Welcome to the Daytrading University!

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

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

Module 1: Essential Skills for All Daytraders to Learn.

- Getting Started: choosing an online broker and setting up your trading software
- 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
• Daytrading Educational Books & Resources: Our Top Picks to Learn How to Trade Better
• Introduction to daytrading methods: knowing when to buy and when to sell
• How to choose stocks to daytrade: screening for high-percentage stocks
• Avoiding the "7 deadly sins of daytrading": how to stay in the game
• The difference between daytrading and investing: stock research tips for daytraders
• Basic Technical Analysis: Choosing data intervals (1-min and 13-min charts), identifying intraday support and resistance levels, recognizing oversold and overbought stock patterns, momentum trading
• TA101 and Advanced Intraday TA: What the Pros Use
• How to Daytrade Bullish Intraday Chart Patterns
• How to Daytrade Bearish Intraday Chart Patterns
• Selling opening gaps up and buying opening gaps down
• Tomahawk scalping techniques: taking small consistent daily profits
• 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

"Fear of Trading"

Click here for Powerpoint viewer program
Click here for MSWord viewer program (3.5Mega)

• 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
• Daytrading Relative Strength Patterns
• Just for Fun

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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 (e.g. 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 (e.g. ISLD, ARCA, INCA).

Some of these include:

- CyberCorp
- MBTrading
- Tradeescape

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

**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.

**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:**

**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 screenshot; [CLICK here to see a recent 6-monitor display example](scroll right)

**RTII and Cybertrader:**
Here’s a screenshot of Cybertrader (below); it offer many advanced features not available elsewhere. RTII (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.
**Example of a basic 2-monitor daytrading setup for new traders**

**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 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 datak 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. ($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.
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**
- 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

**NYSE**
- 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 patterns, trading ranges and how to enter and exit with carefully placed limit orders.

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

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:

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.
Introduction to daytrading methods: knowing when to buy and when to sell

**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"

- 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](http://www.cbsmarketwatch.com) and [ZD news](http://www.zdnet.com), 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":

  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.

  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.
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 till at least 9:35 (after initial open orders are cleared) to trade. My favorite trading times are Tue-Wed-Thur morning 9:35 till 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.

**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 $COMPO 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 COMPO 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 screenshot of the nasdaq composite index and $trin for a recent day:

A quick intro to Level 2 screens: (we'll have much more in Module 2 on Level 2 Trading)
This is a **bullish level 2 screen**, e.g. 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.

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 1.2 Million shares per day average daily volume (prefer 2M+ optimum)
- **Intraday average trading range of 5% or better** (e.g., 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 archibs “chipples’ 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 NWLS QLGC XLNX
  - (GSO): CHK P EBL VRSN VRTS (NB1) AMGN HGSI GENZ MLNM ; others: EBAY BRCD EMLX

Examples:

I like bigeasyinvestor.com (free software) for screening as well as the one at 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:

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

What to look for:
+ Look for stocks that have between 200K-3M daily volume.
+ MOST IMPORTANTLY: Look for stocks who have a good intraday trading range for their share price.

Example: The trading ranges are better for a $22 stock like SPLS with a 1 pt range than a $50 stock like MSFT with a 2 pt range.
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Successful Online Daytrading Training Resources
Avoiding the "7 deadly sins of daytrading": how to stay in the game

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 got it? 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. 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 (”sheeples”) 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 don’t 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.

JOIN ULIUS TRADER FRIENDS REFERRAL PROGRAM
The difference between daytrading and investing: stock research tips for daytraders

Main Points:

You can easily lose money daytrading the highest-rated growth stocks in the market (e.g.: 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 (e.g. all "hold" ratings) if it's going up nicely on higher-than-average volume. It's bad to buy a high-rated stock (e.g. 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:
STOCK #2:

<table>
<thead>
<tr>
<th>Number of brokers recommending as</th>
<th>Average Recommendation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strong Buy</td>
<td>9</td>
</tr>
<tr>
<td>Moderate Buy</td>
<td>7</td>
</tr>
<tr>
<td>Hold</td>
<td>0</td>
</tr>
<tr>
<td>Moderate Sell</td>
<td>0</td>
</tr>
<tr>
<td>Strong Sell</td>
<td>0</td>
</tr>
</tbody>
</table>

Number of brokers recommending as: Strong Buy 9, Moderate Buy 7, Hold 0, Moderate Sell 0, Strong Sell 0.

Average Recommendation:
- This Week: 1.44
- Last Week: 1.50
- Change: 0.06

(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.

Send us email

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Successful Online Daytrading Training Resources
Basic Technical Analysis for Daytrading (page 1)

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.

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 chart. Here's what three intraday AMZN charts would look like with each of these displays:

<table>
<thead>
<tr>
<th>Close line 1-min</th>
<th>Candle 1-min</th>
<th>Bar 1-min</th>
</tr>
</thead>
</table>

![Chart Images]

**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 mutiday “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.

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.

<table>
<thead>
<tr>
<th>Date</th>
<th>Time</th>
<th>Entry</th>
<th>Quantity</th>
<th>Price</th>
<th>Profit</th>
</tr>
</thead>
<tbody>
<tr>
<td>11/24/1999</td>
<td>09:47:45</td>
<td>Sold</td>
<td>200 HRL</td>
<td>41 7/8</td>
<td>$3,364.73</td>
</tr>
<tr>
<td>11/24/1999</td>
<td>15:38:58</td>
<td>Bought</td>
<td>200 HRL</td>
<td>40 1/2</td>
<td>$-8,100.96</td>
</tr>
</tbody>
</table>

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

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**Intro to TA for Momentum Trading**

- Momentum trading includes "jumping on whatever's hot", such as IPO's, morning gaps (either gainers or losers), and news plays. We'll look at reading stocks 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 made 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!
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 ($COMPO), spous, (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 (e.g. during 11:30-1:30 EST) 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 COMPO (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 it’s 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&b'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 stock 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 stock 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”...
How to Daytrade Bullish Intraday Chart Patterns

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/rolloff. 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 high=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 PIZZA 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.

12/08/1999 15:50:15  Bought  500 SBUX  24 1/16  3-12,041.24
12/10/1999 09:26:55  Sold    500 SBUX  24 7/16  333,000.55
Intraday Channel Bottom Bounce Plays: Continuing on with 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: sps 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 (SSOX; INTC AMAT
KLAC XLNX ALTR) and you see the SSOX 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 SSOX 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...
How to Daytrade Bearish Intraday Chart Patterns

### Main Points:
- The main thing I want 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?**

<table>
<thead>
<tr>
<th>High-Percentage Daytrade</th>
<th>“I Don’t Know” Daytrade</th>
<th>“Low-Percentage” Daytrade</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock is rebounding from an extreme oversold condition w/ volume; or</td>
<td>You are not certain which way the stock will go</td>
<td>Cheap chatroom stocks (e.g. EFA to 21 it’s running!)</td>
</tr>
<tr>
<td>It’s heading up in a steady trading channel on good volume; or</td>
<td>You are bored and want to trade something, anything</td>
<td>See above</td>
</tr>
<tr>
<td>You got in early on a positive news release and the stock is running; or</td>
<td>The stock has been fluctuating in a trading channel on flat volume</td>
<td>Read it again</td>
</tr>
<tr>
<td>Technicals (stocks, MACD, RSI, level2) tell you it’s going up</td>
<td>The Level 2 bid and ask columns look similar, and there is no clear pattern in time and sales to follow</td>
<td>It’s lunchtime (11:30-1:30EST) and you like the stock’s analysts ratings or the company’s products/services</td>
</tr>
<tr>
<td>CNBC mentions the stock price being oversold who good reason, or a new deal etc. in a favorable way; or</td>
<td></td>
<td>Stock has run up over 20% in a spike upwards and you’re chasing it</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Stock is gradually selling off and you think you found the bottom (famous last words)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Stocks with wide spreads (1/4pt or bigger) and low volume (under 300k) Can you say</td>
</tr>
</tbody>
</table>
• 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 YHO0 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 higher highs/higher lows, or, wait till it breaks thru the previous top on strength.

**DOWNTRENDING CHANNEL:** Here TVC 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".
• 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.
Selling Opening Gaps Up and Buying Opening Gaps down:

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 38. 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.

[Send us email](#)  [DISCLAIMER](#)
Tomahawk scalping techniques: taking small consistent daily profits

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.
How to read relative strength and major sector stock patterns

Main Points:

- Stocks in each major sector (telcom, 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:

![Image of a stock chart]

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?

![Chart Images]

**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 ‘not 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, who 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"

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":

<table>
<thead>
<tr>
<th>Date</th>
<th>Time</th>
<th>Action</th>
<th>Quantity</th>
<th>Stock</th>
<th>Price</th>
<th>Qty</th>
<th>Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>11/08/1999</td>
<td>15:26:03</td>
<td>Buy</td>
<td>500</td>
<td>SPLS</td>
<td>17 4/16</td>
<td></td>
<td>1,731.25</td>
</tr>
<tr>
<td>11/08/1999</td>
<td>15:40:22</td>
<td>Sell</td>
<td>500</td>
<td>SPLS</td>
<td>17 1/2</td>
<td></td>
<td>1,731.25</td>
</tr>
<tr>
<td>11/08/1999</td>
<td>15:40:16</td>
<td>Sell</td>
<td>500</td>
<td>SPLS</td>
<td>17 3/8</td>
<td></td>
<td>1,731.25</td>
</tr>
<tr>
<td>11/08/1999</td>
<td>15:40:16</td>
<td>Sell</td>
<td>500</td>
<td>SPLS</td>
<td>17 3/8</td>
<td></td>
<td>1,731.25</td>
</tr>
<tr>
<td>11/08/1999</td>
<td>15:40:54</td>
<td>Sell</td>
<td>500</td>
<td>SPLS</td>
<td>17 7/16</td>
<td></td>
<td>1,731.25</td>
</tr>
<tr>
<td>11/08/1999</td>
<td>15:50:02</td>
<td>Sell</td>
<td>500</td>
<td>SPLS</td>
<td>17 7/16</td>
<td></td>
<td>1,731.25</td>
</tr>
<tr>
<td>11/08/1999</td>
<td>15:52:30</td>
<td>Sell</td>
<td>430</td>
<td>SPLS</td>
<td>17 5/8</td>
<td></td>
<td>1,731.25</td>
</tr>
<tr>
<td>11/08/1999</td>
<td>15:51:34</td>
<td>Sell</td>
<td>70</td>
<td>SPLS</td>
<td>17 11/16</td>
<td></td>
<td>1,731.25</td>
</tr>
</tbody>
</table>

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). (Date 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 (+$20 commiss) or -$80 on the trade.

Does that make sense? It's a tight "scalping" play, and shows just one of many ways to daytrade.
Nudging more profit out of the trade: when to shake out vs. staying in the trade

- 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 $COMPO 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 $trig 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/chippers (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.
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.

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 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.

- 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

- 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.

- 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 GSQ). 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.
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."

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.)

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 a 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.
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.

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!
### Tops & Bottoms Skill Building Sheet

**Goal:** Improve my ability to accurately predict stock tops, bottoms & buy opportunities.

<table>
<thead>
<tr>
<th>Ticker</th>
<th>Pattern (Sell/buy)</th>
<th>My Bottom &amp; My Top</th>
<th>Actual Bottom &amp; Top</th>
<th>My Buy Time</th>
<th>Best Buy Time</th>
</tr>
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<tbody>
<tr>
<td>S</td>
<td>B</td>
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</table>

**Example:** Here's 4 days of UIS price movement. The 4-day range is 23 7/8 to 25 3/4. The approximate support and resistance levels are 24-25 1/2. I expect the stock to trade in this range, and am unlikely to buy if the price is in the middle of the range. I'll wait until it gets oversold to 24 1/4 to buy long or to short up at 25 1/2, depending on the $SPX (S&P 500 index), $COMPQ (Nasdaq composite index), $TRIN and $PREM direction, along with technical chart indicators, such as volume and trendlines. **The point? Don't make low-percentage trades by buying in the middle of a stock's trading range; buy on oversold dips that have buyers coming back or into uptrends w/volume.**

![Graph](image-url)
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

<table>
<thead>
<tr>
<th>STOCK</th>
<th>Sector</th>
<th># SHARES</th>
<th>BUY</th>
<th>SELL</th>
<th>Net GAIN</th>
<th>TIME of DAY</th>
<th>Total Time</th>
<th>Reason You</th>
<th>Reason</th>
<th>Stock Price</th>
<th>Price</th>
<th>or LOSS</th>
<th>Bought/Sold</th>
<th>in the Trade?</th>
<th>Bought</th>
<th>Sold</th>
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</table>

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.
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.

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
points already. Sure enough, CSCO went on up to 95 1/4 before selling off around 11:30am. Be sure to follow the premarket action on any stock you intend to trade - the volume should be over 20K shares by 9:30 to provide any meaningful signal. Which other stocks below are gapping premarket? (note: only nasdaq stocks are followed this way).

Screensnap: Worksheet 2 - Click here to dl! Microsoft Word worksheet file (14K)

You should use this worksheet (or a similar one you make yourself) to help you learn the profitable daytrading technique of playing opening gaps.

Directions:

1. Download and print at least 5 copies of this Microsoft Word file: journal.doc
2. It can be viewed with the word viewer (link here) or word pad (wordpad doesn't include the table borders, though)
3. During your market research, look for 3-5 stocks that you feel would be good gap candidates. Places to look include: most active on ISLD aftermarket, stage gainers or stage losers, as well as news plays that have moved at least 5-10% since the last day's close.
4. Papertrade the gap plays for these 3-5 stocks on the morning of the gap to see how you would do. Remember, don't buy premarket gap downs on bad earnings/bad news etc until you see the technical indicators we look for of higher highs and higher lows on good volume (and even then, you would use small under- 3/8 point stops).
5. Make a note of which type of gappers you like to play the most: gaps up or gaps down.
6. Integrate this into your trading style and trade small shares on a gap play you believe would be profitable.

<table>
<thead>
<tr>
<th>Daytraders' Gap Play Worksheet</th>
<th>Date: ________</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock</td>
<td>Gap Direction</td>
</tr>
<tr>
<td>Psuedo Gap</td>
<td></td>
</tr>
<tr>
<td>Target Price</td>
<td></td>
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<tr>
<td>Exit Price</td>
<td></td>
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<tr>
<td>PNL</td>
<td></td>
</tr>
<tr>
<td>Notes</td>
<td></td>
</tr>
</tbody>
</table>

A final note: gap plays should be considered risky, so fast execution speeds and tight stops are important. Try these after trading for at least 6 months.

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Successful Online Daytrading Training Resources
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
whether the price bounces up.

5. Also, look at the charts of stocks that have CNBC mentions for a price movement. There's an example of an HRL CNBC mention play at the bottom of the page. (I waited until the price dropped back down and bought for an overnight hold):

**Screensnap: Worksheet 4 - Click here to dl Powerpoint worksheet file (42K)**

**News Plays: Daytrading Worksheet for CNBC Mentions & Earnings**

<table>
<thead>
<tr>
<th>Stock</th>
<th>Date</th>
<th>Type of Play (GME/Net)</th>
<th>CNBC Mention Move on Earnings</th>
<th>Earnings Play: Up or Down?</th>
<th>Reason for Due?</th>
<th>Reason for Shift?</th>
</tr>
</thead>
<tbody>
<tr>
<td>HRL</td>
<td>5/28</td>
<td>GME</td>
<td>No</td>
<td>No</td>
<td>No</td>
<td>No</td>
</tr>
</tbody>
</table>

**CNBC Mention Play:** I bought the bottom after the CNBC mention because of the good news, earnings and oversold condition of the stock. The fact that it was bouncing off decade (40) resistance was the last indicator that told me to buy the stock. Click here to see what happened the next day...

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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) 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 dl 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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Successful Online Daytrading Training Resources
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.
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
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

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 $TINTQ. 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\times300=\$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 nap headed in the next 20 minutes? Volume? Time of day? The trade wars continue. You have just won a battle. Congratulations

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**Market Sell Orders**

---

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.
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,
it will continue to sell off. That’s why we use such tight stops at DTU.

3. Enter a Limit Order to Buy your stock at the Best Inside Bid price.

4. Once your order is filled, use trailing stops if the stock is going your way, or exit immediately if it ticks down 1/8 point.

5. Plan on exiting once you have locked in at least 1/4 point profit - don’t be greedy and hope for more. Scalping is the art of taking small incremental profits off the table consistently. You are not in the trade to stay in through retracements and the entire intraday range - you’re in to take a small quick profit of from $50 - $150.

**Daytrader’s Scalping Log**

Screensnap: Activity 3- Click here to d/l Microsoft Word worksheet file (18K)

Here’s a Microsoft word log to get you started in scalping. I have you identify the support and resistance levels to help you with your trade entries and exits.

**Daytraders’ Scalping Log**

<table>
<thead>
<tr>
<th>STOCK</th>
<th>INTRADAY NET WNL/LOSS</th>
<th>INTRADAY SUPPORT</th>
<th>INTRADAY RESISTANCE</th>
<th>SCALPING GOAL (eg, % p/l)</th>
<th>PRICE BOUGHT</th>
<th>PRICE SOLD</th>
<th>DATE</th>
</tr>
</thead>
<tbody>
<tr>
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</tbody>
</table>
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 $SOX = INT$ 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 XLNK 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 its 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/telecos, retail or other sectors. This is a useful trading skill to develop.
Module One: Activity 5 - Just for Fun

- 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 home runs. 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 (Casper 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)?

   - Gordon "Greed is Good" Gekko: the aggressive, competitive, win-at-any-cost master trader who crosses the line into insider trading to accumulate wealth. He mentors up-and-coming trader
     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 to 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.
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.

Module Two

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.

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 (3.5Mega)
- Stops and Spreads in Level 2
- MM Headfake Plays
- Graphs, T&S and Level 2
- Shadowing MM Buyers

- Name that Averages T&S Support and Resistance
- Reading the Outside Bid and Ask
- When the Market Maker Flips Over

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Send us email

DISCLAIMER
Module Two
Consultant Level 2 Trading Techniques

- 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, TINTO 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. (e.g. 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 CHBR, trading 10.5 million shares as of 11:51 am EST. A block of 40k has just gone off at the bid (bearish).

**Tip:** Use Market (Yellow Band)

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

**Tip:** Use Bid Line (Green Band)

A key band to pay attention to: a leading indicator to see where the mnms think the price will go.
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, 4600 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, so 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 (e.g. $GNI/$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, stochastic/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 bing, 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 28, 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 stocks 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:**

**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 VRTX had its 5-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 volume flow will tell you who the 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 at who’ buying or selling in size, and to exit when the buyers are drying up and backing off the inside bid.

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 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 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.
Module Two Comprehensive Level 2 Trading Techniques:

- 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).

• **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, let’s say in this L2 box sellers using INCA (intinet) 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 ay 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 siting 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 7000 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 questions 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.

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.

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 boring, 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 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.
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.

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.
Module Two

Comprehensive Level 2 Trading Techniques:

- 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.nasdagtrader.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 II! 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.
Module Two: Comprehensive Level 2 Trading Techniques

- Looking for ‘headfakes’, reversals & pivot points, recognizing not 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 their 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, SLK, 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 breakout 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 38 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 shook out. Pay 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 men’s (eg: HR2G posting 88 bid then taking), flipping back and forth from inside bid to ask, and men’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 12/50, 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 SBUX at 24 5/16 bid? Only knows support is at 1 1/4 and will buy stock there, 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!

Now see in the second chart how I’ve highlighted MLCO at 24 1 1/8? He knows this is the initial resistance level, and has parked his sell 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 12/39/99). Where is support and resistance? Well, we can see support at 25 1/2, and highlighted GSCC as the set 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 if 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 up particularly at the places he puts the bids and asks will help you get better at determining likely pivot points and reversals. As always, use tight stops (under 3%) 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 smaller loss than potential (18% maximum loss).

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 (11:30-1:30 or so), and know your stock's intraday market maker ask and support/resistance levels.

NET BUYING vs. SELLING:

Talk about a run! Look at NOYL here on 12330 going from 35 to 40 in the space of an hour. SBSH is the ask for NOYL, and it's 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 price 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 3/16 selling, you'd call him a net seller). This depends on the volume of order flow being sold, of course. I'd expect a run to sell at least 10 1/16 shares to call him the 'ask' 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 'ask' 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).
Module Two  Comprehensive Level 2 Trading Techniques

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 (e.g. for this 3- to 18-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 headache**: MMs will frequently disguise their intentions by routing their orders through INCA or ISLD. See through this haze by determining how strong the buy/sell action is on the inside bid/ask in INCA or ISLD. E.g. if you see the inside ask stay firm in INCA or ISLD you know some market maker is working a large order and that the situation is “indeterminant” or low-probability 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, SESH 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 “speed” 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, e.g.: 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 Ax to Daytrade**: Even with the ECN routing that MMs use to hide their order flow, there’s still plenty of profitable trading to be had by daytrading. #1: Avoiding buying when a major/MM is selling (e.g. if you see MSCO and MLCO both selling on the inside ask you probably shouldn’t buy if their bid is 2 levels outside the market) and #2: “Shadowing” is the ax’s buying/selling behavior. If you see that all else looks okay, e.g. 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 CLC, etc.) or a morning order flow through ECNs, consider following one of these four main roads as one of your primary indicators.

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

In the second box, both the scalping level and MSCO were on the bid with a small green, followed by a lower highower level. P&L = 7/8th point profit in an hour trade. NETA went on to close at 24 1/8. Nice ride.

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

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**#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 1000 shares of stock in 200-300 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 SFLS I MSCO is on the inside or green band, as he tends to hold SFLS up, and SFLS has up days whenever he’s on the inside (at least the last 8.

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

Bld 4/3/4 x Ask 4/1/2

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 axmen'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 mm's" for 3-5 stocks that you follow like the back of your hand. As you know, I like NOVL, SPLS, OCLK, SEUJ, for daytrading, there are many others out there.
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&L 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 mins on the green bid, only an ISLD 2 green on VRTY.

Daytrading PlayaGreen 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 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 (10-25% 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... >>
Module Two

Comprehensive Level 2 Trading Techniques

Main Points:

- Now that you’ve learned 4 ways to “spot the act” 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 SBSX screen. Of the 4 major market makers we’ll be shadowing, which one appears here on the inside bid or ask?

Ok answer is: GS, bid size 10 at 27 5/8. On the time and sales you see a lot of selling going on, and GS 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 instinct (GNCA size 40), 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

Daytrader’s Play: Let’s assume you’ve been watching for awhile and you see GS 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 T3S), 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.). GS stays a buyer more than 70% of the time. He’s not flip-flopping over to the ask much at all, and seems to be holding the stock up. You also see here that GS’s “trade box” is bullish, he isn’t even posting an ask 3-4 spread up (unless he’s taking via an act). Also, you don’t see any of the other 3 heavyweights selling openly at the ask, no MLCO, SBSH, MSCO.
Play #2: Samson and Goliath: MM ax vs. weak hands

Here's our NETA example with MSCO. Now, let's just consider the 4 major mm's MSCO MLCO SEBSH GSCO. Who is MSCO trading against? Nobody, unless someone's selling a lunch through IJLD (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 3/82 (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 SEBSH 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 spread's 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, so in the stocks I play SEBSH 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" you might say to yourself "If have to be careful as it gets over 24, the high of the day is 25 1/16, so I plan on scalping it and selling when T&S start 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 front run GSCO if you're scalping, or slide in to 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 raising his bid, the price moves up - he's less inclined to sell. If the 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 ISLAND, AARNAP, etc. and so you
see a ton of trades going on here. You
do not try to follow the ask 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 90% of the trading is
being routed through ECNs, right? In
the example to the right, let's see, you've got
MLCO offering 5 spreads up, NASQ (an
"almost big g" mm), with a 2 size two
spreads down, nothing in other words you
can follow in the area of a mm at to trade
with an ECN play.

So, you need to follow trades 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.

Daytraders' Play: T&$ looks bullish, L2 looks bearish
(mix, traders?). Indecisive; 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 SGIN
first, then the nas $COMPQ chart, then $RINGSTICK
etc).

For now, its "sit on the sidelines and watch" stock,
based on what I see here. That's ok, I spend most of
the day watching, waiting for an opportune moment, then
bang fire the order, watch it go in my favor a spread
or 2 or 3, then sell. Or, if it weakens then I'm out 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
oversell, 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. At the same daytrading guidelines apply, eg don't 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 this to be very helpful to identify the major market makers in my particular stock, using the
www.nasdaqtrader.com link (see front page www.tradinglot.com link for "Identity the nas az")

4. Once I have narrowed it down to whichever one is playing my stock the most that day, I will look for
high probability profitable times to play the stock, such as the 10:30 nazo bounce on a down day

5. Recognizing not buying vs. selling is a fairly difficult skill to master. It all depends on your understanding of
how to play Monopoly. So spend at least as much time, 3-4 concentrated hours on a single stock, to try
and identify the relevant T&S using the level 2 screen and 3s for the market maker you believe in
the az. It may take a few times to correctly identify who's moving the stock. In fact, I will probably take
you a number of weeks to get to know it. That's ok, its 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 "quack", 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 pdfs).

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/other resource provides (that I am 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 takes 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.
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 others stocks. For example, I find Level 2 not useful at all for trading WCOM, AMZN and NTC, but very useful for stocks like CINC, CMCSK and NOVL. Factors to look at are: how transparent are the level 2 bids and asks in the level 2 box for the specific stock; the ratio of how many bids vs. ECN orders are represented on the Level 2 (eg the higher the ratio of ECN orders to bids and asks 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: 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

Keys to Success in Timing Level 2 Trades:

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.

2) Indeterminate flow-percentage level 2. If your 18s and 19s 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-potential opportunities”, not guesses.
Daytrader Timing Plays:  Regular back-and-forth trading with Level 2 lets you look at the mechanics of using it comedy 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 chart.

Timing entries with Level 2 — here’s some tips I’ve found helpful:

1. 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 10 heavyweight mms (MSCI 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 and INCA) and a weak mmm bid (MONT at 1) on the ask. This is very bullish.

   (Unless, of course, T&S is telling you differently due to mms’ disguising orders via exn routing, or 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 let the bid to liquidate? Let’s look at some timing indicators. The top L2 NOVL window would tell you to sell at 21 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 21 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 your outside, with your ask 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

2) The quantity of the lead sellers’ size starts to shrink: eg if GSCO’s 10 turns into a 6 or a 7 then he’s going to disappear; if he’s really buying then his 10 wouldn’t stay 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 mms increase by 2-3 in either the yellow or green ask column, you should get out for now. Remember, you can always buy back later. When it looks safe.
4) You see the "ax" or other major mm flip from the bid to the ask. Example: if GSOC jumps over the yellow ask and 2 more people join him at the bid, you should bid the ask at 27 5/8 and get outta there now.

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 you were 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 "hmm, they're not buying anymore, its "fifty!", I'm outta there."

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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 11:52 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: Let's say its NETA used to have 4 sellers at 24 3/8, and now traders have bought so much that there's only the level (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).
This usually works when you’re buying ahead of a major support level (usually at 14 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 1/16 (or 34 1/8 of the front run/CLJP rash) 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 round trip. 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 traded 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 its current spot 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 18th of a point. My target is 7/8, or about a 36% 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 18th of a point. My target is 7/8, or about a 36% 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 don’t bet on it. Remember, you can always buy back in later. So, fill buy here, sell 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 daytrade, folks.

OK, time to practice. Try paper-trading 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 bids/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.
Module Two

Comprehensive Level 2 Trading Techniques

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 "tunnel" approach to daytrading, paying attention to the overall market/sector direction first, followed by the individual stock's intraday price action and technical indicators, swing 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.
And even then, I wouldn't be too sure about this particular stock continuing up. I'd wait and see what SESH 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 SESH, 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 always recommend 2 3 spread stops in general, at a minimum 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 (will not go long a stock, unless there is breaking news (almost never). If the market is “indeterminable” then 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, let's 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 semi (S&O) or nets (S&P), based on their composite charts to the right? (answer: semi will be stronger overall because they bounced the morning at 9am; they bounced higher than the index)

2) What does the last 5 minutes of the STRING 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: STRING is an inverse indicator, I'd be ready to buy stocks before a drop in the STRING, like this is 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 price, reversals and breakouts faster by moving to a 15-minute chart.
The Tape 101: What is time and sales? What’s it used for?

Edison invented the original stock ticker a long time ago. 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 real-time. The “tape” of yesterday is replaced by real-time 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 10:35 AMZN 500, telling us that someone bought 500 shares of Amazon at 10:35. 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!

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.

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- If the majority of trades occur at the inside ask, the “trading sentiment” for the stock is bullish for that particular moment.
• In the DBC chart you can see a string of trades going off at the bid at 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.

<table>
<thead>
<tr>
<th>DBC</th>
<th>Bid</th>
<th>Ask</th>
<th>T</th>
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<tbody>
<tr>
<td>10.3/4</td>
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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 (e.g. 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 (bidders, including MLCO and BSEST) 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, selected 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!**

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 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 scalp. 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 man who's parked his bid here, wait to see how many shares whoever's anonymity 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.
Module Two

Comprehensive Level 2 Trading Techniques:

- Time & Sales part 2: Reading tape speed and momentum plays

**Main Points:**

- One professional tape-reading technique that is not widely known is the "speed patterns" and differences in momentum that you can see in T&S before pivots.

- What this means is, while watching time and sales you should be keenly aware of any speedup in the pace of the trading, especially if trades start to go off faster and faster near a key support or resistance point. This signals that a breakthrough or retracement is about to occur.

- Except for very slow-moving stocks (which I don't trade), there is little value in the "time" part of time and sales prints. What I'm watching is the tape momentum, trades going off at the bid, ask or in between, and the offer/tick sizes and new prints that are entered in realtime. Most of the stocks I trade are over 1M shares a day, so trades are continuously going on. The point? If you can take the time off of your T&S ticker, as you see in my examples throughout the course materials. The price and quantity is what's relevant, as is the momentum, or timing, which I am trading with in realtime (so a timestamp is meaningless).

- This is one section I plan to come back with and add screen-cam type movies to, as it is easier to explain as you watch a tape "in motion". For now, let's learn the strategies.

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**Reading the Tape:**

**Speed and Momentum Patterns in Time & Sales**

Recap: High-Percentage Long Play in Time & Sales

From last lesson, we learned that setups like this are "gifts" that should be played long.

1) almost all trades going off in Time & Sales at the inside ask (bullish)

2) volume picks up at this bottom near 33 5/8 to 33 3/4

3) 10:30 nasdaq bounce is a good time to go long

Bid 11/16 or pay up the spread, use 5/8 as a stop

Now, in the example above, would you want to buy if time and sales was going a) faster than it was earlier, as the stock sold off, or b) slower than it was when the stock was selling off? Hmmm?

Answer: you want to go in the direction of the tape speed, so you'd want to see the buying in time and sales going off a) faster than it was during selling. Why? Speed and volume = momentum voting by the crowd.

Let's think about what's happening - you want to join in on the direction, the momentum, just as soon as the pivot (price direction change) occurs, such as off a bottom, where the stock "looks cheap" and others all want to buy some.
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 shakeout, 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 signal 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 let’s 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 out 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 uptick 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 38 1/16 or better. Nobody’s selling; we stay in long.
**Chart #4:** Now we see even more buying at 8/16, bullish; we stay in long. We end up closing the position at 39.1/16 for a 56 point gain on 500 shares, or $3,500 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.

**“Volume and Block Bear Signs” in time and sales:**

Looking at NTC 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
Daytraders Play: Using the Tape Speed to Enter and Exit Positions

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 retrace or both.

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.

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 traders are “agreeing” with the crowd (important) and will likely maintain direction in the direction that they traded it (eg block going off at the bid, ask, in-between or outside).

3. Be aware that a 1mn 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 into contrarian 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:

- 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 day trader. 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 effectiveness.

  - 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.
Note: The higher-priced bottom or top you’re playing, the more likely a pivot is about to occur (e.g., 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: Traders going off fairly evenly with 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 key 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, e.g., 30, 40, 50, 100 etc., occur at 1/4 point for lower-priced (e.g., $10-$20) 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. Watch to see if the trading direction goes to the 15/16 or 17/16 (or 7/8, 17/8) 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 sales 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, let’s 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 1/2 or 46 as you go ahead and buy, with a stop set at 46 7/8.

If on the other hand it hits 46, then sellers pour in at 45 15/16th, then you see 45 7/8, then up to 46, then back down to 45 7/8 etc., (over a 5-8 minute period), then you know it may not have the momentum to break past 46. Look for a lower higher/lower low pattern on the 1-minute chart. If it looks like it’s weakening, fire off a short at 45 1/16th. Your cover stop should be no more than 46 1/4. Maybe you set a cover target of 45 5/6th, 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.

Here’s WCOM from 12/8/09 – 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 17/64th) 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 11/16th of the wall of buyers at 77 drives 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 5/6th or less if it loses support at 77, so use the 77 1/2 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 they will sell down. Note that MASH is using a bid size of 214 because he wants to be first in line ahead of only SBSH w/77 size. WOC 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 CHRX pattern shows all buyers off 12 support in T&S, see everyone bid 12 1/16? Somebody sold a block at 40K, vary 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 CHRX to stop selling and the stock to trade up to 12 1/16 x 1/8th. The point is, where does it go after that? 1/16th, clearing the spread, is only your first stop. You want at least 1/4 point right?

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

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 window 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 CHRX 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 by 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 1.5M shares/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 1 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 cents up or down right away. You'll have to learn which market maker is the axe, typically the heavyweights (MSDB MSPO MLCO GSOC) don't trade the cheaper stocks. You may see names like FWJ 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.
Module Two

Comprehensive Level 2 Trading Techniques

- 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 (e.g., 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 buy/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 (e.g., 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 stopped 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 (e.g., INXL) and MLCO is somewhat obvious about making his selling known by holding the inside ask (e.g., 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 mm's. 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?
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. Play 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 #3, 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 #5 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 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 $10-$15, 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 activities 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 1/2 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?

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 of 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 14-1/2 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, so 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 76 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-trade exit/enter points, using market/sector direction, T&S and 1-minute charts as primary decision support tools.
Module Two

Comprehensive Level 2 Trading Techniques:

Main Points:

- **Trailing Stops** defined: Once you are in a profitable trade, you should raise your stop loss to "follow" the stock's price as it moves up. This ensures that you will take a profit from the trade and not let it turn into a loser.

- **Example**: You buy WCOM at 44 3/8 (putting an initial stop in at 43 13/16 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 45 5/8. You would cancel your original stop and enter a new "trailing stop" in, 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 thicker on Level 2, now it drops to 44 15/16 and your stock is sold. You lock in a profit of $16.80, or $506/hundred shares (so, if you were trading 300 shares your profit would be $238.) 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 CITU we advocate a 2-3 spread maximum stop loss. I usually use the level 2 strength within a spread, as confirmed by T&L 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**

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 stock players to be undercapitalized and can't afford pro 2 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 171/16 buys at 1610) and thin number of weak sellers on the ask.

In fact, I would be likely to buy here at 1710 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 "new and retrace" for now. This trade might be good for only 1/8 point here, it's 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 tight now, since there’s a “wall of sellers” and it just ran up with 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-1/4 point stops than to take large hits.

Another tip: You can also set your stops using a Dollar Amount, eg never let a stock go more than $200 against me (whatever that works out to in terms of 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! 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.

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 drops fast as well.

3) **Price Levels Widths for your Stock**: some stocks have key levels 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.

Remember: you can make a living daytrading by being right only 20% of the time. Keeping 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 DELT are very difficult to daytrade since everyone’s scalping them all the time for a living, try trading easier stocks at first.
Module Two

Comprehensive Level 2 Trading Techniques

- **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:** occur 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, e.g., usually characterized by a change of at least +6% or -8% for the stock's 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 (e.g., 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 tick/stop management to profit off of these corrections in stock prices. It takes patience 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, e.g. 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 -5% before rebounding later in the day.

Let’s look at how to use Level 2 to help identify where these pivots and momentum stops 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 2 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 ticks and the relative speed and price momentum of the trades is helpful, as is the rim movement within the bands. For example, you can see MCG and MASH are buying here, but are making the market at 3/16 offered. Daytrader sentiment seems bullish as we have higher bid ISLD vs. 10 ask. And, as I’ve mentioned numerous times, HRZG’s large sizes are almost always take, so ignore them.

**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. (e.g. MCG may have been a buyer at 3/32 through 3/16, and wants to sell several thousand here at 3/16, for a sizable profit. In terms of pivots and L2, watch for clues by seeing the width of the 1st outside (green) bars as a leading indicator, and watch to see if the major mm are flipping from one side to the other.

You may be relatively safe joining the ISLD bidders here at 3.12, or even paying up 3.25/2, with a stock like this I’d sell it if we get down to 3-4 market makers at 3.12, though losing traders would hold the position down to 3.06 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 T players on both sides. More importantly, you can see a number of “in-between” trades going off inside the spread, at 3.00/2, 3.05/6 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, 3.18, 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 3.18 x 3/16. Even better, just try bidding with the “in-between” bids at 3.18/2 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 begins to wane, before the direction change occurs.

**Daytrader’s Play:** Pivots are dangerous to play, as the trend is “usually but not always” your trend; the stock may pivot for 1-2 spreads and then reverse back to continue its 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.
Module Two

Comprehensive Level 2 Trading Techniques

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 stocks 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 extended) 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 you 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.

- Newer 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 20 minute roundtrip type trades (my favorite). If you don’t need to have your order filled within a few minutes (because you buy 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 fills. Just be sure to always use limit orders to DAY.

Your Order Routing Choices:
Let's look at the differences between these. I've organized a table below showing the rules, when to use, and costs:

<table>
<thead>
<tr>
<th>SelectNet</th>
<th>SOES</th>
<th>ECNs</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>What is it?</strong></td>
<td><strong>How does it work?</strong></td>
<td><strong>What does it do?</strong></td>
</tr>
<tr>
<td><strong>SelectNet</strong></td>
<td>SelectNet is the system that market makers use to trade with. You can also trade directly with mm's using SelectNet orders. You cannot post bid/offers on Level 2 using SelectNet. There are 2 types of SelectNet orders you can make:</td>
<td>ECNs pair up buy and sell orders and execute them in the order received. The ISLD ECN, used by Deltak and many others, is the fastest and most efficient ECN available to trade on, allowing for instant executions.</td>
</tr>
<tr>
<td><strong>Broadcast</strong></td>
<td>Your order is sent to all market makers simultaneously; they can decide whether or not to trade. Low priority for mm's.</td>
<td>The ISLD booklets all the open orders at each price level. ECNs are the most popular way for day traders to trade. You can trade odds easily on ECNs, and they are very liquid, allowing rapid trades. You can also get price improvements if the bidask price on the book is better than the one you enter.</td>
</tr>
<tr>
<td><strong>Preference</strong></td>
<td>An order you send to a specific market maker, eg 3B3H. Only he sees that bidask order you are making. Hi-priority for mm's.</td>
<td></td>
</tr>
<tr>
<td><strong>NASDAQ Trading Rules for This System</strong></td>
<td>Once entered, you cannot cancel Selectnet orders for 10 seconds.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>For preferred orders, the mm must respond with an Accept/Decline/Partial to you within 15-30 seconds.</td>
<td>ATTN orders must be in the 100's.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>You can't send conditional Selectnet orders (eg all-or-none) to ECNs.</td>
</tr>
<tr>
<td><strong>Advantages &amp; Disadvantages for Daytraders</strong></td>
<td>5-minute rule if 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.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>SOES can't execute against ECNs.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>All SOES orders are done at the inside market.</td>
<td></td>
</tr>
<tr>
<td><strong>ADVANTAGES:</strong></td>
<td>You can execute orders outside the market for best-moving stocks, eg preference a mm who's 2-3 spreads away.</td>
<td><strong>ADVANTAGES:</strong></td>
</tr>
<tr>
<td></td>
<td>As long as you're first in line, you can usually get a fill at the bid/sell advertised to the market.</td>
<td>Speed and instant executions. Price improvement possible. Liquidity is great. You can play market maker (especially pre- and post)</td>
</tr>
</tbody>
</table>
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 (thought the trade will show on the Bks tape).

DISADVANTAGES:
For fast-moving stock the mm’s response 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.

Selectnet broadcast: $2.50
Selectnet preference: $1.00

DISADVANTAGES:
SOES only works on the inside market; you may not get filled, the 5-minute rule.

Selectnet broadcast: $2.50
Selectnet preference: $1.00

DISADVANTAGES:
The ECN’s dont always have stocks 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.

Cost: ISLD/NTRD direct free,
REDI 0.02/share
BRUT/INCA: 0.16/share + $1 if preferred thru Selectnet
ATTINESTR/INTO: .005/share + $1 if preferred thru Selectnet

Pop Quiz on Order Routing
Ok, here you are trading from the floor of your Mercedez, placing an order to buy 1000 DELL.

You see this level 2 screen, and decide you want to buy your DELL on ISLD.

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
G2: 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) MAFD
d) ISLD

Answers below.

Question 1: Answer is BEST. Dear Diary, the real are CCPs.

Question 2: Answer is SBSH, the outside full market maker with the biggest order.
Main Points:

- Some market makers like HRZG MASH often show ridiculous bid sizes (e.g., 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 lot of buyers, where did they disappear to?" These are common mm tricks to panic new day traders 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 mm’s MSCO GSCO SESH 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 mm’s. For these ECN-traded stocks (e.g., 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, NTIC, and MSFT, yet another reason to avoid the “most actives” when it comes to day trading. 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 0.53 to 0.56) the 144 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)
1) **Time and Sales** shows primarily selling action, a lot of trades going off at 19 1/4, including the block trades of 3K 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 very heavily weighted to sellers; it didn’t disappear, telling you that the depth of selling on ISLD at 5/16 is heavy. Also, MS CO is right under the ISLD/ARCA 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 have a drop in the stock to at the major whole numbers and fractions. For decelerate support/trendlines, you might want to increase this to 3/16ths stops. Follow the major mm’s closely for these plays.

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**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 ran up 1 1/2 points off its bottom, Time & Sales is telling us there’s still plenty of buyers of this stock at 26 1/16. Also, since SESH is on the buy side (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 100 CPWR at 26, frontrunning SESH.

**At this point in the trade, you missed most of the major momentum,** and are looking for either incremental scalps (e.g., scalp this to 3/16 - 1/4 max expectation), or short if it loses 26, for a short scalp down to the 6/8-3/4 support. Again, tempered by overall market direction – if it’s a runaway bull market then I may stay in the trade 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 (peak 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 1/16.
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, but I know for sure is that GSCO is really buying since its 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. And most FBCO and BRUT, for that matter. What we're looking for is the tape and the bid/ask size. They're staying the same? (indicating a higher order, impossible to tell the depth order flow), or are they shrinking/getting bigger?

Daytrader's Play: Looks like they're selling 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/bid decision-making support tool
- It is useful to monitor your precise entry and exit timing, when used in combination with a 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 whip-saw 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 SBJX got taken out above the stock (say, SBJX 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 1/16.
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 as 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 aware of in using Nasdaq Level 2, for example knowing the difference between an L2 box that shows a 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
e) I don't know

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.

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, 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 beans (1/16ths is only $62.500) 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 S&O/Selling a nm or selected preferring to see if you can get a price improvement. It's "fishing by selected" 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 it 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 10.3/2 (remember large fractions, the 14s, 12s and 34s) are typical pivot points for under-$40 stocks in general.

We see a lot 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 penny ahead of them, so I can exit my position. If the stock runs through 11, which is unlikely, I can always buy it back 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 fails 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 penny or an eighths 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&E is sold 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 "hit and run" all low-percentage plays, and punching through whole numbers is low percentage. Particularly decade or eights, e.g. 9.20, 25, 30. Wall of bricks, since there's a lot of market stop/market orders lined up at these whole number price levels.

The reverse is true for entering a position on a bottom bounce, e.g. 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.
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. E.g., if SBSH is the ax trading AMZN and his bid is 82 1/2/Ask 94 3/8 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 (S&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 get filled on ISLD at 53 9/16 and SBSH is the ax. Where's your stop?

- 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 B above

**Bonus Q:** How wide is SBSH's "trade box"?

**POP QUIZ Question #2:** Here's AMZN, you bought at 91 13/16 and MLC3'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)
You should use this worksheet (or a similar one you make yourself) to help develop your skills to correctly set and follow daytrading stops using Level 2.

**Directions:**

1. Choose 1 stock to follow and set up your level 2 window next to a 1-minute chart.
2. Following the example that has been filled in already, enter the ticker, current bid and ask that you would buy it at (a papertrading exercise), where you would set your stop at (no more than 3 spreads away, using your level 2 window), and the width of the nrms trade box. Also, enter where you would set trailing stops and your profit/loss on the trade.
3. This is a great technique to get familiar practicing setting stops using a Level 2 window.

### Level 2 Stops Daytrading Worksheet

**Goal:** Improve my ability to set stops using Level 2

<table>
<thead>
<tr>
<th>TICKER</th>
<th>CURRENT INSIDE BID x INSIDE ASK</th>
<th>WHERE I WOULD BUY IT</th>
<th>How Wide is the “nrms” trade box?</th>
<th>Trailing Stop/Av</th>
</tr>
</thead>
<tbody>
<tr>
<td>NOYL</td>
<td>31 7/16</td>
<td>31 1/8</td>
<td>30 7/8 (your stop)</td>
<td>SBGH 31 1/8 x 2 1/2</td>
</tr>
</tbody>
</table>

...
Module Two: Comprehensive Level 2 Trading Techniques

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/reversal 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 suckerized 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:
Directions:
1. For one trading day, choose 3 stocks to follow intensely and look at nothing but the L2 and TSS for them.
2. Whenever you see one of the "market maker headaches" that we described above, make a note of it on the chart and identify the Real Pivot (top/bottom) that the stocks drop to or gains to.
3. For each of these headaches, I want you to jot down a brief note that describes what "warning signals" were there, if any, that you could’ve / should’ve seen to help you keep out of the trade.
4. If you were wrong (it looked like a headache but wasn’t), identify why, and what you could’ve done differently to capitalize on that particular trading situation.

Level 2 MM Headache Daytrading Worksheet

<table>
<thead>
<tr>
<th>Ticker</th>
<th>Type of Supposed MM Headache</th>
<th>The Price this was Observed At</th>
<th>The Real Pivot Breakout Price</th>
<th>Notes for how I should’ve traded it</th>
</tr>
</thead>
<tbody>
<tr>
<td>CFWR</td>
<td>X (MSCI)</td>
<td>21.1/2</td>
<td>20.1/2</td>
<td>T&amp;E showed all sellers</td>
</tr>
</tbody>
</table>
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 elements and wavelengths in a mirror, 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 made 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 intensively 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 alert you the stock is a buy.

3. Enter the details of why each of these 3 indicators told you it was a buy, along with the actual price you would have sold the stock at (this is a paper trading 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) 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 all Powerpoint worksheet file (43 KB)
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 up trend, down trend, 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 to 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. **DAILY TRADING & 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?

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**“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
- GSFO
- MLCO
- MSCO
- MASH
- DEAN
- HRZG
- SHMD
- PAUC
- SLNC
- DEAN
- MADF
- BEST
- Other

**Notes:** Remember, this works best for stocks that aren’t heavily traded on ECNs (eg ISLD, ARCA INCA). Also, pick a moderate-volume stock (0001C-2000/day) priced from 51-23 that’s forming or a key resistance level or is in a steady uptrend.

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**At what Price did you see the mm start to buy more of the stock at?** When?

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**Your Day Trading 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?

---

**Once you see the market maker step 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?**

$
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 >5 million shares. Do not pick DELL/CSCO/INTC etc. that has sold/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 3M shares and an intraday trading range of at least 5% (eg $1 or a $20 stock)
2. Carefully watch the level 2 action premarket of the two, is it market makers or chippies on ACR/ARCA/ARCA/BID 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 big players 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 checklist 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 that 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 that 10K shares at a given price level, Headlines and Switching from the bid to the ask repeatedly (he’s probably not the ax if he doesn’t 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 ax is hollow 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 trader's lead
   - Practice trading small sizes of 100-300 shares by following the ax after paper trading 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 SBSH 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 SBSH 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 ask on SBEUX 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 front run him? Wait? Check Time and Sales? It all depends on the price action and technical signals on your 1-minute SBEUX chart.

The immediate “battle” is between GSCO and whoever is selling on INCA (Inhibit). The players line up under these two for the moment, no real strong move next to this action. SBSh and JLC are each a couple of levels down. It’s an indecisive 1-minute window until we see a pattern of buying or selling in the time & sales window.

If INCA trades and we have ISLD/INITE left, with GSCO staying strong you might BID SBEUX 27 5x8. 100 shares or 27 2/32 500 shares etc. to front run. The battle goes on.

Comprehensive Level 2 Trading Techniques:

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.

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 till 11:00 am in a time and sales window.** (By the way, I 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 10:00 am till 11:00 am

3. At first, 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 10k-15k size trades? How fast is the tape printing?
4. Next, I want you to look for directional trends in the tape display. How long does each "run" in one direction or the other last? Do you see "in-between" trades going off at a price between the bid and ask, and is it signaling a pivot in the price?

5. The most important skills 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 pattern.

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 tape window (e.g., its 9:50 and, watching the tape you think to yourself "ok, the stock is going down now", so you write 9:50 NOV/L down 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 going (e.g., "ok, NOV/L is going down, based on chart support, L2 and B2 momentum, I think it may be good for 3/8 point and 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 steps" is the most important trade management skill you can develop.

Again, I would strongly recommend that you choose 3-5 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 active, as these tend to attract the best traders and have lower price/volatility. See my latest L-monitor and B2 monitor setup for a look at the stocks I was following in January 2000 (note: ARNTVMO were just play the setup for a look at the stocks I was following in January 2000 (note: ARNTVMO were just play for that day, some of the others like CIEN NOV/L 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 shorts tops. Invest a lot of time in watching the tape for a couple of stocks you want to trade for a living, from 9:30 am to 11:00 am and perhaps 2:30 pm to 4:30 pm. Don’t burn yourself out by watching the tape all day. Best wishes!

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 mms's from the 1st outside level (green band) to the inside (yellow band) indicates that they want to lock in their buysell 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 to 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 MSBO SBSH GSOC, as usual).
3. 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.

4. 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. LADM bid 1 vs. 1 market maker each offering 10 at the ask means I’d think this stock would go down to 36 1/8 before it will go up to 36 3/8.

Remember, it’s dynamic, so respond with your trade 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**

**Activities**

- 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 SBSH.
- 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 not selling.
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 till 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 about 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 new 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?
Module Three: The Mental Game of Daytrading

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

Trading 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 (3.5Mega)
- 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 DAYTRADER FRIENDS REFERRAL PROGRAM

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Successful Online Daytrading Training Resources
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 (BO. Cleanestat, Bigcharts, CBOE Marketwatch), 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 clips from guys like Serge Millman around the office. A photo of the feereki trader from Star Trek. Anything I took to get myself thinking like a trader: 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 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 professional, 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图标, experiment. Keep CNBC (and the other channels) 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’m able to scalp for 3-5 to 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.

- **Barrier #7: Not managing your physical readiness for daytrading.** I don’t just mean drink a pot of coffee, even though 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 microwave baked potato or have some rice and eggs etc.), keep yourself fit by walking around the block or something
Successful day traders 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 (e.g., spotting gaps up or open, playing the day's gainers/losers correctly, news plays, chart & level 2 sigs, etc.). There is too much financial information available; learning to quickly identify what is important is a skill worth developing.

2. **Keep tiny small stops:** Although I say it way too much, it's the number one day trading skill to master: taking a few small stops so you can profit from large runs to critical. It builds confidence, so I may take $1/100th point stops while trying to find a bottom before it rebounds. 1/2 or 1/12 points that's great. I walk away a winner. Stops should be no more than 2-3 spread max (I usually use 2 spreads w/ micro look at the 1st outside bid/ask).

3. **Post your winning trades around your trade area:** When I get started, I always print out an intraday chart of my winning trades and use a green felt marker 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.

4. **Document your trade losses in your trading journal and look for common themes like the types of stocks you played, the time of day and number of shares you traded each trade.** Standardize what is working for you.

5. **Develop day trading goals and a trading plan you believe in:** Having goals that you believe in is a powerful motivator (read Tony Robbins' stuff). Now, when you 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. On other days, you shouldn't trade at all. On other days, you should trade very aggressively, as your net risk is lower. It's important to identify your goals through, starting with a profit target, so you can budget for living expenses, etc. Also develop a day trading process, 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 day trade in front of me", or "I will keep a 2-stop 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 $TNC $TNP confirm that market direction is headed my way for the next 5 trades.

6. **Share your day trading 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.

7. **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 markets are great. Maybe you're not in a good mood. Or you have a hangover. Or you had a fight with your third wife/boyfriend, etc. Don't trade those days. Just watch, learn, or take a break. Regroup, perhaps take a few days off. For learning, find going to the beach, park, library, etc., is a nice change of scenery. You may be re-reading a day trading book, but somehow reading it in a different place causes you to pay attention better.

8. **Read day trading books often:** My favorite book for getting encouragement is Fredric intrinsic's "Secrets of Successful Day Traders," followed by Schwager's "New Market Wizards" and Peltier's "Mind of a Trader." For the mechanics of day trading, I like Tony Ozi'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 day trading plan.

9. **Find other day traders in your area to network with.** A great example is "Day traders of Orange County," now 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 any meetings for energy, ideas, sympathy, and learning. Day trading can be the world's most lonely profession, so it's important for you to connect with other traders. The chat rooms are not a social substitute, but most do not post good calls.

10. **Commit to your personal success at day trading.** 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 till you believe it. Now say "I trade for a living. I am serious about it." Finally, say out loud "I will be persistent and keep at it until I learn how to day trade for profit." Might take awhile, but I'll get there in time. As I improve my trading skills, I will expect to make higher profits, which will spend on (your choice)." Clearly identify personal benefits to day trading.

11. **Make a list of helpful day trading behaviors for your trading style.** Jot down what you do and how you feel when you're in common day trading 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 the best you can.

**These tips should help your trading results, let me know how they work for you.**
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 of 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.

Successful Trader Characteristics

- Patience
- Discipline
- Trading Skills
- Personal Attitude

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 Self-Assessment: How Well Prepared Are you To Compete Right Now?

Jot down your answers to each of the following 12 questions to help determine your current level of readiness for trading the financial markets. Use it to pinpoint your personal trading strengths and areas for improvement. Take it periodically to assess progress.

Rate yourself on a 1-10 scale on each of the following questions:

1. I'm not yet good at this, I need a lot of work in this area
2. I'm ok at this, sometimes I do well at it
3. I'm excellent at this and could teach others

Patience

#1. I am by nature a patient person and can wait for things to happen.

#2. I have a good sense of timing for stocks and usually wait for the best time to buy and the best time to sell.

#3. I am realistic with myself regarding my expectations from trading and am patient enough to learn how to do it right.

Discipline

#4. When I am wrong in a trade I can recognize it, admit it, and have the discipline to sell at a small loss.

#5. I am decisive and can enter and exit positions based on technical indicators and momentum. My emotions are under control and I am a disciplined trader.

#6. I am disciplined enough to learn and apply professional trading techniques. I discipline myself to learn from my mistakes.
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 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 hide 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 (e.g., 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 (e.g., 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 lost 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 'cage' in a week than 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 to see what the latest up/downgrades and commentaries are.
- You've got your computer on and all your quotestreamer 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 breakfast 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?

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, but I recommend it.

**Premarket Checklist of "Mental Things to Do" To Get Ready for Daytrading:**

Here are 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 your 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 ticker 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 VISA HRL DBCC CCL TU 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 x 16th with a wall of L2 support at 20. I just bought it on a retracement of SPLS at 20 x 16th and fully expect to swing trade it to sell at 21 1/2 or better sometimes 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, a standpoint the last thing you should do is buy a declining 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 totime various things you are doing, to getin the habit of click-on click-off time-based activities. Its a fun way toget yourself in the right frame of mind to do things quickly, and will train you tothink in terms of faster-paced action that is needed in 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 its closing price, the 5-day support and resistance levels, and the maximum stop that you will take - for example if you are trading AAPL and decide to buy on strength at 67, you might want to have a 3/8 point stop.

While this out ahead of the days 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:

- 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 working 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 screenshots of your winning trades) and tape those 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 till 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 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, dock, 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 9am to 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 too late for daytrading. I 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 trade 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.
- Put notes like "High percentage daytrading for daily profits is Required, Kent Continue to Succeed". Your mental frame of mind is so important to success as a trader; risk management and trading techniques are academic 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 "loto" approach). 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 focus 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 you're 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 related 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 eyes and wrist strain related products and equipment layout for your health.
- Step 3: Add the encouraging reminders and trading metaphors 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...
Main Points:

- A string of trading losses, or a “dead portfolio”, can have a seriously 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 at least 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 businessperson, 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 wins 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 “sigh, I’m down $850 on the ELOX tank, now I’m an investor” is terrible. Swear 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

- Do try not 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 some 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 “fights 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. Paper trade until you are good at real trades, or at least trade small shares (100-200) until you are good at it.
- You should look at the big picture, nobody likes losses, even if they’re small. They are better than large losses. Many of your trades are not profitable, though they’re 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. E.g. for every 3 10% point losses you take you also get 1-2% 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

- A large loss is a mistake, no doubt about it. There is 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 overnighting 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 trades are 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 bad date and then never going out with the person again is a “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 shouldn’t have been prevented early on.
- 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 NOW chart. At no time in this trading day did 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 down trend, consolidating in a tight range at 20 3/16 x 3/16 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 unsustained, 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" and "low percentage" plays vs overtrading. An important part of trading for a living.
Module Three

The Mental Game of Daytrading

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/intrusive "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 50% point score. That's profitable for me. Or, maybe I want to scalp a slow mover for consistent 1% a day 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. 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 63% 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 Tassie 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 372 points and winning 1168 how long will you 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 there, for NEON. So let's say you bought it at 57, thinking it sold off "enough" and wouldn't keep going down. Wrong! It keeps plummeting:

Only limit stop up.
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 a 14% point stop on the trade, admitting defeat quickly

d) Decide “I’ll hold on to this stock for a few days or weeks, if it come back some time, it’s a good company, nice analysts ratings, and they just got into a deal with XXX company...”

I hope you’re a DUTU 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 14% 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 scalp's 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 (14% 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 gave 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 65 1/8, it goes up to 65 1/2 now you should have a trailing stop at 55 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 3:4 or 4:1 target.

Like Serge Milman says in Electronic Daytraders’ Secrets (Friedfort/West), these guys are killing themselves losing points and making quartets.

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 at all the time. My broker likes this of course; I try to maneuver for high percentage trades, and don’t mind “flying for the win” a few times, even if I take a few small cuts before I nail a 1/2 point 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 that’s 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 12/12000, 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. 1. 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 was right. A breakout 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.

Buy using limit orders, sell using market orders in fast-moving stocks.

Okay, 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 not to think in absolutes, saying to myself “well I tried to buy WCOM and missed it so now I won’t trade it anymore today”. Instead, be a tighter and if you still have the initial reason to enter the trade in motion in the market for that stock at that time, then buy 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 minecart. 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

Disciplined Trading: 10 Practical Tips to Stay Ahead of Trading Losses

Main Points:
- 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, eat 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 your eye on the % gainers/losers most active 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.amazon.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. e.g. was it the stocks you played (like cheap $5 chartroom pump & dump specially), was it lack of discipline to keep small stops, lack of knowledge of level 2 or chart patterns, etc? 2) paper trade or 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 have made it can be a big confidence builder. I find if I’ve lost and I’m feeling down re-read the "Secrets of Successful Daytraders" by Friederings/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 author’s 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.worldtradingexpo.com/recordings.html and the recordings at www.worldtradingexpos.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 (haha), you may have luck by contacting others in your area.

The worldtraders.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 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 NSFT 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 CEN 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, e.g. trade 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 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 (e.g. I recently swing traded BBCC 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 (e.g. buy 500 at 44 1/8, add another 200 at 44 1/4, sell them all at
Tip #9: Change your trading environment drastically.

Go buy a better chair (I use a leather executive 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), write down your trades on it (wheelies work too).

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 trading 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 it into you, 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 6-10 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, speed 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.
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 arena, 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 day trading, we look for the extremes and play retracements of 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 it's 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 till another trading day).
- Each trading day if it's own "world," spend a lot more time than you currently do looking at the daily composite charts ($COMPQ, $SPX, $T岗$B) as well as sector charts like $RLX $SOX $GIN. This tells you if there's more not 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, for 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 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, as if it wiggles in 16ths in a 14-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 Cyber, Delta 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 scaling瑜ively or flipping 1/64s 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’re 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 add-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 52.5/8 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 300/1000 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.
- 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 300/1000 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.

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 ants go to the other fellow (your small 144 point stop), and when to hold your trade for more profit.

If the cards are against you in a trade after you’ve arro’d up, then give up the trade, take a small hit, and...
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 day-trading-type profit target (recent example: Mar 2000) bought ROST at 13 and sold 3 days later at 15, but holding another week would've given me 22.1. I took a 15% profit but could've had 30% if I'd been more patient with that swing trade. Could've would've should've have no place in our trading self-talk, thought.
  - Every exit and profit target will 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 being 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.

- **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 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):)

  $362 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/loss 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, e.g. it goes from 60 to 30, you buy at 30, the sell target might be 34.50 or so for a swing trade and maybe 31-32 on a day trade.

Trading Areas to Develop Patience In:

- **Be patient with a stock whose price is rising, looking in profits with a trailing stop.**
Personal Learning

- Almost all traders I work with underestimate how much there is to learn about trading stocks for profits—learn patience with yourself.
- You should look at at least 25 stocks a day and highlight those with the most potential. Most of these have few buyers and sellers, but they offer a starting place.
- Going up against the stock market requires a detailed trading plan that's not set in stone. The strategy is the details of learning how to trade.
- To help develop patience in the area, try making a commitment for how many hours each week you will sit aside and learn or do DTV related and Courtney from other sources.

Stock Research/TVDD

- Many traders want the real-time 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 anyway.
- Learning Technical Analysis is a core trading requirement and takes month of study. We provide patterns and training here at the site to help cut, will take you years of practice and market watching before you can correctly identify overbought/oversold/trending stocks that you can trade profitably.
- To develop patience here, use the preprints 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 Buy

- Avoiding cheap or low percentage trades is an important success skill. Most of the time, you will be waiting for the chart, 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 nervous or because of a 10 or 100 point fall.
- Since it's your money, be very careful before you hit the buy button. Enter your positions in small increments, eg start with 100-333 shares and build the position from there, check your jinx in to 1K unless it's really on fire, a rally.
- 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.

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 you require patience, plenty of it.
- To help develop patience in this area, think of the market like a professional class, you don't get excused from much of anything, we know the patterns 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 SPSL trader and buy from 18-20 and sell from 21-25, on swing trades. If I'm day trading, I look for SPSL or the inside bid and know that it gets first peek around 18-19, so I look to buy on open or a bit later after lunch it's still showing strength. That's about it. No magic, no uncertainty, I know this stock and profit from 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 few volatility (but not too much, like SPY/MGT/GENE etc., unless you're a seasoned veteran). 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 IN THE NEXT 16 MINUTES. A big mistake I see far too often amateur day traders make is to enter WAY TOO LATE. You should ideally look at a chart and say to yourself things like "yes the PIVOT entry would have been good, way back at 1134, now it's at 12-7/8 and most of the momentum is out of the stock. I should have bought 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're still off an a down day, or play the afternoon short rallies and bounces.
- Patience is NOT TRADE, is the most important one to develop. Study all the examples at DTU, try to see things from a pro standpoint, why do we call a stock, how closely do we have to fine tune our trades to make it profitable.
- Patience is to Let Your Winners Run (or Swing trades only) in the second most important.
- Nibbles 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 $100 - $250 profit. With 34 shares I want 800-1100 more (unless I am less, but this usually means 1 day's or 10% of 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 sell 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 10th - 15th point stops. No big deal. On buy breaks and set the stop right under the support line.
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 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, Schwager's "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 10:30-11:30 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 & trends

___ **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 predetermined stop loss limits with more discipline and stop killing 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.

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**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 three of us who take it seriously and 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 an actual business? It involves hard work. Lots of self-study, practice, paper trading 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 chat rooms. Beware of bad "idiot traders" out there, hustlers 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-$30 stocks then beware. If nobody says things like "semi's are strong today, the $SOX is up, the trim 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.

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 "get the stock market is tough!" Don't 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 went your money

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**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 3 techniques I am going to start using to be more disciplined in my trading (e.g. tape 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. E.g. 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.
Main Points:

- **Are you tired of losing money in the market?** A lot of "almost got it" 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.

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Trader's "TURNAROUND WHEEL"
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/SCM 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 (e.g. retracement or breakout/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’s 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 stop/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/day trading. 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, Biotechs etc.
- How many shares you trade at a time: Is your average trade size 300 shares? 1000? 5000? 10000?
- 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 O incub to trade 800-share lots of junior stocks like ELOT. You’ve been losing. Well, try switching to better stocks using our trade criteria (Module 1), scaling back to 200-300-share trades, try buying stocks around 10:30 on days that open down (looking at S&P/Q/S), and use cyber or intrading and “teal” 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 mule CNBC instead of following a bunch of losers in a chat room.

**Evaluate**

This is the easiest part. Suppose. Evaluate your daily Profit & Loss, measured in dollars, and put it on a graph. Use a spreadsheet if you want, plot your daily winners.
One thing I did that was helpful was to make a horizontal trading fractions checklist and place check marks near the amount of my winnings 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.

**Trading Times**

<table>
<thead>
<tr>
<th>Date</th>
<th>Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>01/01/2023</td>
<td>10:00 AM</td>
</tr>
<tr>
<td>01/02/2023</td>
<td>11:00 AM</td>
</tr>
<tr>
<td>01/03/2023</td>
<td>12:00 PM</td>
</tr>
<tr>
<td>01/04/2023</td>
<td>01:00 PM</td>
</tr>
<tr>
<td>01/05/2023</td>
<td>02:00 PM</td>
</tr>
</tbody>
</table>

**Note:**

<table>
<thead>
<tr>
<th>Date</th>
<th>Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>01/01/2023</td>
<td>10:00 AM</td>
</tr>
<tr>
<td>01/02/2023</td>
<td>11:00 AM</td>
</tr>
<tr>
<td>01/03/2023</td>
<td>12:00 PM</td>
</tr>
<tr>
<td>01/04/2023</td>
<td>01:00 PM</td>
</tr>
<tr>
<td>01/05/2023</td>
<td>02:00 PM</td>
</tr>
</tbody>
</table>

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 trader/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 addresses of others who've attended, and really check it out. Don't waste days of your life and $5,000 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 audiotape/video/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 bet 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 leagues 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. 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.
Main Points:

- To become a successful trader, you must really believe that it can happen. Many people expect to lose unnecessarily 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 OTU 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 getting played against amateurs who try to buy dips on higher highs or higher highs is frustrating. This is why there are so many reversals and breakdowns 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 efforts, 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 buy yourself up over a dumb trade rather than put yourself in 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, these plays will eat your capital.

Reward yourself for being a Consistent, Disciplined trader that follows a trade plan, whereas 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 click this link from the homepage for a list 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...
- 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 show off with your trading
- Apprehension, worry, concern over personal trading skills.

What else motivates you to trade better, from inside?

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, as 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 stay with them, with small stops and small chance, 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 go through to gain a daytrading lifestyle. How long will each one take you?

It could vary from a month in each phase. Or it could be a matter of months in each phase. 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 "Break-even-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 through 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.bigwaveinvestor.com, use 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 full time 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 picker/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 chatrooms who lose their money. After the April sell-off/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.

I learned 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 multi-million dollar resorts out of thin desert air; they built the playground out of the public's lost money. The banks 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 take 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. It's the small consistent payoffs you're after. You can only get that with a consistent set of trade rules.

Trade well and prosper!
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 weed out some of your thoughts, your plans and ideas for dealing with trading losses successfully.

Small losses/stops are what I call "winning losses" (okay, I'm weird). 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 144 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 becoming 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'ts 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 wobbling up or 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: Stuck in a Breakthrough on Volume
• TA: It was bouncing off support level
• TA: Other Chart Pattern
• News/Earnings/Release Play
• Just thought it was going up
• Inside/Outside/Chamomile Call
• Level of Time and Sales Momentum

Why did you sell this stock when you did? (circle one or more):
• Hit predetermined stop
• Stopped thinking and just 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 about 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 it up and keep 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

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. If you’re to be financially independent, have a great family and live on a tropical island by the age of 30, I did it (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 unprepared to wage war in their trading activities. Of all day trading, the toughest type of trading of all is 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 a 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 breakthroughs 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 1/16 Stop 19 3/8 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 at 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.

   ![Finding Your Trading Discipline Worksheet](image)

   **PTDI: Personal Trading Discipline Inventory**
   
   1. Lack of focus:
   
   2. Lack of discipline:
   
   3. Lack of knowledge of the stock market in general:
   
   4. Lack of planning needs:
   
   5. Lack of self-discipline:

   **Disciplinary Trading Environment:**
   
   1. Get a new computer:
   
   2. Get different trading software:
   
   3. Get a different account:
   
   4. Get a different floor:
   
   5. Get a different firm:

   **My Personal Plan for Discipline**
   
   1. Get a new computer:
   
   2. Get different trading software:
   
   3. Get a different account:
   
   4. Get a different floor:
   
   5. Get a different firm:
The PowerPoint worksheet below is designed to help you identify your trading habits, patterns, strengths and weaknesses.

1. Do you feel like you’re fighting back and forth with the market, like the cartoon on the left?
2. 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 steps” 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 12 point trades than 20% on 1-point “home run” trades. The sign of a professional, in trading like in 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 successful and unsuccessful trading behaviors and patterns

**Instructions:** Complete the form each day when you’ve finished trading for the day. Unlike our earlier technical trade analysis worksheets and audits, this one is designed to help identify and reduce the impact of “emotional trading.”

**Today’s Mental Preparation**
- Calm
- Ready
- Frantic
- Peaceful
- Tired
- Energetic

**Today’s Technical Preparation**
- Knows the key support & resistance levels
- Prepared for unexpected moves
- Ignored the technical analysis
- Lied to yourself about the market

**Today’s Financial Preparation**
- I was ready to go, cash and looking to trade
- I was not ready to go, margin calls
- My broker kept emailing me with new offers

**Readiness To Enter Trades**
- “Scared to trade”
- “Eager to trade”
- “Uncertain to trade”

**Readiness to Exit Trades**
- I didn’t use stops
- Stops were identified
- I didn’t know where to place my stops

**Sensitivity to Market Conditions**
- Ignored the market and sector index direction
- Based on composite and sector index direction
- Ignored the market and ignored other key economic data that were due today

**Hopeful, Greedy, Fearful**
- My trading was highly emotional
- My trading had very few emotions in it
- My trading was highly rational

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**Module Three:** The Mental Game of Daytrading

**Worksheets**

- **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 22.12... 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.

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**Increasing and Decreasing Trade Sizes**

The technique is:

- Adding to a position does not mean “averaging down”, although that may be one technique that...
people are familiar with. As opposed to that (generally losing) method, we want to instead look for ways to dynamically change our total position size based on price action and chart patterns.

Professional day traders 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 up trending position in gradually larger sizes.

Instead, you want to play the probabilities. Let’s look at a few examples:

- Buy/add smaller sizes in winning (up trending for long) positions. If 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: 1 buy 300 DCL at 48 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. Exit them if it drops to 48 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 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.

<table>
<thead>
<tr>
<th>INITIAL BUY OR SELL DECISION POINT:</th>
<th>SECONDARY BUY OR SELL DECISION POINT:</th>
<th>FINAL SELL (or cancel) DECISION POINT:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fill in the blanks</td>
<td>(after you’ve initiated a position)</td>
<td>(as you’re exiting the position)</td>
</tr>
<tr>
<td>TICKER: __________</td>
<td>BUY/near? (add to current position)</td>
<td>SELL THE ENTIRE POSITION?</td>
</tr>
<tr>
<td>INITIAL POSITION SIZE:</td>
<td>SELL? (drop out)</td>
<td>SELL PART OF THE POSITION w/trailing stop for balance</td>
</tr>
<tr>
<td></td>
<td>or, No Change</td>
<td></td>
</tr>
</tbody>
</table>

**Example:**

- I’ve just bought 100 SELL at 16 3/4 (initial size)

- The stock has increased in price to 17 1/8 and has an up-trending wedge ( bullish) pattern, so I add another 100 at 17 3/8

- SELL gets more buyers, we’re up in the high 18’s, I know SELL has a 1-day breakout range weekly, and the trend is up. I put in a stop at 18 1/2 and set my limit at 19.50. Exit at 19 3/4 at 19 1/2. Total profit: $1225
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 bosses, 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 day traders over trade 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:

<table>
<thead>
<tr>
<th>Situation:</th>
<th>Pro Traders’ Action:</th>
<th>Amateur/Losing Traders’ Action:</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Divergence exists in the market, semiconductors (SOX) are stronger than internet stocks (EGBI) today.</td>
<td>1. Ignores all charts for all beta, puts up a few more semiconductor charts to look for trade opportunities (takes 1-2 minutes)</td>
<td>1. Still watches the same group of stocks, including a favorite internet they like to trade. May try to buy the last on a dip, even though the sector is weak that day.</td>
</tr>
<tr>
<td>2. A trade is going against him (or her).</td>
<td>2. Exits immediately, waiting for a better entry price.</td>
<td>2. Waits, hoping for a turnaround. Position goes so far against them they hold onto it, putting another nail in the “dog pound” of stocks they stay long in as an “investor” vs. trader.</td>
</tr>
<tr>
<td>3. Trade is going with him (or her).</td>
<td>3. Takes some fast profit, sells the position off a bit at a time, sees shares at small gain, more shares near the top until position is completely liquidated by the time the stock starts to weaken before lunch.</td>
<td>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 500 shares at a time.</td>
</tr>
</tbody>
</table>
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, breaking out of support or resistance, etc.)
- Choose 1-2 technical indicators you want to use closely. I recommend starting with volume and moving averages.

Market Sector Scan & Analysis

- Identify 2 different market sectors you want to keep a close eye on, and on what exchanges they are traded (e.g. Nasdaq, semis, and the "sector leaders")
- For each sector, identify both the "sector leaders" (e.g. YHOO, EBAY, AMZN, AXL for internet stocks, 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? Was it the "nests"? Software? Biotech? Software?
- Finally, practice paper- and real-time trading stocks within the sector leader for the day you're trading.

Trading Someone Else's Money

- A pro trades with their client's money in a fund account, and the client will actually receive a profit only if they do. 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, e.g. "I want to earn exactly $500 a day each day of April!" says instead "for the month of April I want to earn a profit of $10K, which averages $333/day". Why?
- On strong days you should trade more than on weak or choppy days, depending on your trade style. Do you scalp? You want choppy days. If you're a longer-term trader, you want slow/weak days.
- Also set trading process goals (e.g. "I will trade 100% of the time I see a high- percentage trade opportunity")
Module Three: Activity 2 - “Becoming Focused on the Trade”

- It is essential that you narrow your focus 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 with 50% 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 if 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, 10% of the thousands of people who visit us here at CTU are still using E4.0, 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:
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 “drugs” 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. 
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, e.g. the number P&L +$1,000 in green is a motivator for me, any red 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 watch. I need to check my chart patterns, only carefully pick the high-percentage setups and sit out the "jiffy" - questionable trades, especially longs in a down market, for example.

Module Three: The Mental Game of Daytrading

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 5 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 (e.g. 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 (e.g. avoid trading in lunchtime or other low-volume times).
- You know to give pedestrians the right-of-way (e.g. don't trade against our '4
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 helped 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 on 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. E.g., I have "tight stops - no exceptions" - 2 spread/14 points on 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 GSOC 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 last 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 it in the example below:

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Shares</th>
<th>Trans.</th>
<th>Type</th>
<th>Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>DCLK</td>
<td>400</td>
<td>Buy</td>
<td>42 1/2</td>
<td></td>
</tr>
<tr>
<td>RNWK</td>
<td>300</td>
<td>Buy</td>
<td>38 3/8</td>
<td></td>
</tr>
<tr>
<td>ATHM</td>
<td>1000</td>
<td>Buy</td>
<td>18 1/2</td>
<td></td>
</tr>
<tr>
<td>DCLK</td>
<td>400</td>
<td>Sell</td>
<td>44 3/4</td>
<td></td>
</tr>
<tr>
<td>RNWK</td>
<td>300</td>
<td>Sell</td>
<td>39 1/2</td>
<td></td>
</tr>
<tr>
<td>ATHM</td>
<td>1000</td>
<td>Sell</td>
<td>18 1/4</td>
<td></td>
</tr>
</tbody>
</table>

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:

<table>
<thead>
<tr>
<th>STOCK</th>
<th>Profit/Loss</th>
<th>REASON</th>
</tr>
</thead>
<tbody>
<tr>
<td>DCLK</td>
<td>-300</td>
<td>Bought at bottom end of trading range, sold at resistance</td>
</tr>
<tr>
<td>ATHM</td>
<td>+250</td>
<td>Got stopped out (small stop), chart pattern reversal</td>
</tr>
<tr>
<td>RNWK</td>
<td>+339</td>
<td>Momentum play, Time &amp; Sales was all buyers when I entered</td>
</tr>
</tbody>
</table>

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.

- **Time of Trade Buy/Sell**
  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.

- **The Stocks You Trade**
  Take a close look at the types of stocks you've traded profitably vs the ones you've lost in.

- **Number of Shares Traded**
  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)

- **Trading Equipment/Broker**
  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?

- **Reasons for Buying & Selling**
  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.

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.
Remember the market tank in April and early May 2007? 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 onto success.
- When all else fails, you should increase your efforts, but in entirely different ways than you've taken before. Think about getting, for instance - if you keep missing the bat, 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 Falls...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 cyberloop.com simulators and just speed up your speed 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. CPF T HET MSG JNJ PBG BEY 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
Talk with Other Traders

- Sharing trading stories with other traders in person, by phone and by e-mail 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), 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 Café, 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 e-mail, 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 stop of higher profit targets then we do in daytrading, although you incur greater risks as well.
- If you're consistently losing at daytrading, then take a break, learn a lot more, paper-trade, and then try swing trading with small shares (typically 100-500).
- 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 steps 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, 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 be yourself in a new hobby or something you enjoy (I like watching movies and golfing).
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.

Trading 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 ourtraders.

Click here for Powerpoint viewer program
Click here for MSWord view program (3.5Mega)
- 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!
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 every 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 what to exit vs. stay in the trade, and to not mix up your day trading with swing trading. Do Not hold on to a losing day trade and say "well I guess I am an instant losing 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 trade in a trade to your favor, using appropriate risk management and entry/exit trading skills. Realize that unless you are extremely well-capitalized (e.g., you can tie up $10,000 of capital for extended amounts of time), "if 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 500-2,000 share size swing trades, "casting a wide net into the market" vs. the nail/pinpoint style approach that is required for daytrading.
- One 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 new styles until you come up with the one that best matches your skills, personal expectations, and money management results.
- In terms of your lifetime progress as a trader, I would begin as an investor (buy mutual funds, etc.) for 6 months plus monitoring trade new basics, than move to swing trading (1-3 days to several weeks), then finally, after you know the market fairly well, try daytrading. Then, use the techniques in Module 2 etc. for best scalping profits as a maximum revenue technique. Then, it's fine (and recommended) to stop at swing trading if that's where you make the most money at.
- Daytrading in the broad sense of the word is exceptionally difficult. The Module 2 content has gotten you started on many of the undocumentated yet techniques and strategies that professional day traders use, and you still have a lot of learning to do. The skills you learn here will be invaluable in later modules, as market conditions and trading techniques change over time (e.g., 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/Pacquartball. What are the differences?

Swing Trading vs. Daytrading

**VOLLEYBALL** - slower, lob/spike**

**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.

**DAYTRADING DEFINED**: Daytrading can be one of several types: Scalping daytrades (300-1,000 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 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 and 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 when 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 it's more an "overnight hold play" vs. a swing trade.

STOPS & RISK MANAGEMENT:
- Stops are much wider in swing trading, and your profit objective is larger.
- For overbought 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 use the 20/50/100/200 MAs.
- Stops for swing trades can be as high as 5-10% (but no higher), and if I thought IIMT 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 day traders 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 stochastic, 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:
- Day trading 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 day traders will play for a morning momentum run (in and out multiple times from premarket through 11:30am), 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:
- Day trading stops are never more than 1/2 point or so, depending on the stock price, and usually we 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 okay here, e.g. buy 100 at 50, add 200 at 45, add 300 more at 40 (total average price now at 47). Let's say it corrects at 45-40, then heads back up, your stop is at 45; in 6 days we're at 49-7/8, you sell the whole lot for a $1,200 profit, or hold another couple of weeks and sell at 52 for a bigger profit etc. There are more “downs” in this approach than “ups”, so 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”, e.g. 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 play).

In bottom fishing swing trades, as in daytrades, you must see a volume reversal, showing real buyers are back (not just short sellers), 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 each of 2-6 stocks I'm holding. My current swing trades: DBCC HAS CCL MSK AKOYUM LEX SPLS (SAINT)

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

Swing Trading Strategies

- Avoiding low percentage swing trades and bad investment risks

- 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 "indeterminates" or "tempestuous" trades.

- You should look at 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 & 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 analyst ratings, eg buying highly-rated (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 analyst ratings, although 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 analyst 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 bought into, 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 (e.g. SPLS, NET, ROST, SCGC)

- 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 hold it up for a few days (eg YUM POST ANN Mar 17, 2000).

**Post-earnings gap downs:** If a stock gaps down on recent earnings, it may have buyers over the following days or weeks (eg XRA US CCL).

**Positive analysts ratings:** Overpaid stocks (eg bouncing off a 52-week low or other key support level) that are highly rated (1 or 5) 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 to GCMC DCLX VMTC 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 200DMA bounce for either a momentum daytrade or swing trade.

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 this 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 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's generally not a good idea to hold through earnings releases, as stocks will frequently gap down.

In addition to chart TA, be sure to know your stocks' ratings before buying it. I frequently buy stocks like HRL IHP SPNC DCLX that have good ratings and avoid poorly rated stocks for swing trades. Get ratings at these two links: Zacks and ZacksBigCharts. Below are some examples.

**Good Analyst's Ratings:**

Examples: AOL, DBCC, SPLS: I trade these actively

**Poor Analyst's Ratings:**

Examples: ETYS, BA: I usually don't trade these
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, analyst ratings are frequently uncorrelated with price movement, so you need to use chart technical analysis as your primary indicator, ratings as a secondary. Get bigeasytrader.com (free) for good swing trade research and streaming.

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 run up, “if you missed it you were too late”, don’t chase. Common chart patterns 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, 6 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 6th.

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 48) before buying. Don’t catch a falling knife, you might get a bounce on the way down but it could have a ways further. Eg recently got taken out by CCL, thought 32 was a bottom, actually it’s 22. Missed it.

Buying a cup-and-handle breakout: these are usually a safe breakout play. In this case I was in at the bottom (18 5/8) since I play SFLS 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.

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 OFCL 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.
Module Four
Swing Trading Strategies

Main Points:

- Review our brief guidelines for "how to choose the best stocks for swing trading" 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. In general, swing trading is defined as trading smaller shares (100-300) of the number you most often, may go as high as 100X, 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 at chart patterns, and to a lesser extend, price movements relative momentum, analysts ratings and news, to help decide whether not to enter a position. Charts also 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 stocks are a $4 more valuable for swing trading than for daytrading, but do still when you do your own research and learning.

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 rating, price movement, trading range and overall 1-year trend. This is the widest part of the funnel. Then we drill down and look more closely at the specific supportresistance areas for the most recent 10 days of trading, along with volume patterns before buying.

In daytrading, look at market (Kellycapping), 10-day, then sector (Dow, S&P), then intraday charts, followed by 160, finally using level 2 to time our entries and exits.

In swing trading, we start by looking at the analyst's recommendations (must be >1.5), volume patterns, 1-year chart and it's 300MA, 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 breakout 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 be a $24 stock go up all the way down to $19.314 before a stop is taken. It depends on how many shares you're trading for what time horizon. Of course if I were daytrading the same $24 stock my stops would be no more than 3/8 of a point, more likely just 1/8 spreads.

The point? Swing trading has 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 (up ORCL last summer, CCL now). I generally prefer to hold only 2-10 days max, however, as I do not want to be 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 at 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 don't even 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 (4.7) 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 300MA 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. It 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 covered/buy 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 real-time, 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 5-10% profit, not scalp fractions.

IMGX 1-day/Intraday chart: Ok, now I sold at 14 1/2 (the 2nd top), which was correct, on the 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 13.75 on the open and continued higher up to 15 before being sold off. Instead of taking the first profit (which would have been nice), we waited to see if it would make a higher high.

It didn't, so we sold shortly after the next top, at 14.12. This was the right decision, as the stock retreated back down to 13 at the end of the day.

The play on the day following this pattern? If it drops down to 12.00 and starts to sell then wait for it to get back above 13, if it gaps up to 14-14.12/10, still wait for it to push above 15-16 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 most insiders will try to take out stops at the "obvious" areas. Choose something slightly different.

- In selecting stocks to swing trade, make sure you net buying monolithic expansions, or stocks that have had a huge runup in the last couple of months. Focus on buying towards the bottom of a trading range, and even 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 timing 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, bought at 33, at least 30 and continued all the way down to 20! Or WMT, I bought at 113, it went down to 40! 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 killed in half of its earnings, but it has been able to sustain that level.

As you can see, the first drop, to 22, wasn't the real bottom. That happened a few days later, when it dropped to 13. I think 30-33 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 up out of the pit.

It will have a tough time over the next few weeks but a drop this sharp (like in LGTO) seems a bit much. I could be wrong.
Major Trend

Is “the trend your friend”? Well, maybe, if you buy strong stocks on pullbacks. Overall, though, trends have seemed to work strongly during the first part of 2000 and volatility seems to be the name of the game. So, Buy Reversals and Sell Points in more profitable.

Let’s look at this 1-year chart of DCLX. We have plotted the 200-day MA (white), the 100MA (orange) and the 50-day MA (yellow). Why care about these numbers? Well, an interesting thing here, you see, DCLX has never lost it’s 200MA, and unlike GCOM, 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 DCLX is almost certainly a BUY at 75-80, it’s 200MA, with a stop loss at 70ish.

The 100MA-200MA spread is often a testing range, so you can look to ask the position before it touches the 100MA (or possibly 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 HRR! FC - nice to eat there too. I like to check 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 PIZZA JBP OSSI.

Capitalizing on volatility in stocks like this is a goldmine, look how much it swipes 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 2003) and I would be a long-term buyer of all of them. Same thing with many retailers, such as RSTT WMT TGT ANH etc.
Module Four

Swing Trading Strategies

- 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, it's advisable to look at three main variables: your overall risk, the number of shares you will trade, and the length of time you expect to hold the stock.

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, well 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 $10) equities. Why? You want to limit your risk. Also, I often swing trade as little as 50 shares of expensive yet palatable stocks, between $60-$120/share, for 6-8 point profits over a one-week to two-week time horizon.

You should also have what I call a "time step" on the trade as well - if you're taking 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. The idea is 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 smaller increments to your winner 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 at 300 days later at $48. Add in small increments to your winning swing trades, do not add in larger increments (by 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 of 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.

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Managing Risk in Swing Trades: Time vs. Number of Shares

**Number of Shares to Swing Trade**

"How many shares should I buy?"

**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

Remember, your risk reward ratio is higher for swing trades, so you should buy fewer shares than you would for a daytrade.

Daytrading trades 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 patient cautiously when we trade. The key is to limit your risk in as many ways as 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 10 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 100-300 share increments that are new...
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 you 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 nonperforming “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 16-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 exiting 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 19-20.48 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 chicken-future-charts prediction websites, rather, print out the 3-month chart of your stock and draw out the support/resistance lines and the neckline you will give the trade to be profitable, or to be stopped out of, in.
- Example: If you enter the trade April 15th, maybe give it till the end of the month (or meeting your profit target or stop loss). If it’s still showing around and you’re 2/7 points with no major movement after a couple weeks, consider closing the trade and rolling the money into a different stock pick.
- THE MORE SHAPES 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 minimum. 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 days/days become investment losing 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

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 hand of stocks that you trade simultaneously. I have held anywhere from 2 to 5 different stocks, almost all small shares (100-300 shares each), for a 3-day to 2-week or so held.
- What types of stocks to have? I’d suggest picking 1-2 from each of several different sectors (eg. technology, retail, auto).
- 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.

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 “decimal” 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 lock the profit and re-buy the stock again. If it pushes it’s way through 60, say you might buy again at 61 1/2.

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 5-day chart, I want you begin by to cover up the “left 3 days” with a piece of paper. Now, move the paper down 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? (remember it must be less than 5% of the stock price). Now, how would you figure an exit strategy? Where would you lock a profit, or use a trailing stop? How would you manage your stops for each example?

**BGN:**

- 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?
Managing Your Portfolio: The DTU Rotation Method

When swing trading (which we'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 are 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 stocks.

   Example:
   100 RRIM @ 37
   100 DCLK @ 62
   100 BVSN @ 33
   100 NOVL @ 19

2. Write down major support levels (as 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 those prices).

   Example:
   RRIM Stop Loss = 34.78
   DCLK Stop Loss = 59.34
   BVSN Stop Loss = 29.78
   NOVL Stop Loss = 17.76

3. Write down major resistance areas and profit targets for each stock in the portfolio.
   Example:
   RRIM resistance = 46, exit target = 44.46
   DCLK resistance = 70, exit target = 88.70
   BVSN resistance = 40, exit target = 38.38
   NOVL resistance = 22, exit target = 21.78

4. Okay, now you have a swing trading plan defined. This is critical.
   Another tip to remember is to set 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 60 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, lock the profit, then go buy the other stock, "rotating your capital" into a higher-percentage trade.

Let's say that NOVL drops to 17.76, 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 3.7 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 own stocks all computer stocks, or internet stocks, or brokers.

Try spreading your picks among 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" and diversification strategy.

For example, the stocks in the above example are all from different sectors. You might include 1 semiconductor (eg VDSI VXSK AMD), 1 telecom (T WCOM), 1 wireless (OCM AKHC), 1 retailer (WMF RGST) and one pharmaceutical (AGN OCN), 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 Strategies

Main Points:

1. Moving average lines play an important role in helping you determine where other traders will see support and resistance levels.
2. 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 "breakouts" and "breakdowns" based on these important lines.
3. The most important lines to plot are the 20, 50, 100, and 200 MAs.
4. 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.
5. MA lines are very useful in helping us determine how to play the 5 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 lessons examples below we have a pair of charts: the 6-month "big picture" chart and the 10-day "swing trading" chart.

BREAKTHROUGH SWING TRADING PLAY ABOVE RESISTANCE USING MA LINES

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 buying opportunity. It looks like 40-60 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 50’s, once an 424 and again on 50.

This tells us that if we were to enter a swing trade here we should place our stop loss just right under 424 and again on 50.

Our exit target should be right under the next MA line, the 100 MA, at about 70. So, this swing trade is:

**A Breakout Play would be to buy since CSCO has closed over 70.1/2 or so, with a stop right under 70.** Bottom bounce play. Enter buy at the $55’s, stop loss right under 60, exit target 69/33.

**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 4/30 and 5/1, buy signal on 5/3.

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**MA Lines:** CMGI has ‘least 300 MA support at 81,’ so major trend managers probably won’t be buying till it’s over 81.

Notice that unlike CSCO from above, the MA lines (especially the red 20MA) have crossed over, a bullish 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 is CONSOLIDATION (choppiness) around the 45/70 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.
Finally, we have SPLS, a classic "selling stock." You can see the recent trend is down, and that 22 is hard resistance, as the 30 DMA.

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.

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 1/8 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 chasing playing a stock that’s run up hugely in the last several months. Those are "bubbles" that may burst, like the biotechs did in Jan-Feb 2000.

Your stop on this swing trade would be right under support at 15 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 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 midday trading ranges to help determine good entry and exit points.
- 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.

**Oversold Swing Trading Chart Pattern Using 10-Day & 6-Month Charts**

Notice in this 10-day chart that PSUN has:

1) sold off to a low of 11 1/2-1/2, at which point you see huge buying volume.

2) started to rebound from the 12 1/2 area from a previous 10-day high of 29.

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.
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?

Wait, let's look to exit once right before 15, say at 14.34... sell 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 26 again.

I plot out resistance areas and re-buy once (and if the stock breaks through resistance) buy off support and sell into buyers on the way up.

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 140, and that it's consolidating in the mid 130's range. I would go long if it broke over 145 on volume, or, short it if it closes 130, with a cover stop at 131 or so.

6-Month CIEN Chart:
Notice a couple of key things from the 6-month CIEN chart:

1) It's been in a trading range from 90-110 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 110 support.

3) If a breakout occurs, eg it goes over 150 on strong volume, then it should be bought again.

These are the three messages this 6-month chart tells me. That, and the 300MA 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.

Here's a short-term overbought PUMA chart from Mon June 5th, 2000. We ran all the way from 30 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:
PUMA in a 6-month horizon is telling you what? A couple of things:

1) It sold off form a high of 100 down to 10 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? Today, yes, it wouldn't be a buy at 34 or 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 33ish for an entry at 34. Sell under 30 resistance.

**CHANNEL SWING TRADING CHART PATTERN**

**USING 10-DAY & 6-MONTH CHARTS**

Here's a stock that's been oversold and is relatively safe for a trading channel, prior to a recent breakout, RNNW.

RNNW's 10-day pattern shows you that it rallied between 31 support and 59 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 43ish is support.

How do you trade it? If 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 drop kiss in at 39-38 or so.

What does the big picture 6 month chart tell you here for RNNW?
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 50, 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 in 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

Finally, let’s look at a couple of strongly 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 SELL 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
semiconductors (AVGO, VTX, 3LNK) 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 decent number support level (eg 81.70, 80).

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 3LNK.

Remember, as in any kind of trading, we're always looking for high-percentage trading setups, one's 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.biocharts.com if you don't have a pay quote service provider.

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**Module Four**

**Swing Trading Strategies**

- Understanding the Mechanics of Swing Trading: Recognizing Recurring Stock Patterns & Likelihood of Fibonacci Retracements

**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 stock retracing levels 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 traders, you want to look at the 6-month and 6-month charts, along with the 10-day charts, to establish Fibonacci 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" all during morning trading.
- Review this link for a quick one-page tutorial on Fibonacci retracements at Equities.com. They have a great free online "TA from A to Z" resource there too. It's required reading for everyone, along with consolidation.
- 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 resistance 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 93-94, then settle in at roughly half the distance between the high and low, the midpoint? This is where you should not be trading, long or short, because it's in the middle of your Fibobands and the previous days' high and low support and resistance areas, etc.
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 CHDS chart that:

1) our 10-day range is 7 to 14

2) after moving up, the stock pulled 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 the short in the stock at the top of the range, 13 3/4, the first cover target).

3) buyers bought the stock back up to 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 (50% PSR) trading in this 10-day chart of RRWK:

1) On the chart is blurry, I wanted you to look for the same types of things that I do when trading PSR.

2) The buy on 8/29 was obvious as it was testing a prior low.. the stop loss would be at 44 1/2 or so, but we did not get buyers, at 10 300, 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 (you can spot these in 8/23 and 8/29).

4) the midpoint becomes a new support level for the stock on 8/31, as it went through 47 1/2 on good volumes.

5) It broke out above a key resistance area, 60.

6) The next buy would be above 50 1/2 on good morning volume, with a stop loss at right around 53. Off support
Finally, let's look at 10 days of KANA - another well-annotated chart to help you see the precision with which I track 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 these annotations.

1) Okay, we define our range as 34 1/2 to 40... note that we didn't know where a bottom would attract buyers till 8/28... which is why we just watched it till then. Never try to catch a falling knife; or guess where the bottom is, for all I know it could have gone to 12... I wanted to see buyers come back with enough strength.

2) Having defined our trading range (as 8/28), 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 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... our exit target is right under 40, at, say, 39 5/8 or 39 3/4 or so. We look for a 2 1/2 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 15 1/2 and 27 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 3-6 month) time intervals as well. Apply it to the unique trading style and risk management strategy you have for your stocks.

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**Module Four: Swing Trading Strategies**

**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 daytraders, especially when played premarket over (ESD).
- A note on buying bottoms: frequently, I've found that the first bottom isn't the real bottom, a second falling wave can also follow, which can be painful. which is why stops are so important... look for consolidation (one column to right) before trying to buy a bottom, or an otherwise compelling technical reason on the chart, eg it's bouncing off a 50-week low that's a decade number (like 20 or 30) at 10 3/8 and of course you need to still keep a tight (25%) stop.
- Buying into pullbacks: a stock has been gradually bought over a long time period (eg 36 months) in a slow steady uptrend... you can buy it on a pullback, again with a stop less tight under a previous low.
- Consolidations and why they're important when you're bottom fishing. A consolidation is when a stock has picked up a tight trading range that it hasn't yet broken out of. Let's say AMZI sells off down to 28 and it's within two gaps of 30... you buy it yet? No... you wait for either a sharp reversal (more of a daytrader), or wait for the stock to "stabilize" into a 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 the buyers are in control, at least for now, and a trade can be entered from the long position. The inverse of all this is true for shorts, naturally.
- Another good example is HUFI 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-month and 10-day chart.

Here’s a tip you never hear about when buying into dips for a downtrending stock: Make sure the buyers re-emerge regularly and that it’s not a slow decline with no buying interest. If you see a trend reversing, in other words, make sure there’s some volatility, ups and downs, in the 3-month or 3-month chart if you’re buying into a downtrend. You can see this in the 6-month DISH chart in the above right.

Let’s look at the 10-day DISH chart now for the ‘real action’. Where do you see consolidation in the 10-day chart? The middle 4 days or so, eventually buyers win and the stock breaks above 34 1/2. where a swing trade 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 50-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 29.50. 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 even right above 41 or so. Earnings are due out,
6-month and 18-day HL/IT charts:

In looking at the 10-day chart for HL/IT, we enter a buy after the breakout from the consolidation range of 22-25, say, we buy the stock at 25 1/2 or so. Our initial exit target is roughly 1/2 to half the distance from where it dropped. So it dropped from 41, we buy at 25 1/2 we look to sell at right under 30 (30 1/2) the first time, then buy again at 31 or so and look to sell again at 37.56. Set up the resistance areas at ‘Decade’ numbers like 20, 30, 40, sell at the 0-9 and rebuy in at the 1-2.

Using the Composite and Sector Indexes for 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 $COMPQ is underperforming the $CQMO, so you don’t buy internet stocks yet (wait for key support areas at the $COMPQ for a bounce), and look for other sectors to play in long right now, eg semicon, or networking, whichever strong... use the divergence as a relative strength indicator

BUYING INTO PULLBACK CHART PATTERNS

18-Day CDOV 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 COVID 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’ll sell here and wait to rebuy a dip later. During the run up, you try to buy towards the bottom 1/2rd of the day’s trading range as a general goal.

Looking at RMM here, you see lots of buying over a 10-day period. What do you notice regarding time-of-day effects for RMM? It generally tends to get afternoon buyers, do this is a stock I'd like to buy more often in the afternoon, say 1:30 pm, then in the morning. The low of the day tends to be at 10 1/2 and in the late afternoon as well, say at 3 3/10. These are the buy times for this stock.

Well, that should help with some of the patterns you should be on the lookout for in terms of swing trading bottom bounces and uptrend buying times. Get to know the ‘personality’ of a few stocks and trade these.

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**Module Four**

**Swing Trading Strategies**

- **Identifying High-Percentage Swing Trading Patterns:** It's Saying
  "Buy Me Here"

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**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 60 day consolidation, or a reversal after a sustained decline (cg & finally looks cheap to more buyers than sellers).

- In swing trading, this means we rely heavily on chart patterns, earnings calendars, and market/sector/fledging 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, 2014).

- 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’d 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 upward 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 6/1, so you wouldn’t buy. You'd buy on either of them, eg on 6/300.

Where did we see this? On 6/300 is the trade good for more? Maybe, but I put my first exit target right under the consolidation at 23... since I set out decade resistance I might buy at 16 1/2 and sell at 19 1/2 or so. A stop loss would be at 15, of course.

CREDS Swing Trade

Again, buying the first bottom at 9 on 7/27 would’ve been wrong... also, I didn’t buy 9’s anyways (6,18,29,39,49) since there’ll be resistance at the decade number above it. We saw a heavy volume reversal at 11am on 7/25, 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 at new high of day (nhd) to enter.
MRVC Swing Trade

I just heard about MRVC from Teen 00’s new book. It’s got great volatility for trade.

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 82 or so on the next trading day, and still has buyers at 10:30 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 said 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 3.0 on 8-5.

When do you buy, right, you ask? Well, I would wait till it’s over 40 1/2 resistance in an uptrend and better than average volume, or buy in the box 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 okay 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 WSTL would be ok...

Next entry would be at 12 1/4 on a moving uptrend, with a first exit target right under 20. Swing trade exit is at previous low in the downtrend, say 14 or 15 under 24 (buy 20 1/4, sell 23 1/3 or 26).

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 count in a swing trade.

Bounce pattern: This is typical, look closely at 8/7, you see a morning sell-off, a quick bounce, then it sells a bit and consolidates. The next trade entry would be right above the high of the bounce point on 8/9, about 16 or so. This occurred at the end of the day, so I'd either buy for the next day's gap up (halves), 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 some volatility to take T up a fair amount from its current levels. That is, I'd expect to see 30 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 Fibonacci number), say at 32 1/2 or 33.

USING 1-YEAR CHARTS TO HELP IDENTIFY HIGH-PERCENTAGE SWING TRADES
I also frequently (eg daily, before entering any swing trade) refer to 1 year and 3-month or 6-month charts to identify SMA/200MA and major support/resistance levels.

**RNWK Swing Trade - 1-year chart pattern**

What do we see here? RNWK is in an up trend here and now is a good time to buy the pullback to 40/50.

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 6-8% of the share price, eg 2 points or so, with an exit target of right under 60 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 10K for a single position trade, I’d buy DCLK at 30.

The one-year chart shows we’re testing the 32-week low, and the fundamentals 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 traders, along with ZIIV, RNWK, MRVL.

ATHM Swing Trade-1-year chart pattern

ATHM looks like it’s taken a beating and the sellers have clearly won for calendar 2001. 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 until 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), this stock is highly-rated, as both RNWK an 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).
**Swing Trading Strategies**

- **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 make 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 setup (bottom) in anticipation of an upside gap the next day, that's another story. Some stocks that sell off more than 5% or so on no news may well rebound a couple of days. 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 externals; if the stock has skyrocketed you should sell half your position to lock in profit; holding the balance in case there's an upside gap. If it gapped down, wait, and if it keeps falling, stop out with a partial profit still in hand.
  - When is 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 size you are playing. I'm a big fan of interviewing your share price movement, eg start with 300 shares, add 100 if it continues, sell out 300 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**
**Business: COVD Example**

Here is COVD, a stock that recently sold off to 16 1/2. It has broken through resistance at 15, 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.

**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 it was already in. I would have sold the 16:10am top 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. 03 1/2 if you wish.

**What does the volume tell you?**
Buyers in the air, low volume the rest of the day.
Risky Bottomfishing #1: RHNK Example

It's important to know the trading range and trend for your swing trades. Here are RHNK, it broke over 48 resistance a few days ago and has dropped to near that level today.

I entered a small-share long position on the close at 46-1/8 in RHNK, with a wide stop at 44 7/8.

Why? The stock had plenty of buyers for at least 1/2 of the previous 50 days (closed higher), no advance 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 38-44 range. I believe that it will retreat 50 within a week, however, so I am willing to chance it. I still have a firm stop at 44 7/8. If it gaps lower than 45 on the open and continues to sell off, I'll get out the position, and not re-enter if 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.

Risky Bottomfishing #2: DCLK Example

I bought DCLK on the close at 40 7/8 on Monday... 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 39, which is where my stop is at. Little did it gap open at 41-1/2, and starts to climb the next day. Where do I sell? Right under the previous day's major trendline, at 40 2/8, I'll call at 34 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 6%. 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.
- Steps 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 wait an overnight hold that gap up.
- Remember that gaps on the open of over 5% on volume above 20X attract traders... both on the upside and downside. The 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 generally see 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 10-15 minutes to get a close picture of the market's direction. Cops and handle patterns are important to look for using your 3-minute bar or candlestick chart during the first 10 minutes of the market open.
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 and 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 sell.
- 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 aiming more in terms of a bigger stop, in your swing traders, you must develop the patience to let the trade work in your favor, and not sell it 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 RMM 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 RMM - 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 (e.g. original or quantstocker.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 okay 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 greenest stocks at the top of the list. I’m looking at the deep reds (e.g. over 5% or 6%) at the reds for possible buy-ins if the reason they sold was weak earnings or other major “real reason” for selling. A sell-off above 5-8% in an otherwise flaring market or no news is always a good candidate to look for buy-ins.

In this example, we called VISX as a sell from a previous hold since it’s up 18.8% on the day.

Look at the Big Picture: 6-month, 10-day, Intraday Charts

As we mentioned in Module 1, you should use a “zoom” approach to T/A for your stocks, e.g. 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 14-15, with a recent breakout. Resistance is at 10-20.

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 sell the position right at 19.34, however, and cut out the tug of war between buyers and sellers as it tries to take out the resistance at 20. That’s a low-quit 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 mugging 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 “hard” of paper-trading 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 “Drill” like Homer Simpson when that happens.

But, each 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 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.

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**Module Four**

**Swing Trading Strategies**

- Making the transition from swing trading into day trading, and vice-versa

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**Main Points:**

- Decide whether your trade is a day or swing trade. Before you get into it, you must be allowed to rationalize and set a kind of 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 cheapest online broker (like datek.com or interactivebrokers.com etc) for swing trades and a DAX (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 trading).
- If you are unsuccessful in your current trading efforts, remember to 1) trade the market the way it’s trading, e.g. don’t go long in downtrends, or expect big moves 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 in time-consuming and take a hard look, 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.

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**Going from Day Trading to Swing Trading:**
In switching (or adding) swing trading to your arsenal of trading styles, you take on added risk and potential added reward as well.

Your stops should be wider, and the size of your trade should be smaller (e.g. 100-300 shares).

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.

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:

- MA crossovers, e.g. 20MA, 40/100/200 MAs
- 10- and 30-day trading range support and resistance levels and bounces
- Earnings release dates
- News-related gaps, either direction (up/down) on the open
- Buying feeling pressure in the entire sector the stock belongs to over a 10- day period, e.g. E*TRADE for Internet stocks, $GOO for semiconductor stocks
- Seasonal fluctuations, e.g. retailers, energy strong in the fall/winter season etc.
- Candlestick reversals (1-day charts)
- A single PC monitor, slow 5/10/20  moving average online brokerage account is fine for swing trading
- You do not need to invest in the commission load of a daytrading broker and data feed if you're solely swing trading
- Recommend that you trade a "basket" of 3 to 5 stocks simultaneously with small shares, e.g. 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.
- Picks can be "dead cat bounces", e.g. buying $KSS $CLK 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 (e.g. open gaps down, just like daytrades, but with a longer holding time horizon)
- Ahh, this is fun. The swing traders' personality needs to be a bit more relaxed than the daytrader, as you can panic if the stock loses 1:2 point.
- Conservative, deliberate, patient. Analytical personality types do well with swing trading. Those who are important will stop out of their swing trades prematurely. It takes patience to "let the winners run" and not take profits too early.

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 30 minute round trip trades. It's like racing on a track, you need to know what you're doing.

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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.
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 outline of your trading 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-blank type resources you see.
- 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 midstream, unless you have a significant profit or the position. If you buy off with support being met 435th, sell at 40 1/2 just because you have an open profit, that’s just a trading stop for your trade plan and stock with.
- Recognize that any transition is stressful and take 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 area you feel weak. When in doubt, just take cash. Preserve your capital and be persistent in your efforts.
- Whatever you do, do not let the market take away money from you. Right this list for every 1/4 point and make sure to not be afraid to take small losses, no matter what your trading style is. Keep your emotions in your pocket or your primary goal, using your trading to determine and plan to minimize losses and take gains from the marketplace. For enough competitive games and you need to be on the right side of the trend and not just into the paper match money.
- I feel that the financial news is generally worthless to watch and avoid this year. Instead, focus your energy on playing stocks whose price movements I believe foremost with (like DELL) and tune out the “noise” that the shareholders tend to generate. The more information is usually a contrary indicator. You should be skeptical, not the fed’s, but the profit - those goals are to take your money, or avoid listening to it, not opinions. Listen to the chart, the time & sales, the bottom 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.
Module Four
Swing Trading Strategies

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 pre-nascar 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 unorganized manner. Learning professional technical analysis and trades 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 quarter (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 choice.
- Based on conversations with hundreds of traders, I can tell you that most are weakly underprepared to be trading with real money. For example: Are you still using a 56K internet connection? Do you want to race against your Formula 1 with your Hyundai? I hope not (well at least for day trading… you can swing trade with Goldman Sachs 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 business’ profit and loss/balance sheet.
- Why do most traders fail? They are not serious business people 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 give 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 got frustrated at the unrealistic 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 i.e.
- Let’s take a look at a transition plan he 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, 1-3 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 with capital needs & 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-month part-time successful trading, at this point, you will be ready to trade full time at this point.

For each phase, you need to allocate resources and timelines, 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 F W H takes ESL), the ongoing 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 indices and futures, even though they need to know this stuff. A good overview of the fundamentals is needed to help you understand financial flows at work, and how to profit from them. It is an important thing for short-term traders to know, but it should not be overlooked. It is one of the prerequisites to do well in your trading.

**Products**

You need to develop a detailed plan with key measures, metrics, attached to each step in the process. These measures include your personal trading outcome, eg profit and loss, stop, average profit per trade etc., as well as market measures that are important, such as RSI, indicators, the RSI for specific stocks, industry overview, volume patterns, and numbers, and other T.A. related metrics. Fair value and the impact on opening buying/selling decisions. These metrics are key to your understanding of the market, and how to trade without knowing key financial metrics & their impact on short-term traders.

**Pattern Recognition**

Pattern recognition is probably the single most important skill to learn in short-term trading. By this, I mean both chart patterns, market patterns, and how to read chart patterns, and so on. You are buying and selling peoples’ creations and beliefs in the market, you’re playing people, so you need to know the “mind psychology” as reflected in patterns that you see. Learning price and momentum patterns, pullbacks, average trading range, time-of-day effects and other market patterns will help you get high-potential trading opportunities that you should be aware of. Technical analysis is important, I do not use all of the indicators, but knowing several key ones will help.

**Trading Skills**

You must remember that your goal is to become a good trader. What is a trader? Someone who helps at one price and sells at another 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 where to buy and hold, and when. In short trading, we need to know how to use different order entry types, how to manage trades, handle risk, and turn our trading into a successful business.

**Pantographing**

The next step in your development as a professional trader involves practice trading, and paper trading. This is not enough; you don’t get the experience of real trading with paper trades, so instead use live paper trading to get a feel for how you would take real trades. This is the most important skill you need as a trader, as well as technical analysis and stock pattern recognition. An extension of this is to trade with real capital (30-60 shares at a time) to get a feel for how to enter and exit trades.

**Swing Trading**

After paper trading, you want to do some live swing trading, again with real capital, but with smaller trades in relatively expensive stocks, like $49.99 shares. A real swing trader, over $10, and this requires a lot of patience. Live swing trading should be done for three months, with an average of 5-10 trades per week, to get the initial exposure you need to begin considering trading for a living. This is all preparatory activity, by the way.
After live trading for a while and after you have prepared too, for that matter, you need to evaluate your trading progress. Did you make money or lose money? That’s the bottom line. Also evaluate your trade skills, such as self-management, percentages of trade and profits taken correctly, and other measures. At this point, if you are not making at least 25% return on investment in 2 months of trading you should go back to the first step and repeat. Do not progress past this point until you are at least 30% ROI in 3 months. Example: you started with $25K on July 11 live trading, it’s now Oct. 1, you should have at least $34K.

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 (dynamic trading), equipment such as multiple monitors and a fast PC, perhaps larger apartment or office so you can dedicate a room to trading, etc. Your business plan must include start-up costs, marketing for profit and loss expectations, and other variances 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.

Your goal as becoming a professional trader is to make consistent profits. That’s it. However, losses and favorable gaps are sure, but professionals make money by shorting, buying long, and all the other trade skills that are available out there to get favorable prices. Your goal at this point should be to make consistent profits in your trading while still maintaining a steady occupation for six months time period. If you can earn 45% to 6 months on your capital by trading stocks (not just in a bull market either), then you may be prepared to trade for a living. You have now made the decision and accept the responsibility involved in such a major life event. If you can trade “pretty well” out of the money, and have only a few losses 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.

Getting Your Edge

With support, encouragement, and personal problems and office politics always a threat, it seems that at least being able to take directions financially if you have to is an important skill to develop. Let’s say that you have an “easy” job but you’re trading 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.

If you are not used to being by yourself, if you can’t be by yourself, that is my biggest challenge. I am used to being a teacher and conversational like people. The financial freedom to live where you want and to spend more time with your family is great, though, in time that “never ever get such working like someone else” and if you remember the energy and time without responsibilities there is a lot better to that. Being financially self-sufficient is still hard work, but it’s different nature. You do get more freedom and resources, but it’s more responsibility. The best place is missing your own small business - if you were ever 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 New York and am having the best time of my life. I am my own mentor in my corporate life at Fed, Relevent and McDonnell Douglas (i.e. staff meetings and coffee) but I enjoy the time with my family and the ability to travel and live in New York much more.

I hope you find the trade skills you’re looking for in your trading and professional life, and that this guide has given you some “food for thought” regarding trading lifestyle and independence.
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 (BIGEN sector) may be up and the retailers (SRELX) may be down. Use the relative strength to help you sell into strength and buy off of bottom bouncers and into new breakout plays.

Look at these examples: The overall market has sold off a bit and is consolidating, so you can tell from the black charts to the right, ECOX/PG, Nasdaq Composite and $SPX SP?

Now, look at the bottom three sector green charts below. IGEM - Internet, EPIX, Retailers, $RELX, Biotechs. Which of these three is the strongest? (BIGEN) Which is weakest? (SRELX)

How do you trade them? Well, I’ll look for strength in a bottom stock (egMMN-HEIBI 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 exploit the differences in sector strength

**Step One: Identify Three Sectors You Want to Play**

In the space below, list the symbols (eg: energy, semi, retailers, telecom, software etc.) that you will be playing stocks within. Write down the symbol of each sector so you can track them on your charts. (Note: there’s a link to a list of all sectors on the members home page.)

<table>
<thead>
<tr>
<th>SECTOR</th>
<th>SYMBOL</th>
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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:BPN), you might want to watch AOL, MIND, EBAY, GOOG, CBOG.

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<thead>
<tr>
<th>Stock</th>
<th>Symbol</th>
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**Step Two: Play Relative Strength Patterns**

Now that you’ve identified 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 and exit trades. Use a deadline like this one daily or weekly to help you make a plan for entries and exits. Remember to sell into strength when you see a decent profit, and to exit quickly when your stock loses any support level.

- Stocks I will watch in the sector:
- Stocks I will watch in the sector:
- Stocks I will watch in the sector:

**Module Four: Swing Trading Strategies**

**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 make 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 what 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.
I find that the Bottom "Dead Cat" bounce works best in a 5-day cycle, where the other two take a bit longer to consolidate and are best for up to 10-day swing trading cycles.

Here’s the three patterns we’ve been stressing in swing trading as the most effective ones to play:

Bottom ‘Dead Cat’ Bounce
Trading the Channel: Support & Resistance
Breakout Above Resistance

Please note where “stop loss” appears in each diagram. Discipline to keep this is the most important skill you can develop as a trader.

You should use this worksheet (or a similar one you make yourself) to help you track and capitalize on which of these three patterns you are most effective at using for your swing trades. Note that the timeframe for swing trades is 2 days to several weeks.

Directions:

1. Print out a copy of the worksheet below and use it whenever you are deciding on which stocks to swing trade. Which of the three patterns are you best at, with the stocks you trade? It varies for each person. Personally, I am best at the middle one (channel), 2nd best at bottom fishing and 3rd at buying breakouts.

2. Use this worksheet to help you identify where your strengths are in playing the patterns. Do 80% of your new trades with the pattern you’re most consistently profitable at.

### 5- and 10-Day Swing Trading Patterns Worksheet

<table>
<thead>
<tr>
<th>Stock Symbols:</th>
<th>Pattern You’re Trading:</th>
<th>Entry Price</th>
<th>Exit Price (profit/stop)</th>
<th>Per Profit/Loss</th>
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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

Complete this worksheet for each new position you are swing trading.

Stock Symbol: [Blank]

Trading Range Analysis:
- 10-Day High for this stock:
- 1-month High for this stock:
- 10-Day Low for this stock:
- 1-month Low for this stock:

Stop Loss and Profit Target:
- Stop loss right under previous low.
- Profit target right under previous high.

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:

Factors:
- Min/Max Time of 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:
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Timing Exits: Should be based on the stock total sell-out a trailing stop that you’ve placed on the trade, or the stock has stopped advancing in the time period you’re trading (e.g., it went from 20.12 to 23 and has stayed flat for 3 days) Identify why you exited your next 3 trades in the spaces below:
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Module Four
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.
During your first couple of years trading, you'll want to experiment constantly, working on developing a trading style that works best for you. This also means you should discipline yourself to try new ways of trading.

We present many different trading variations at DTU, in the hopes that you'll be able to find some of the trading styles useful and profitable in helping you make good trading decisions.

Remember to treat trading like a business, and as a small business owner, you want to minimize costs and maximize profits. Would you start a new small business by spending money on lots of things without any business plan or market research? Those that do help account for the 80% failure rate of new small business failures. Same exact thing in trading - many fail because they do not do their hard work and research and stop leaders that are necessary to succeed. You have to do your work and not enter a position and "hope it goes up". you have to know why it may go up, when you'll exit, and how you'll manage the financials.

So many traders are lazy and look for easy money in the markets. Most lose. To guys like me, who do their work and treat this as a business. You simply have to work hard. Period. Gamblers should go to Las Vegas, at least they get free drinks and flashing lights while they lose money.

Traders who are serious, and I know most of you are since you've joined DTU, should expect to work 4-5 times harder than they currently are before they can expect to make profits consistently, for a living. That was my learning curve, and I'm a former F1 engineer/statistician from the Ford Motor Company. Charts were my work life. and trading is much harder than that ever was.

Eventually, you get to a point where you're not surprised by anything the market does, you're skeptical of most trade situations and use a criteria list to rule out trade entities, and go deep when you see a window of opportunity present itself that you feel will work out. It becomes kind of routine, the emotions go away, you know what you're looking for, you make a living at it. The good part is, the hours and pay are a lot better. And the places where you can live. It all counts.

1. Print out a copy of the worksheet below and use the guidelines we've included to help you manage your open swing trade positions.

2. As always, keeping your stops is the most important part of the trade, followed by a profitable exit.

Screensnap: Worksheet 1 - Click here to download Powerpoint worksheet file (43K)
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 WMN T FR HRL HET VSSX 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 EED for 8090 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? If 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.

Swing Trading Strategies

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 (100-300) 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 down trending 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, 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 (best 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 RIMX DCLK SPXL. 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 5-point gap down that would cost you $500 - $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.

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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 (>5% 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 1st-day position, if it drops from where you bought on day 1 then take the stop and look for a better entry on a following day.
6) Don't chase a swing trade, look to enter before 1:30, 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 II chart are important.

Learning how to correctly identify breakouts, trends, and support/resistance lines is critical to becoming a successful swing trader.

Candles are a great tool for 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, so 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 prices 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 exits 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 patterns 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, at 30. This stock could be just an overnight hold, or could be held for additional longer-term gains.
Module Four: Activity 4 - “Playing Positive News and Earnings 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 news, a good recent example is GS GOOGL, 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 overbought condition, selling to buyers who entered later than you did, for a profit, several days or weeks later.
- We'll hope you practice swing paper trading both earnings and news plays in this activity.
- In general, stocks tend to sell off 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 2016, it ran from 12 to 23 then back down to 14 the next day.
- It's tough to play positive news releases unless (and if) 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.
- Buybacks haven't been coming in to scoop up overvalued stocks as much this year, so dead cat bounce days 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 technical indicators (eg stochastic, RSI etc) for the intraday charts you're using, don't attempt these trades if you don't have a professional set up (eg 2 monitors, L2, time decay 1 to 3-minute intraday charts on esignal or RTR etc). Why? Because you'd be trading at a disadvantage, against those of us who invest in those tools.
- Also in this category are Downgrades and Upgrades, a recent tip: look to buy stocks in the same sector that sell off 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 gets sold off "in sympathy with" the stock that got downgraded this is usually best for either a scalp daytrade or a swing trade; SPCE sympathy sell off is >5.7%.
- Papertrade a handful of these as well, it's easy to look at the day's winners/losers within about 20 minutes into the trading day... or look at the most active on ESLO premarket around 9am... see what the crowd's reaction is, in a trend, in 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 these stocks a day or two before the release is due, using barcharts.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 BWSN has a 2-point range)

Paper trade 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 2-week lows for bad earnings, or gapping up (rarely) 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 luncheon 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, or 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 retailer's coffee shops. They release this information Wednesday at 4:30 pm. The stock has 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. Do not do it. Wait at least 10-15 or 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 if it keeps moving on good volume for at least 20 minutes or so early in the morning... usually the gap has "wasted the buying urge" of the public and sellers/shorts 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 under 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.shootoutwall.com or www.cryptotes.com or another service... and, most importantly, you've got a real-time 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 stock's price (eg announced new strategic partnership, won 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.
5. 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.
6. 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 send sell signal orders, selling the stock off... so, wait to make the buyers prove to you that there's buying interest in the stock.
7. For shorting, almost the opposite is true... if you see a "Furniture Recalls" news headline then you may be able to get a short off... because of the spike 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 the day, since you may not get an uptick to short... you might, it's just not as easy.
8. Okay, papertrade the news releases with your real-time 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 there's 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 stock 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.
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 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) the position based on profits you're taking and major swing support and resistance levels.
- A good guideline is to 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" is a good strategy: eg. buy 500 shares BELL at 30, add another 300 at 34 and a final 300 at 35.1/2, sell 500 at 37, sell 300 at 38.34, sell the final 300 at 35.75. As the stock price drops, you want to add the most weight to your position at what you think the bottom is, then add a lot 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 take 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 chasing your swing trades, eg. 3-5 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 reversing on the edge of selling off, etc.
- Some of the types of stocks that are ok for swing trading are ROST, DISH, SRLS, NOVL, SMT, 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 ENOC, SBL, 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 48 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 $60 stock with a $5 range (it's traded in a range or trend from 48 to 63).
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 re-buy 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 re-tests 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 500 when the momentum starts to fade etc... this can be an extremely powerful swing trading 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 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 $XIN, $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.
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 to now you're in the red.
- You may be reading this thinking to yourself, "Well I 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 article, 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. It'll give you what you need to know.
- Here's an example (from my mind, training days). I want you to cross your arms, raised across your chest, right now as you're reading this. Go ahead. OK, now unfold them and cross them the other way. Pulling your right forearms 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, at 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 mainly 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 valid 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 interim 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-holders are, who are sitting in red positions waiting for a bounce. Right?

**Shorting quick intro:**

**What is shorting?** Shorting is simply selling a stock fast, 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 "quick 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 ticker shows a green up arrow, not red down arrow. This means you may only try to enter a short order several times to catch the up tick.

**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 stop loss. A long trade of $100 RYNAK bought at 41 means you have a $4,100 investment at stake, it could conceivably drop to zero, in which case you'd lose $4100. If you shorted RYNAK at 41 it could run to 210, and you'd owe your broker the difference, or (210-41=169) or $16,900. If you're not good about taking stops, then you shouldn't ever short. 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 CEN CNCT 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 gaps up 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 screen maps 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 HLAQ from 53 and it gapped up to 82, wouldn't you want to sell it on the open? Most other people would too, so this is an ideal market to sell stocks as well, shifting it, then covering at the thousand retracements eg down 30% from the high, roughly a third down.

If you see a stock gap up over 40-50% (raw, but it happens), look to short it as well. This is one of the viable parts of looking at the "Day's Chances" lists early in the morning - even as late as 10:00, look for the stock to begin selling off into the gap up and then 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 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 trend line.

For example, FRN60Y loses 40, yard looks to short at 39.94, with a cover stop loss at 40.14 or so. You'd have an exit target at SF-60 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 the new low of the day is hit. We'll show lots of annotated short examples 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 a 2-day 3min candle, intraday 1min stochastic, and 10-day 16 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 trade (try to outguess a reversal) 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 tape reversal shorts: This is your chance to profit from the classic 'gap and trap' play that market makers love to do. On stocks that pull in a 10am high (that is flat to 2-day high), you may want to short it if it starts to get selling into a "microdowntrend". This area 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 pull downwards during the 11:30 to 12:30 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, look up - how many of you have been caught trying to catch a bottom for a stock you think is going to bounce up? We’ve all done it. Sloping 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 then they correctly guess the top. We want to use technical analysis, U1 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 “squashed” here, as everyone rushes to cover their short positions. The market makers step off, and the prices rise. These are good opportunities to getting, when a new-high is made. Do not try to short momentum stocks unless you’re very fast, have very tight scaling-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 60%, eg I nailed the INTC top at +45%, 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 00 support, making a new low for the day. You get the short off at 59 3/4, it wiggles up a bit to 60 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 last 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 retiring 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, 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 500,000 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 incorrectly 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-negotiable are not shortable either (including under-$5 stocks).

Okay, let’s move on to some chart patterns and examples...
Module Five

Shorting Skills for Active Traders:

- Open Shorts: The Safest and Best Short Play

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 oversold stocks (stocks gaps up over 15%) on high volume (over 30k shares traded) 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 falling after the open, eg 10% gaps, and loses a 10-day support level, making new lows. (eg ALT5 closes at 40.34 near the low of the day, the next day's pre-market trading at 40.14, it loses 0.24 on the open at 9:30, short it here with a stop loss at 40 and an exit target of 50 to 100 points.)
- As always, if it's a good idea to place a close short sell 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 downswing on the gap occurs from where the stock was trading premarket. For example, if it closed at 35 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 39.75 by the time the market opens at 9:30, you'd want to consider buying a short at the open (using a cover stop loss at 40 1/4) and an exit target of roughly 1/3 the retracement, at 38 1/2.

How to Trade Open Shorts

Here's a perfect example of an open short play, for a stock called GALT that gapped up over 20% premarket on Oct 17th.

The 2-day chart to the right shows the stock closed at right over 30, and didn't trade on much volume. After a positive news story came out, the stock gapped up to 42 premarket on high volume (over 100k shares traded before 9:30am on Oct 17th).

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 short it because its up 30%, it could end up 40% 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 35 3/4 (exact quote). I advised them to cover around 36 or so (be extrapolated). 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. Is it likely that we didn't get the full range of the chart, we're happy to take almost 4 points (guaranteed) on a 340-point

Let's look at some more examples...

Ebay had run up to 60 and consolidated the day before (Oct 17, 2000), right before the close. If it ran up a bit more on the open here, consolidated a bit more for the first half-hour, then based 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 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 gap up.

Here's Oct, 12th KLAC, a semiconductor company: notice we could have gotten an open short off at 32 on the open, if we were fast... however, I like to wait till it blurs 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 saw 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 3 1/4 points won.

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" either 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 those pro techniques in mind for playing open shorts.
Keep in mind the reasons 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 day trade (day trade w/o a day broker, for that matter). Cover with market buy orders (or OSELS limit/SLD).

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 5-10%, for example. We look to play tight on the long side if they make a new 5-day high or are making a cup pattern. Watch your "daily % gainers" list and look to short stocks that are trading over 60-100% volume or so that have gaps 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 heavy (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 analysis, of course, but because of the upstk 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 "taxi")

Use Fibonnaci retracements to help you identify your targets for where you should cover your open short trades. In the GLAX example above, we don't expect more than 35 out of the trade since that's near a 0.618 line. Your open gap 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: (Previous Next)

Time of day patterns for best short selling: finding the best trading opportunities

**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 breadth market indicators as always, an eye on the Nasdaq TIN, the COMPO, and your sector charts, to confirm the reversals and time-of-day patterns as they occur in the market each day.
  - In time, you will hopefully become more practiced, more "on time" with the market's many pieces 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 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 new "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 dummy shares, 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 he 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 to 12:45 or so. Late entry shorts can often be entered in this timeframe 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 compaq is making new 2-day lows after 2pm or b) the market has run up considerably until 2pm, 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 falter. The key is, you don’t guess at the top; you wait if 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 29-1/4 on the open, traded to 30 decade resistance, then sold off again, the short is at 29-5/8.

**Patterns for 10am Shorts:**

![Chart Image](chart.png)
Sometimes a stock will chop around till around 10am, at which time it makes a break 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 shoot a breakdown.

As you can see from this example, the stock broke down early at 940 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 30 5/8 or so, and it drops to 30 3/4 then starts to bounce, we cover soon with a small 1 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 2% point on $20 $50 stocks are fine to take, they are the 'bake 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:**

Often times 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/liquidity 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: ANAT is stairstepping down in a classic downtrend: lower lows and lower highs all morning long.

**Late Session End of Day Shorts:**
Finally, we can look at late end-of-day selling. There's two main areas to be aware of: one is from 2-3:30, and the other is during the close, from 3:30 to 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 buying or short covering, so, careful holding any short positions post 3:30pm.

Module Five

Shorting Skills for Active Traders:

- Premarket indications for shorting opportunities: chart patterns, news/earning

Main Points:

- We've already discussed how to look for large premarket gaps up, over 3-5%, that are getting set up on the open (bear cup) for 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%.
- We'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 charting 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 20,000 minimum volume by around 9:10 am. If a stock has gapped up a lot or down on just 12,000 volume, for instance, you don't want to touch it... yet.
- We're 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 9:50 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... in the future. If we did that, we'd be investors. (think 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/high02 day lines to help you see what I’m looking at as well. In NTAP we see support at 20 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 11am.
Larger Premarket Gaps Down Under Previous Day’s Low

Remember we typically start looking for bounces in stocks that gap down more than 5.10%, right?

One exception to this is if the stock gaps down to retest the immediate day prior’s low. In this case, we go short. This was under 20, at 19.34.

One good thing about these charts is that you can easily see where your stop-loss would be, e.g., the 19.34 low.

So, a short on the open, around 19.60, would let you cover as low as 18.60 or so before a bounce takes out our trailing cover stop.

For these types of patterns, make sure you have confirming indicators that time is the right now, e.g., your sector charts all gap down a bit on the open, the COMPQ is making a new 52-day low, or is failing off after a huge 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 21.54 a couple of times before letting it go. Once on a breakdown, new low Under the Premarket Low. Bottom is important, make note of it.

That’s also under the previous day’s low.

In this case, we could suitable +1/2 on a short under the 21.54 shot on the open, cover around 21.
Module Five

Shorting Skills for Active Traders:

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 examine in other lessons as well.

Pattern recognition is one key to successful day trading.

By showing you many examples of annotated chart patterns for these short plays, I am hoping 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 of trading experience] should never go against the trend and try to short tops, of momentum runners.

It is always important to remember to use a lower stop loss on shorts, just as in long trades... eg if you're wrong, get out with no greater than a -38 bps, etc.

In general, I like to short under a whole number, stay at the 34 or 50, 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 highs 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, till around 1 or 2... stocks will often pull down during this time frame, making for good shorts. Between 12:30 and 2pm look for 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 more experienced traders only, these are worth learning as well - you need to be very experienced in reading time & price to even consider these. These are following multiple runs up, and are shorts initiated after pulling below a whole number has occurred, eg you see a "bear cup" pattern and have a 10% 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'll take a stop loss on the lunch 2-day breakdown as indicated below.
Lunch Weakness Short

Here’s another example of a lunch weakness short on an intraday chart, PWFR losing support at 35.

We enter the short at, say the 34 5/8, and trail a cover stop down to we’re out at the 33 1/4 area, for a +1 3/8 on it.

Lunchtime seldom gets new buyers, the market is often choppy and/or weak.

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, when 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 TRIX is under 1%, 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 choppied 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 is 1/4) if in long, and possible reversal 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 of the top.

How would you 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 shorting not up but high volume in the consolidation zone at 10:30, telling us a lot of stock is changing hands... bear cup forming from 10:15-11:15 and DJ 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 fact and good with...

Module Five

Shorting Skills for Active Traders:

- TA for Shorting #1: Basic Short Chart Patterns: Identifying Intraday Sell Patterns

Main Points:

- As with your long trades, being able to recognize successful shorting chart pattern setups can help you profit if you learn them.
- You 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 'kicking down, like there's no buyers around', silly 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" them 3-30 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 $20k average daily trading volume.

Pattern recognition, eg "buy 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). Not that this is an open gap down, for which we'd expect a lot of buying. Again, these are intraday plays, so you're entering the short in the early part of the second day. You use 2-day charts for your intraday trading.

**ALTJ Short:** Last 2-day support level at 3-45.

To the right we see an ALTJ 2-day chart 10:30-10:55/2000.

First of all, what's the support level on 10:55/2000 trading day? It was roughly 47.

So you say to yourself, oh, I'll look for a short in ALTJ on 10:55 if it goes 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 10:40.)

Here, we see & got a bit of buying from 10:10, but couldn't get over 47 support (new 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 at 47 3/16.

Where do we cover ALTJ? I typically look to cover around 10:30, since I expect buybacks, but in ALTJ’s case no buyers emerged. An initial short profit of 45 1/4 or + 1.34 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 10:55 in our intraday traininghoopen.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 9:45-10:00 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.
- 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.

**Sell Test:** Using two-day support for an intraday EBAY short:

- Identify the 2-day low/support level for EBAY.
- What is your "short signal" on 10:50?
- Where should your cover stop loss be located?
- Where would you look to exit with profit in this trade (hint: always always always cover shorts before 3:30, since you will have an end of day short cover rally most of the time)

Cup and Handle Breakdowns: High Percentage Chart Pattern

Here we see the opposite of 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 its opening price, look to fire off a short trade. Let's take a look at an example here with CMCAS.

CMCA Short: Last opening price level of 44.14 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 taught to get a short off if there weren't many upshocks to short info. The key is to keep hitting the short button till 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, till right before lunch.

INTC Short: Last 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 till 9:45), then sold off for the rest of the day.

Notice too that the stock is in a technical downward, 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 looking for 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 ATM example below, this pause was at 11:15. Do you see it below? We missed the 12 to 11 tank, but getting onboard with the 11.16 to 10.36 was a bit easier.

ATM Short: Selling from the open, no buyers in sight.

After an initial pause of 9:40, ATM kept selling down from 11 3/4 to 11 1/6, paused for a bit longer, then kept selling off to around 10 support. As with longs, you look to find resistance near decade numbers, eg 10.00, 10.20, 10.30 etc.

Quick ‘solve’ where is the micro-resistance level from the timeframe of 11am 11:30pm etc?

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 or 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. Support off this support level would be 20 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 pullback patterns in the stocks that you trade. Notice that none of these examples tell you to short stocks that are coming up - a common novice trader MISTAKE. You want to Sell Weak Stocks and Buy Strong Stocks. Do NOT try to short a short-term bull, or buy a falling knife.

These patterns are to help you sell weak stocks at the right times, for highest short profits. Good trading!
Main Points:

- In psychology, there is a saying that "past behaviour is the best predictor of future behaviour." In the stock market, we say "buying winners, buying losers." When it comes to repeatable patterns, there are very few, in stock price movements, beyond an initial retracement and false breakouts 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 GLGC chart immediately below, the volume is heaviest at the open/hide, and then down from 12-2 daily.
- How do you use this to profit? Buy on similar patterns day to day, sell short and bounce or short new breakouts/buy new breakouts, particularly when this volume propels the stock price through a 2-3 day high or low.
- Be a detective - look for clues in the stock charts, using all your technical knowledge from previous OTU lessons and other books out there.
- Volatility is important as well - see if a stock is exceeding or nearing its 2-3-day trading range, eg if you know KLC 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 compelling technical breakout.
- Put the probabilities in your favor - make sure to know your stock, 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 sessions.

Using Volume Tracks:
Repeatabale Early/Late Day High Volume Patterns

Let's look at several days of GLGC in the chart below. 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 good 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 low of the range down from 44-1/2 on the open of the second day, we instead waited for it to break the previous day's low, and shorted 33 5/8. The second short entry, on the third day, is again when it breaks the previous day's low, about 32 5/8.

What you want to learn here is how to study the charts like this and see what's going on. That "most of the action" occurs at high volume in the first hour or so of the trading day for this stock. Thus, we know that a stock 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 left (MNCH), that showed us a good short entry under the decade low support, on the open of the current trading day, under 69.56.

Why? Heavy sell volume on the open drags the price down, and our profits go up, as we short the 69.56 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 cap pattern reversal or heavier volume starts to form. That’s our “cover the short” signal, and we’re out at 67.54 or so for a nice 1.88% 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 380.01 on the way down.

**EXTR Close** 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 380.01 on the way down.
Finally, we have CMPC - you can see the first entry was a bit tough to catch, as we went a new low, under a whole number, meaning our short entry is at the $15.50.

It consolidates for awhile, then sells off an 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 3/7/01 than it was on 3/7/01.

Also, you can see CMPC sold off on the open of the previous day as well, another hint that this is a "stock to short".

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**Module Five**

**Shorting Skills for Active Traders:**

- TA for Shorting #3: Using Stochastic Reversals to Identify short opportunities

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**Main Points:**

- Remember that we use several types of indicators in daytrading, those called "OSCILLATORS" (eg stochastic, futures, $COMPQ) and "TREND" indicators (individual intraday charts, 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 set a long trade on a bounce, or where 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 80 on a downtrend, or below 10 on an uptrend. So, they've either gone above 80% and are now headed downwards, having just crossed over each other (time to sellshort), or have droppped 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, like 15/5 (use 15, slower stochastics, in actual oen, see below). So, you use them as a secondary, confirming indicator in your trades, along with other things like the $TINTRO, 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 sharply 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 stop loss, no more than 14 points.

**BVSN Short**

Looking at the stochastic here, we see they gave us an “overbought” pop signal when the price is over 95% and crossed over. The stock price made a pop right after this and headed back down.

You would wait until the stock has lost some of its initial momentum, say 10% or 25%, and enter the short at say 29 3/4 after it made its first peak. You would watch carefully to see if there was support at 28 or below. If there was, you could enter at 28 and re-shoot if it fails to hold 28 3/4, and repeat the short until the stock price consolidates and stabilizes in a range to cover.

Stochastic pools are used to define “overbought” conditions in the stock price. What is the key chart pattern we use? Cup & handle. In the case above, we use the stock price made a “bear cup” from 28 to 29 1/2 and back down to 28 3/4, a conservative entry.

Experienced traders would short the stochastic reversal pop looking for it to lose 10%, after the first stochastic low, and short at 29 3/4. Both strategies worked in this example, for +1 gains.

**Traders’ Plays**

- Practice identifying when the stochastic indicate “overbought” (>90%) and “oversold” (<10%). If you see too many wiggles up and down past these points, readjust your software or adjust your settings on a one-minute candlestick intraday chart.
- You learn to short the reversals in stochastic that get over 90%, also using white 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 to hold it from left to right to simulate the trading day... What do the stochastic 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 limit to them?
- Where would your cover?
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 book will help you, in using stochastics properly.

AAPL Open Short: Lost opening price level of 21 1/2 at 10:00am. 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 (unlike you're a scalper, in which case they're very important) in determining whether or not to enter a trade.

The more thing to look at is the chart pattern, the S&P500, the sector indices, and the time & sales for your stock.

The stochastics level 1 is always of secondary importance. This does not mean you do not use it, on the contrary, you want to use the stochastics to reverse to the downside over 0% 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 time.

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 unimportant information, i.e. 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 indices, like the S&P500 and S&P500.
3. Be decisive on acting as soon as you get a confirming 10x0 crossover signal from the stochastics. They move fast, and as an oscillating indicator you goal as a trader is to use them to rapidly help you fine-tune trades.
4. Be fast to take stop losses when you are wrong, we always advocate 2-3 spread stops for deploying, usually 1/4 to 1/8 point.
5. I use stochastics primarily as exit criteria vs entry criteria for rallies / eg when the stochastics start to go over 80 then lead downwards, I will be likely to sell out a profitable long position and look to enter a short if it is right under a key resistance (eg whole number/10/share price inc level).

Practice using stochastics as part of your trade setup. I put them on my large intraday (10-12 day 9am - 12noon) chart, only. Do not put stochastics, volume and other TA indicators on a list of small thumballer charts, it clutter them. Focus in on a specific trade by putting the ticker in a large, full-screen size intraday chart, that has all your technical indicators on it. Good trading with it!
Shorting Skills for Active Traders: Module Five

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 GSCI (integrated), SSOX (emerging), $GIN (fashion), $SQQ (software), $CP (networks), $SPT (telecom) and $RLX (utilities), $NXT (biotech), for example.
- Learn to recognize variation in chart patterns among those sectors charts. You should use 1-minute 52-day close line charts to follow the various sectors. At first, choose only 2-3 sectors to watch, say the $GIN, $SQQ and $SSLX.
- 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 bounce combined across sector charts” as they may out during the moring, from 9:30 am.
- 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 list of “10” stocks within each sector, at least 2-3 per sector (eg $GIN, EBAY YHOO, $HSD, MDFT ADBE $SQQ $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 and $SPT are weak, we go look to short stocks in that weak sector, eg $COM and others.
- 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 $SQQ and others to ID short sectors

You should have at least 2-3 1-minute 52 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. There 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 SHBA sector is weaker than the other two, as it is just now testing its high of the day, just now completing a bull cup, while the other two S&P and MMUB 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 SHBA (hardware, e.g. 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 select 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 graph box that has only the COMPO and major sector percentages in it.

This gives you a very useful, handy reference for which sectors are under- and over-performing the COMPO, and what their relative ranking is, minute by minute throughout the trading day. Powerful — use it.

This chart tells us that internet are the weakest today, down 3% (now), while retailers were off 2.5%.

**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 EDAY or YHOO (over 1) and trade a low 2, smaller cap stock like PBPT or CIXK 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 9:30 as a key entry point, also after 10am breaks are put in and again near 10:30 (where we'll cover on down days, or at least, tighten up our trading stops).

2-Day New Low in the COMPO = Great Time to Short

The trend is 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 COMPO is making a new 2-day low. This occurred right after 10:15 or so on the 2-day chart to the right, on 2/26/01.

After lunchtime choppiness (expected), the market continued selling down throughout the rest of the session.

Food for thought: what would you do if the COMPO 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.
Avoiding Common Shorting Errors & Mistakes

**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.
- Shooting is primarily for more experienced traders, and is not recommended for first-time 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 market, 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 1.0 point, something's wrong, and you need to pause and evaluate why.

**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, an confirmation of buyers, is the right play. If much more fear of shorting a huge gap down, eg over 8-10% 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 at that day, since the stock opened.

In our live trading room, we nailed the long over 35 38 for good profits. (a competitor 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 it teach you to do.

- 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 trading errors, eg trying to short via SNET when only ECNs are bidding.
- Also, you want to use level 2 in your shorting, yes 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 tradeable 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 have very clear idea on the sales for it.
- That's why I say shorting is for experienced traders only, as you need to get both shorting into the quick play correct, as well as stop analysis and risk management.

Here's a few common errors and mistakes you want to check yourself prior to trading short:
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 OSPN 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 look for 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 bit.

Error #3 To Avoid: Failing to Short a 2-day Breakdown
Example: Watching vs Shorting a 2-day low

Remember to not get paralyzing analysis if you see a solid entry on a technical signal like this one.

The stock, JDJO, is making a 2-day low breakdown under 37. We short it at 36-66, and look to cover around 34 for a nice profit.

2-day breakaways are good to short into, generally speaking, so be prepared to recognize and trade those 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: very experienced traders only, short a stock that is in a mini technical downturn after running up over 12-15% during the first hour of the trading day and is now reversing. Note that is 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**
## Short Trading Journal

Directions: Use this sheet to help you identify the type of short you would take, as well as timing for short trades, compared to when the actual best (approximate) time to short/cover would be.

<table>
<thead>
<tr>
<th>Ticker</th>
<th>Date</th>
<th>Type of Short</th>
<th>Time I would have Shorted it</th>
<th>Actual Best Time to Short</th>
<th>Time I would have Covered?</th>
<th>Actual Best Time to Cover?</th>
<th>P/L</th>
</tr>
</thead>
<tbody>
<tr>
<td>ALTR</td>
<td>1/23</td>
<td>making 3-day low</td>
<td>10:05</td>
<td>10:18</td>
<td>10:20</td>
<td>10:20 (chk)</td>
<td>+ $3.4</td>
</tr>
</tbody>
</table>

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Finding Support and Resistance for Shorts

Complete this worksheet to help you identify chart pattern support/resistance levels for shorts.

On the RMMK 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

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

On the SUNY chart to your left, draw in the following:
1) 2 day support and resistance areas (horiz. lines)
2) Correct short entry (intrady, 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 shares in, on a regular basis (your "core shorting basket")?

<table>
<thead>
<tr>
<th>TICKERS</th>
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<tbody>
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</table>

**What types of short trades** do you think you’ll try to do, primarily? (circle)
- Lining 2-day support (best)
- Intraday range shorts (ok)
- Shooting momentum tops (risky, for pros only)
- Other:

### Short Risk/Trade Management Plan:

**What stop losses will you use, maximum, per trade (circle)?**
- 1.88th - 1/4 point (short selling, scalping-style)
- 1/4 point (two-spread cover stops)
- 1/8 - 1/2 point (wider stops)
- 1/2 point or more (do NOT do this) keep all stops < 1/2

**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 shares)
- Shooting too many shares at first, over 300 shares in your first 5 trades
- Trying to short stocks that your broker doesn’t have short shares for
- Shooting without clearly understanding the best Order Routing choices for you to cover with (I prefer ISLD and SDIES limit orders)

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### Shorting Skills for Active Traders:

#### 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 “gapper” should be for stocks that have gapped up or down 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 for stocks with at least 500k volume that are up 20-30% on the day for these.
- The other “gapper” 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 80 minutes makes reversals every 10-15 minutes and you want to be on the right side of these in both your long and short trades.
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... Be 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 paper trading 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:

Activities

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 login” 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 stock? 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. Paper trade 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 those 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.

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.

- Updated pages within 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, $COMPO and $TRINO 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 viewer program (3.5Mega)

- 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!
Module Five

Shorting Skills for Active Traders:

**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 1994 to 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 not a single rule 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 "walking an order in the other way around." Uncomfortable at first, but it still works! It gives you what you need to know.
- Here's an example (from my morning 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, pulling 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 in 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, at 2 years + occasional swing trading experience.
- I will show you the best ways to short stocks in this module, using current examples, in 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 mainly 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 valid 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 wrong long positions that are reversing; you can sell it out as a profit, then enter a short and ride it down to an interim 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 became 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-holders are, who are sitting in red positions waiting for a bounce. Right?

**Shorting 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 "quick 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 stack 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 upturn.

**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 $4 means you have a $4,000 investment at stake, it could conceivably drop to zero, in which case you'd lose $4,000. If you shorted RNWK at $41 it could run to $210, and you'd owe your broker the difference, or (210 - $41) or $196,000. If you're not good about taking stops, then you shouldn't ever short. 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 my trading style I'm comfortable with. I wouldn't be able to stop, wondering if good news will cause my short to gap up against me the next morning.

Look at stocks like CEN CNCT 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 gaps 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 screens 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 retrace back down will happen. Think about it. If you had a position in HTAC from 52 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 ideal time to sell stock as well, selling it, then covering at the fibonacci retracements, eg down 38% from the high, roughly a 15% 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 Change" lists early in the morning... even as late as 10:00... look for the stock to begin selling off into the gap up and then 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 neckline.

For example, FINWY 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 35-36 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 the day is hit. We'll show lots of annotated chart examples 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 1min stochastic, and 19day 15 min candle charts to trade.

Always pay attention to the sector and index market indexes: short stocks on weak days, buy stock on strong days. Do not trade (try to outguess a reversal) 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 tape reversal shorts: This is your chance to profit from the classic "gap and trap" play that market makers love to do. On stocks that put in a 10am high (that is flat or 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 1:00 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, look up - how many of you have been caught trying to catch a bottom for a stock you think is going to bounce up? We've all done it. Selling momentum stocks is the same exact thing, in reverse.

Do not even, repeat even 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, UI 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 wiggie, 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 goes up. 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 scaling-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 60%, eg I nailed the RONE top at +40%, 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 COC after it force 00 support, making a new low for the day. You get the short-off at 50.24, it wiggies up a bit to 50.74, drops down to 50.14, then runs back up to 50, then goes to 50.14 and beyond.

What's the proper way to have managed the trade? Your cover stop loss should be a bit over at the support level that the stock test that caused you to enter the short in the first place. If you shorted because you think 50 was a key support level that was tested, and your reason for retiring the trade is proved wrong, eg they take it back up over the 50, then you'd want to cover right over 50, at 50.14 max.

Rule #7: As with all daytrading stocks, make sure to only short stocks trading over 500K 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, 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 500,000 shares.

If you're trading a thin stock, you may not get filled in 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 shettable 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 breakout gaps though.
- You should look to short overextensions to news (eg gaps up over 15%) on high volume (eg over 3X screen volume) 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 ALTS closes at 48 3/4 near the low of the day, the next day's premarket trading at 48 1/4, it loses 4 3/4 on the open at 9:30, short it with a stop at 49, and an exit target of 58 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 downside 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 1/2 by the time the market opens at 9:30, you'd want to consider going off a short on the open (using a cover stop loss at 40 1/4) 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 20... near it's low of the day. Then the next day it gaps down a lot 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 1/4. You might look to cover it near a 15-day support level, or, use a trailing-cover stop about 1/4 below 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 afterwards).
- Take a minute to review ModLesson10 and the next lesson as well, stock basics for 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 9:30-9:35, 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% on screened on Oct. 17th.

The 3-day chart to the right shows the stock closed at right over 10, and doesn't trade on much volume. After a positive news story came out, the stock gapped up to 42 premarket on high volume (over 10X screen) and 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 gapping up after the open. Be selective, and then "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 10%. It could cut to -3% or more before topping. Let the chart tell you the story, short only after it loses a support level.

In our Trading the Open, live trading now, I advised traders to "Short GALT if it loses
-30 support, say at 35 3/4 (exact quote). I advised them to cover around 36 or so (too expensive). This was a great trade! Hope this makes sense: 30 (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 chart, we're happy to take almost 4 stocks (guaranteed) on a 540 stock list!

Let's look at some more examples...

Ebay had run up to 60 and consolidated the day before (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 boxed 60 support twice, a double bottom.

We would have been stopped out for a -36 or so loss the first time, but on our re-entry (second time it lost 60), we were in for a nice win as it dropped to 65, consolidated, and sold off down to 50, where we covered, for a + 4.34 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 37 3/4 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, an open gap up.

Here's Oct 17th KLAC, a semiconductor company - notice we could have gotten an open short at 32 on the open, if we were fast... however, I like to wait till 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 saw 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 300 at 27 1/2. Your trades do not have 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 gap (short term or long term). 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", sq 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 margin broker (day trade w/o a margin broker, for that matter). Cover with market buy orders (or SOES limit SLB).

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 >5% for example (we look to play price on the long side, if they make a new 2-day high or are making a cup pattern). Watch your "daily % gainer" list and look to short stocks that are trading over 400k volume or so that have gapped up over 15-20%. 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 heavy (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 analysis, of course, but because of the uptick rule and the dynamics involved as shorting you should pay closer attention to level 2 support/resistance for shorts than for longs. The 5% is more important of course, that's your navigation for the trade (the "headwinds").

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 38 out of the trade since that's near a Fibonacci. Your open gap up will almost never close the entire gap, I look to get out at 1/3 to 1/2 of the retracement range.

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**Module Five**

### Shorting Skills for Active Traders:

**Time of Day Patterns for Best Short Selling: Finding the Best Trading Opportunities**

#### 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 as they play out 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 bread market indicators to always, an eye on the Nasdaq TEDS, the COMPO, and your sector charts, to confirm the reversals and time-of-day patterns as they occur in the market each day.
  - In time, you will hopefully become more practiced, more "in tune" with the market's many pieces 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 anticipate time of day patterns that yield profitable short trades.**
  - 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.
  - 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 perfect. This is why market watching a core basket of 5-8 key stocks for weeks, months on end, doing 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 like a mini-world in itself, you need to stay focused, watch the market, but be prepared to be flexible and trade "what the market is telling you" for each separate session.
- Paper trading, or trading TUI-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 six months initially before doing live trades.

- Let's take a look at some of the timing patterns he 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 to 12:45 or so. Lately, 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 or days where a) the cp is making new 2-day lows after 2pm or b) the market has run up considerably until 2pm, 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, gaps up to meet resistance, and starts to fall. The key is, you don't guess at the top, you wait if it makes a new low of the day, and short under the breakdown.

These are best if they are making a new 3-day low as well (in this example, let's say ORCL traded 30.31 1/2 on the previous day, today, it opened at 29.37 on the open, traded to 30 decade resistance, then sold off again, the close is at 29.56).

![Bear Cup Breakdown Chart](chart.png)

**Patterns for 10am Shorts:**

![Chart with Bear Cup Pattern](chart.png)
Sometimes a stock will chop around till around 10am, at which time it makes a break out 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 9:40 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 9:30 or so, and it drops to 9:30.50 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, traders with over $200 point or 20% stocks are fine to take, they are the "base hits" that are our bread and butter. Of course the home run + 1/4 type trades are great to get as well.

**Shorting Lunch Weakness with the mms:**

Often times 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 man's return from lunch and volume/interest 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: ANAT is stair stepping down in a classic downtrend. Lower lows and lower highs throughout the morning.

**Late Session End of Day Shorts:**
Module Five

Shorting Skills for Active Traders:

- Premarket indications for shorting opportunities: chart patterns, news/trading

Main Points:

- We've already discussed how to look for large premarket gaps up, over 10-15%, 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 charting 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 100,000 minimum volume by around 9:10 am. If a stock has gapped up a lot or down on just 10,000 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 short stocks that are making new 2-day lows at around 5:00 below the whole market that was the previous low/support level. You will see this in the charts below.
- Charts show you 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 (lash 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 20 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 1/4 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 8-10%, right?

One exception to this is if the stock gaps down to retest the immediate day prior's low, in this case the right. TQCC, that was under 20, at the 10 3/4.

One good thing about these charts is that you can easily see where your cover stop loss would be, eg the 19 5/8 low.

So, a short on the open, around 19 6/8, would let you cover as low as 18 6/9, or before a bounce takes out our trading cover stop.

For these types of patterns, make sure you have confirming indicators that checking is the right move, eg your sector charts all gap down a bit on the open, the COMPQ is making a near a 5-day low, or is selling off after a huge 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 testing 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.
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 the entries.
- 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 breakout lows using bear stop 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 hoping that you can learn which shorts are likely to work out, and which types to avoid, based on your trading experience.
- For example, new trades [less than 1 year of trading experience] should never go against the trend and try to short tops, of momentum runners.
- It is always important to remember to use a proper stop loss on shorts, just as in long trades... e.g. if you've gone short with no greater than a -1% loss, ever.
- In general, I like to short under a whole number, say at the 39 or 50, and use the whole number above my short entry as the max stop loss exit to cover.

Major Types of Short Daytrading Plays

(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 day's low, and short under the whole number below the area.

Lunch Weakness Shorts: As we mentioned, look for weakness after 11:30 a.m., till around 1 or 2... stocks will often sell down during this time frame, making for good shorts. Сom веі of 12:30 and 2pm long reversals, on rare occasions.

Morning Top Shorts: Often you will see stocks put in a top at around 10 a.m. 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 turns up, and are shorts initiated after selling below a whole number has occurred, e.g. you see a "bear cup" pattern and have a 1% 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, a 2-day support breakdown only counts out for a short. In this case, we'll 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 example of a lunch weakness short on an intraday chart, PME-5 forming support at 35.

We enter the short at, say the 34.50, and trail a cover stop down to where we're out at the 32.50 area, for a +1.00 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 breaks 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.

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**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 1.00, 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 its 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 is 1/44) 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 shorting 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 of the tag.

How would you 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 if a multiple hit up by high volume in the consolidation zone at 10:30, tell us the stock is changing hands... if bear cup forming from 10:15-11:15 and if finally, most important, a bear cup breakout under the $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 fact and good with.

Module Five

Shorting Skills for Active Traders:

Main Points:

- TA for Shorting #1: Basic Short Chart Patterns: Identifying Intraday Sell Patterns

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 order a short when the stock is making a new 2-day low (except for shorting the bottom of a stock that’s tanked already oversized), of course—i.e., that’s an open gap down, for which we’d expect a lot of buying. Again, these are intraday plays, e.g., you’re entering the short in the early part of the second day...you use 2-day charts for your intraday trading.

**ALT.R Short:** Last 2-day support level was 9-45.

To the right we see an ALT.R 2-day chart 10/6-10/8/2000.

First of all, what’s the support level on 10/04 trading day? It was roughly 47.

So you say to yourself, oh, I’ll look for a short in ALT.R on 10/6 if it looses 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 10:15.)

Here, we see & got a bit of buying from 10:10~15; but couldn’t get over 47 support (new 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 ALT.R? I typically like to look to cover around 10:30, since I expect bounces, but in ALT.R’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 and day traders or covered around 43, for a 44 point gain on the short. (Note: we even called this short on the morning of 10/6 in our live trading-heopen.com forum beta test).

**Traders’ Plays:** What to look for in 2-day support and resistance level short trades:

- Identify the 2-day low/sell level for the stock
- Look to enter a short from 9:45-10:00 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 ISL/ICON or OEXS limit buy order).

**Sell Test:** using two-day support for an intraday EBAY short:

- Identify the 2-day low/sell level for EBAY
- What’s your “short signal on 10:50?”
- Where should your cover stop loss be located?
- Where would you look to exit with profit in this trade (hint: always always always cover shorts before 3:30, since you’ll have an end of day short coverally most of the time).

Answer: EBAY hits a 2-day low when it started tanking on 10/6 and test 62 1/2. Covering by 10:30 or so at 96.
**Cup and Handle Breakdowns: High Percentage Chart Pattern**

Here we see the opposite of our cup and handle breakout on the open, a cup and handle breakdown. Actually, this is more of just a cup... imagine a coffee cup turned upside down, for the price action that you see in the initial part of the trading day. When it loses its opening price, look to fire off a short trade. Let's take a look at an example here with CMCSK.

**CMCSK Short**  
Lost opening price level of 44.14 at 10:45am.

2-day support level broken at 9:45

Our sell short signal is where we indicate it in the chart to the right. In this case, it would be taught to get a short off if there weren't many upsides to short stocks. The idea is to keep hitting the short button till 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, till 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 at 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 first) to enter a short, e.g. finding a 3 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 up tick 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 ATMH example below, this pause was at 11:15. Do you see it below? We missed the 12 to 11 tank, but getting onboard with the 11 to 10 was a bit easier.

**ATMH Short**  Selling from the open, no buyers in sight.

After an initial pause at 9:40, ATMH kept falling down from 11 3/4 to 11 1/2, paused for a bit longer, then kept selloffing off to around 10 support. As with longs, you look to find relatively near-decade numbers, eg 10-20, 30 etc.

Quick selloff - where is the micro-resistance level from the timeframe of 11am 11:15 pm.

Answer: micro-resistance at 10 3/4, notice it couldn't break over that point though it tested it 2 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 or 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 look to cover somewhere before 20 support level, in this case we got strong support all day long at around 21 1/2, so off this support level would be at 21, 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 no selling patterns in the stocks that you trade. Notice that NONE of these examples tell you to short stocks that are running up - a common novice trader MISTAKE. You want to Sell Weak Stocks and Buy Strong Stocks. DO NOT try to short a speeding star, or buy a falling knife.

These patterns are to help you sell weak stocks at the right time, for highest short profits. Good trading!
Main Points:

- In psychology, there is a saying that "past behavior is the best predictor of future behavior." In the stock market, we say "buyers win, sellers win, pigs become bacon."
- When it comes to repeatable patterns, there are very few, in stock price movements, beyond an initial rally and failure of a break 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 OLCG chart immediately below, where the volume is heaviest at the open-close, and then down from 12/2 daily.
- How do you use this to profit? Buy on similar patterns day to day, eg, resist and bounce, or short new breakouts/buy new breakouts, particularly when this volume propels the stock price through a 2-day high or low.
- Be a detector - look for clues in the stock charts, using all your technical knowledge from previous OTU lessons and other books out there.
- Volatility is important as well - see if a stock is exceeding its 20-day moving range, eg, if you know OLCG 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 (past) compelling technical breakout.
- Put the probabilities in your favor - make sure to know your stock, its 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:
Repeateable Early/Late Day High Volume Patterns

Let's look at several days of OLCG 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 good 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 top that of volume down from 20/41 on the open of the second day. We instead waited for it to top the previous day's low, and shorted 22/50. The second short entry, on the third day, was again when it broke the previous day's low, at 20/38.

What you want to learn here is how to study the charts like this and see what I'm doing that "most of the action" occurs on high volume in the first hour or so of the trading day for this stock. This week, we knew that a chart 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 (EWCOT) that showed us a good short entry under the decade '70 support, on the open of the current trading day, under 69.50.

Why? Heavy sell volume on the open drags the price down, and our profits go up, as we short the 69.50 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 67.54 or so for a nice 1.78 short profit.

**EXTRA 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 3/3/01 on the way down.
Finally, we have CMRC— you can see the first entry was a bit tough to catch, as we went a new low, under a whole number, meaning our short entry is at the 15 5/8.

It consolidates for awhile, then sells off down to 10 5/8, 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 3/10 than it was on 3/8.

Also, you can see CMRC sold on the open of the previous day as well, another hint that this is a "stock to short".

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Module Five

**Shorting Skills for Active Traders:**

- TA for Shorting #3: Using Stochastic Reversals to Identify Short Opportunities

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**Main Points:**

- Remember that we use several types of indicators in day trading, those called "OSCILLATORS" (eg. stochastics, futures, STOCHOSC) and "TRENDS" indicators (individual intraday time, 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 RIVETS: when to enter a long trade on a bounce, or where 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. watching 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 is when the two lines, %K and %D, are crossing over each other OR above 80 on a uptrend, or below 20 on a downtrend. So, they've either gone above 80% 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, like 16/6, (use 16, slower stochastics, as shown here, as below). So, you use them as a secondary, confirming indicator in your trades, along with other things like the $TOMO, time & sales, level 2 and chart patterns 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 stop loss, no more than 14 points.

**EYXN Short:** Looking at the stochastics here, we see they gave us an “overbought” pop signal where the peaks were over 80% and crossed over. The stock price made a pop 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 made its first peak. You would watch carefully to see if there was support at 26 whole number, possible cover there and re-short once it losses 27 3/4... repeat the short until the stock price consolidates & stabilizes in a range to cover.

Stochastic peaks 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 26 1/2 and back down to 26 (short signal right under 29), 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, re-adjust your settings till you get clean signals, eg the 90% and 5% settings, on a one-minute candlestick intraday chart.
- You look to short the reversals in stochastic 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 stop to them?
- Where would you cover?
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 idea will help you, if using stochastics properly.

AAPL Open Short: Lost opening price level of $21.12 at 9:30am. 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 more thing to look at is the chart pattern, the EMA/MA, the sector index, and the time & sales for your stock.

The stochastics and level 1 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 80% 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.

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 S&P/ES and ZI.
3. Do decision on exiting as soon as you get a confirming 100 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. When the stochastics start to go over 85% I turn downsides, 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/100/200/500 mark).

Practice using stochastics as part of your trade setup. I put them on my larger intraday (1/2-day 9am - 12noon) chart, only. Do not put stochastics, volume and other TA indicators on a list of small, thumb-sized charts. It clutters them. Focus in on a specific trade by putting the ticker in a large, full-screen 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 COMPO and TRIN, 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 (Internet), $SOX (semiconductors), $MCHI (banks), $YHOO (software), $CP (networks), $SPY (technology), and $BLK (utilities), on the weekly chart, for example.
- Learn to recognize variation in chart patterns among those 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 $SFOO.
- 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 on the chart; c) chart pattern weakness and strength, as seen by “how high are the bounces compared across sector charts” as they play out during the morning, from 9:30 am.
- 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 2-3 “Lead” stocks within each sector, at least 2-3 per sector (eg $GIN, $EBAY, $YHOO, $SFOO, MSFT, ADBE, $SOX, $INTC) etc.
- We look to short stocks that are in the weakest sectors each morning. In real time, 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 $STLC, are weak, we go look to short stocks in that weak sector, eg WCOM and either Intels.
- 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, 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)

![Sector Charts](image)

Answer: the $OHA 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 $GFP and $IBT sectors made bull cup breakouts much earlier in the session, at 10:30. Can you see this? What does it tell you?

The stocks in the $OHA (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 gauge box that has only the COMPO and major sector percentages in it.

This gives you a very useful, handy reference for which sectors are under- and over-performing the COMPO, and what their relative ranking is, minute by minute throughout the trading day. Powerful: use it.

This chart tells us that internet stocks are the weakest today, down 7% (ytd), while retailers were off 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 EBB or YHOQ (i.e., 1) and trade a lower, smaller cap stock like BPPT.OOLK.RMWK 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 breakouts after 9:30 as a key entry point, after 10am tops are put in and again near 10:30 where we'll cover on down days, or at least, lighten up our trading stops.

**2-Day New Low in the COMPQ = Great Time to Short**

```
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<th>Interval Chart</th>
<th>P</th>
<th>V</th>
<th>S</th>
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<tbody>
<tr>
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</tbody>
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```

- 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 2/26/01.
- **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.
Module Five

Avoiding Common Shorting Errors & Mistakes

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.
- Shooting is primarily for more experienced traders, and is not recommended for first-time 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, as you are making money on both sides of the market, and this occurs 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 36% of a point, that’s normal. If you take a large stop, over 1.0 point, something’s going wrong, and you need to pause and evaluate why.

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, an indication of buyers, is the right play. I’m much more leery of shorting a huge gap down, eg over 8-10% 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 gap trap.

You need to look for cup pattern reversals following a gap, and play the trade according to the market trend for that day, since the stock opened.

In our live trading room, we rallied the stock over 30 36 for good profits. (a customer 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 much as you do.

Much of what you find in the way of errors are simple mistakes, eg not using the chart patterns correctly.

Other mistakes may be due to order trading errors, eg trying to short via SNET when only ECN orders are filling.

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 entry timing, 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 skills for it. That’s why I say shorting is for experienced traders only, as you need to get both shorting into the stock 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:

New traders may think to short open gaps down on perceived weakness. This is almost always wrong, we look to buy open gaps of 3-5% on reverse over whole numbers, if it gets a cup long pattern.

Do not short open gaps down unless there is a continuation of the trend, under a whole number.

Here’s an example of BRCD: we traded it long 3 times in a row at TTO after a large gap down.

Would not be a short unless it lost 34 support.
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 $22, it already ran up 2 points", only to see it go up another point and a half, as in this OSPI 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 run 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 'paralyzed analysis' if you see a sold entry on a technical signal like this one.

The stock, JDSU, is making a 2-day low breakdown under 37. We short it at 36-6/8, and look to cover around 34 for a nice profit.

2-day breakaways 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 9:46am or so. Short under whole number resistance, eg at 34.

**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 9:40-10:00am.

**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 downturn 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, lower loss max on these.
## Short Trading Journal

**Directions:** Use this sheet to help you identify the type of stock you would trade, as well as timing for short trades, compared to when the actual best (approximate) time to short it would be.

<table>
<thead>
<tr>
<th>Ticker</th>
<th>Date</th>
<th>Type of Short (2-day low, gap up...)</th>
<th>Time I would have Shorted it</th>
<th>Actual Best Time to Short it</th>
<th>Time I would have Covered?</th>
<th>Actual Best Time to Cover?</th>
<th>P/L</th>
</tr>
</thead>
<tbody>
<tr>
<td>ALTR</td>
<td>11/23</td>
<td>making 2-day low</td>
<td>10:05</td>
<td>10:18</td>
<td>10:26</td>
<td>10:28 (clk)</td>
<td>+ 3/4</td>
</tr>
</tbody>
</table>
Finding Support and Resistance for Shorts

Complete this worksheet to help you identify chart pattern support/resistance levels for shorts.

1. On the RMAK 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

2. 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

3. On the SUNY chart to your left, draw in the following:
   1) 2 day support and resistance areas (hori. lines)
   2) Correct short entry (induced, hori. 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 shares in, on a regular basis (your "core shorting basket")?

<table>
<thead>
<tr>
<th>Tickers:</th>
</tr>
</thead>
</table>

What types of short trades do you think you'll try to do, primarily? (circle)
- Dying 2-day support (best)
- Intraday range shorts (ok)
- Shooting momentum tops (risky, for pros only)
- Other:

<table>
<thead>
<tr>
<th>Notes:</th>
</tr>
</thead>
</table>

Short Risk/Trade Management Plan:
What stop losses will you use, maximum, per trade (circle)?
- 16th - 1/4 point (close trading, scalping-style)
- 1/4 point (two-spread cover stops)
- 36 - 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%)
- 500-600 shares (average daytrading size, after you're doing well)
- >600 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)
- Shooting too many shares at first, over 500 shares in your first 50 trades
- Trying to short stocks that your broker doesn't have short shares for
- Shooting without clearly understanding the best Order Routing choices for you to cover with (I prefer ISLD and SDES, limit orders)

Module Five

Shorting Skills for Active Traders:

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 this link: https://www.yourwebsite.com 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 30-30% 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 40 minutes 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, that's at 24 1/4... Buy the short at 23 3/4 and have a cover stop at 24 or so...
5. Keep track of your open short profitability 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: 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 login" 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 98.7, 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 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, COMPO 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!
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. 

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.

- 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, $STRING 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)
- Scalping 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 Retracement/Pivots

Click here for Powerpoint viewer program
Click here for MSWord view program (3.5Mega)

- 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

- 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
Module Seven

Scanning Strategies and Software

Main Points:

- Scanning Basics Part 1: Choosing the Types of Stocks to Daytrade

- This lesson will help you learn how to select stocks are best for Nasdaq daytrading.
- Start by quickly reviewing the first into module page on the subject, eg avoid the most actives and those with 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 Module 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 times of day, eg 9:30 til 11 am, and be selective in choppy market.
- Stock selection for daytrading is based largely on trading ranges and chart patterns. The volume and volatility are essential to creating profitable trading opportunities are important to learn how to read.
- Scanning through a list of stocks, like those on the line, is done each morning premarket starting at 8:30 am EST, we look for prompt buying/selling/gaps and volatility as an early indication of the market trend. We also look at the COMPO on the two day chart.
- The stocks I'm trading 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 I sector leaders like MSFT, or ones that some of the rooms trade heavily, like JCP, I may use only as indicators, ones I keep an eye on, while trading activity is focused more on ones like VRSN, CHK, ADBE, AMAT, GES, BEAS,
KEY IDEA: Scan for "CLEAN CHART LINES" on charts with WIDE 2-4 point intraday trading ranges and volatility, stocks priced $30-$80 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 XNIX 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 $30-$90 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.
Compare the "good stocks" and "bad stocks" examples below - what differences do you see?

GOOD STOCKS FOR DAYTRADING EXAMPLES:

[Graphs of stock price charts for AOGE and HGSI]
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.

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.
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 "thread the eye of the needle" with some stochastic par 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 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 pattern.

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.
Module Seven

Scanning Strategies and Software

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 greenned, 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 daily 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 Prey day (NEI SOX) Weak prey day (GIN GSO) if you see that in the previous session, say NEI closed +1.5%, 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.dowtradinguniversity.com/5emon.gif] (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:

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Pct</th>
</tr>
</thead>
<tbody>
<tr>
<td>$NBI</td>
<td>+0.8%</td>
</tr>
<tr>
<td>$COMP</td>
<td>+0.3%</td>
</tr>
<tr>
<td>$GNI</td>
<td>0.1%</td>
</tr>
<tr>
<td>$GSO</td>
<td>0.5%</td>
</tr>
<tr>
<td>$SOX</td>
<td>-0.7%</td>
</tr>
<tr>
<td>$GHA</td>
<td>-1.3%</td>
</tr>
<tr>
<td>$GIP</td>
<td>-1.7%</td>
</tr>
</tbody>
</table>

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 trend 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 (Biotech, NBI) and most red (Networkers and hardware, GIP/GHA) and most red by 9:48am?

Note that we usually get quick market reversals around 9:40 to 9:50/10:00 am 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 9:48am, and you are:

a) more skeptical of longs than shorts on an open like this (meaning you're likely to mainly try 2-day 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 biotechs, 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 2-day 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 breaks/day-break tops, eg by making it punch through at least 2 to 4 over the high of the previous trading day, in 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 9:30/9:40 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 chaos 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 off at 4pm in the same rough order as they opened, with biotechs the strongest.

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Pctv</th>
</tr>
</thead>
<tbody>
<tr>
<td>SNBI</td>
<td>+4.8%</td>
</tr>
<tr>
<td>SCOMP</td>
<td>+0.3%</td>
</tr>
<tr>
<td>SGNN</td>
<td>0.0%</td>
</tr>
<tr>
<td>GOSO</td>
<td>0.3%</td>
</tr>
<tr>
<td>SOX</td>
<td>-0.7%</td>
</tr>
<tr>
<td>SGHA</td>
<td>-1.9%</td>
</tr>
<tr>
<td>SGP</td>
<td>-3.2%</td>
</tr>
</tbody>
</table>

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 (HBB) and VRSN CHK (GSO) and AMAT XMLX (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

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Trading 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 Lows? - 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 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 COMPO 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 viewer program (3.6Megs)

- 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/Friends - What do You Do?
- Separating out the Signal
- Scanning Profitably: A Personal Action Plan
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= Updated pages w/in last week.

**Trading 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
- Trading 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 COMPO
- 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, COMPO 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

- 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

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