for yourself - the main point for long sector-based scanning strategies is to continually sort the sector percent changes from the open and then selectively enter breakouts from among stocks that belong to the "lead sector"

This is a big help if you face the common problem of "ok I see 6 chart patterns that look okay for longs, which one do I go with?" In this example, say you are watching GENZ (NBI) and VRSN CHKP (GSO) and AMAT XLNX (SOX), given chart patterns that are all roughly the same, you would want to go long GENZ since it's in the strongest sector, thus has the 'best odds of following through'. Make sense?

#### Your Own Observations:

Okay, so practice with this powerful technique, it's one of my most important signals in my daytrading entries and exits, as I explain daily in the live training room. Hope it helps - enjoy!

REST WILL FOLLOW WHEN THE AUTHOR FINISHES AND PUTS IT ON HIS WEBSITE!

## Module Seven

### — Scanning Strategies and Software —

Click on each link for a new daytrading lesson. Be sure to complete the trading worksheets and activities for each module.

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Trading Lessons

 = Updated pages w/in last week.

DTU Module 7 Lessons:

- [Scanning Basics Part 1: Choosing the Types of Stocks to Daytrade -](#)
- [Scanning Basics Part 2: Identifying Signals vs "Noise" - What Should Get your Attention?](#)
-  [Scans for Volume Patterns - What Volume Criteria is Important?](#)
- [Scans for Percent Gainers - When Do We Look for New Longs? - New!](#)
- [Scans for Percent Losers - When Do We Look for New Shorts?](#)
-  [Scans for Premarket Gaps - Gap Scanning Strategy Explained](#)
- [Sector Strength and Weakness: How to Monitor and Trade off of the Signals](#)
- [Scanning for Sympathy Moves, Bounces & Breakouts within Sectors](#)
- [Scanning for 2-Day and Intraday Breakout & Breakdown Plays Using Candlesticks](#)
- [Scanning for Resistance/Support Patterns Part 1: Using the COMPQ 2-Day and 10-day Chart](#)
- [Scanning for Resistance/Support Patterns Part 2: Intraday Consolidations & Breakouts](#)
- [Scanning for Cup Pattern Breakouts - How to Evaluate the Likelihood of Success](#)
- [Scanning for Ascending Triangles, Pennants and Trends](#)
- [Scanning Software: What to Look for](#)
- [Scanning with Your Eyes Wide Open - What to Look at Each Trading Day](#)
- [Professional Scanning Techniques - Spotting Trading Opportunities Quickly](#)



## Worksheets

[Click here for Powerpoint viewer program](#)

[Click here for MSWord view program \(3.5Megs\)](#)



- Your Personal Daily Scanning Log
- Scanning Successfully: What Types of Trades Work for You?
- Matrix of Sector Scans and Trading Setups
- Results and Risk Management: Scanning by the Numbers



## Activities

- "Scan It, Trade It, Profit, and Repeat"
- Your Radar Spots  
Hostiles/Friendlies - What do You Do?
- Separating out the Signal
- Scanning Profitably: A Personal Action Plan

## Module Eight

### Advanced Scalping Plays

Click on each link for a new daytrading lesson. Be sure to complete the trading worksheets and activities for each module.

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Trading Lessons

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DTU Module 8 Lessons:

- Precision Daytrading: Scalping Explained from a Professional Traders' Perspective
- Scalping Goals, Objectives, Risk/Money/Trade Management: An Overview
- Stock Selection for Scalping: Scanning Strategies for Scalp Trades
- Trading Styles Compared: 1) Core Daytrades: 2 to 20 minutes, 2) Scalping: up to 5 Minutes
- Trailing Stops, Stop Losses and Exit Targets for Scalping NASDAQ tech stocks
- Scalping in Size: Trading 1K-2K shares for profit
- Become a Market Maker: Scalping by Buying at the Bid and Offering at the Ask
- Decimal Trading and Scalping: How to Trade the Decimalized COMPQ
- Types of Scalping: Channel/Consolidation Trades vs Breakout Scalp Runs
- Scalping and Chart Patterns Part 1: Using Stochastics, MA and Candlesticks
- Scalping and Chart Patterns Part 2: Using the TRINQ, COMPQ and Sector Charts to Scalp
- Scalping and Time & Sales Part 1:- Using the Tape to Scalp
- Scalping and Time & Sales Part 2:- Assessing Buy/Sell Pressure
- Scalping and Time & Sales Part 3:- Trade Entry and Exit Using the Tape
- Scalping and Nasdaq Level 2: How to Use It Correctly (and, How to Not Use It)
- Order routing challenges and strategies for large share size trades
- Scalping with Fibonacci Levels & Retracements



## Worksheets

[Click here for Powerpoint viewer program](#)

[Click here for MSWord view program \(3.5Megs\)](#)



- Nasdaq Daytraders' **Scalping Journal**
- **Worksheet for Trade Management: Position Size and Stops**
- **Stock Selection Criteria for Scalping: The Matrix**
- **Your Personal Scalping Trader's Action Plan: The Next Steps**



## Activities

- "A Quick Scalp Here, a Quick Scalp There"
- **Scalping in Action: Tracking Your Progress**
- **Taking Early Profits on Your Scalping Trades**
- **Position Sizing in Scalp Trades: Order Routing and Trade Size**