LAS VEGAS 1998

Simple is Simply Better

Using Classic Techniques to Identify Low-Risk Opportunities

STEWART TAYLOR

Stewart will share with you his simple approach to finding confluences of price, time and pattern that offer low-risk entries and solid stop placements. Workshop attendees will learn how to extract the most meaningful portions from many of the leading technical disciplines. The techniques are applicable across a broad spectrum of time frames and markets, but the workshop will focus on day and swing trading methods as applied to the financial and metals markets.

Stewart will show you how to identify Wyckoff price/volume patterns and behaviors, and how to combine these patterns with simple Elliott patterns, Fibonacci objectives and retracements, sentiment and volume and open interest analysis to arrive at a solid and tradable market opinion. He will show you how he combines basic oscillator patterns with daily/weekly range projections and support/resistance risk points to identify low-risk trading opportunities, placing special emphasis on Wyckoff analysis of accumulation and distribution. He will share many of his basic day trading rules and observations.

Simplifying the decision process removes many of the psychological impediments involved in placing an order and frees valuable time for trading. Sixteen years of real world trading and advising have convinced Stewart that simpler...is simply better.

* * *

Stewart Taylor began his trading career sixteen years ago by trading basic patterns and breakout strategies. These simple strategies evolved into complex day trading strategies utilizing Elliott wave and intraday cycles. Stewart's trading style has come full circle, and he is now a leading proponent of the "simple is simply better" approach.

Stewart developed his analytic abilities as an institutional broker serving the fixed income community with Brittenum & Associates, Refco, Vining Sparks Securities, Shearson Lehman, American Express and Prudential Securities. In 1992, Stewart formed Taylor Consulting Inc., and began publishing his market letter, *The Taylor Fixed-Income Outlook*. The newsletter has been published for profit since October 1992, and subscribers include many primary dealers, international trading desks, hedge funds, money managers, bank holding companies and mortgage bankers.

Stewart, sole owner/officer of Taylor Consulting, Inc., is a Commodities Trading Advisor holding numerous professional licenses. He has given presentations to the Mortgage Bankers Association of America on subjects ranging from inter-market technical analysis to practical applications of options as a pipeline hedging vehicle. His observations are extensively quoted in the financial press, and he makes frequent media appearances.

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PRICE: THE ULTIMATE LEADING INDICATOR

Wyckoff Analysis

The Art of Price and Volume
Reading The Tape

- Wyckoff is the study of price, volume, and the relationships between individual waves of buying and selling. These relationships reflect the balance between supply and demand.

- The market constantly tests the force of supply and demand.

- By comparing the intensity of the buying and selling pressure, it is often possible to ascertain the technical strength or weakness of the trend and the likelihood of the trend continuing or reversing itself.

- Buying and selling waves last as long as they have a following. Once the following is exhausted, the market enters a trading range or changes trend.

- These relationships often allow the analyst to ascertain the behaviors and motivations of large operators (hedge funds, banks, etc.). These operators are considered "smart money".

- Price change = Result. Volume = Intensity of the participants.

- Wyckoff uses three types of charts. Vertical (to ascertain supply and demand), wave, and point and figure. For this discussion, we will focus on vertical charts with volume.

- This type of analysis is a thought process. It is a way of looking at the market that requires judgement (as opposed to a mechanical system).

The Laws

SUPPLY AND DEMAND

- If demand is greater than the available supply, the market will move higher. That is the only way to satisfy the need or want of the composite man. When demand is satisfied, price will stabilize. If the available supply is greater than the composite need, the market will move lower until price has marked down sufficiently to stimulate demand.

EFFORT VS. RESULT

- Price spread should always be proportional to effort expended (volume). If the composite man puts forth a big effort, he should receive a big reward.

CAUSE AND EFFECT

- The extent of a market move is directly proportional to the amount of cause.
- *CAUSE OR POTENTIAL:* The amount of strong-handed accumulation or distribution inside a range. In the case of a bull market, the greater the zone of accumulation, the less supply will be available to satisfy the need of weak hands who enter after the new trend establishes itself. Point and figure charts are used to project move targets based on the width of the range.
- *EFFECT:* The result of the cause that is built. Without preparation building cause, it is very difficult for a significant move to develop.

THOUGHTS ON THE LAWS

- Tops and bottoms aren't usually made until the last short needing to cover is forced to cover or the last fund manager who is behind his duration target is forced to buy. Generally speaking, tops and bottoms are not made by accounts flipping their positions and moving from long to short or short to long.

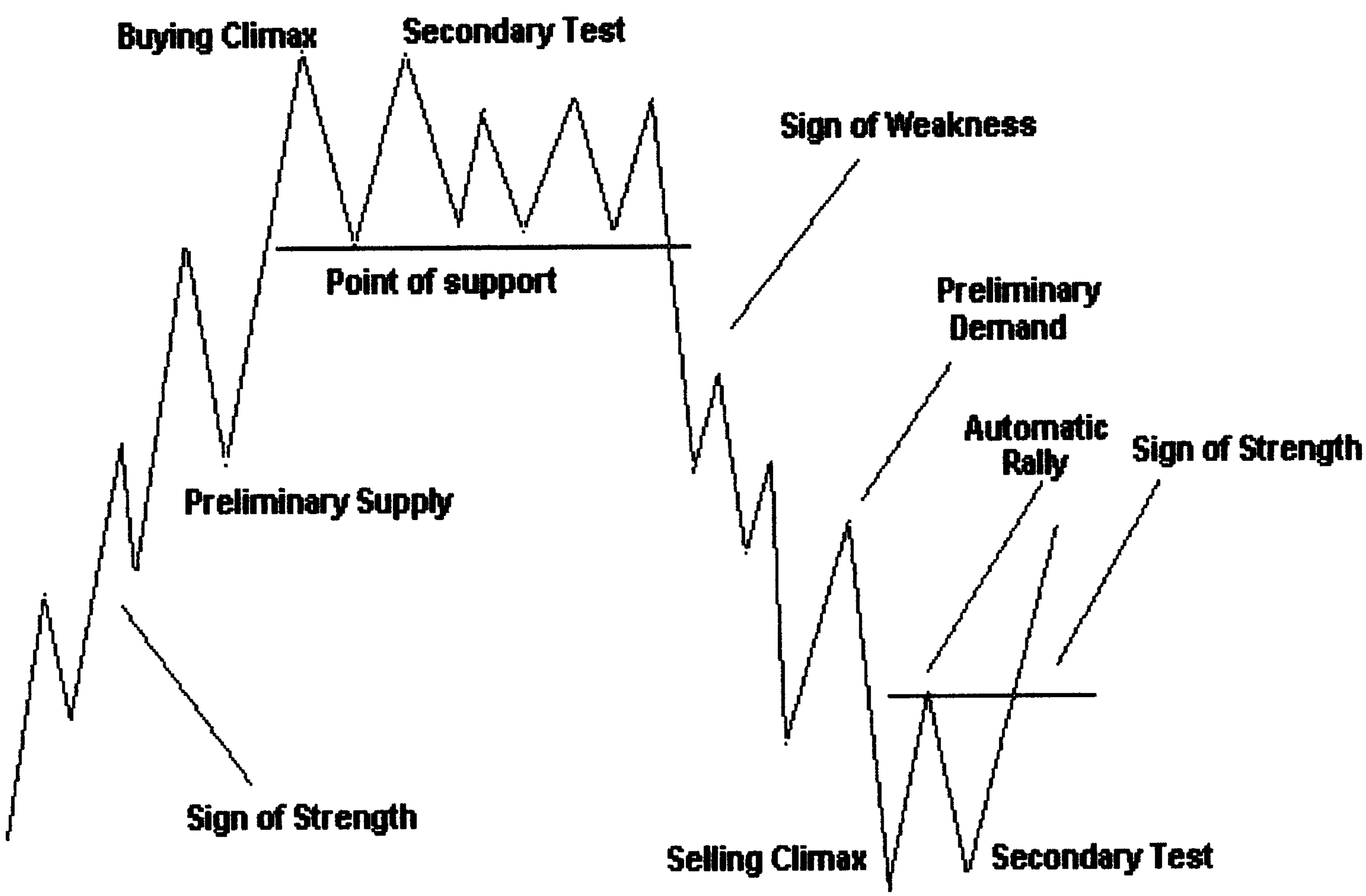
WYCKOFF SEQUENCE

- Market tops and bottoms are usually formed in sequence. A classic Wyckoff bottom exhibits the following elements:

- 1) Preliminary Demand. 2) Selling climax. 3) Automatic Reaction. 4) Secondary Test. 5) Sign of Strength.

- The general consequence of this sequence is a change in trend or strong counter-trend reaction. The counter trend reaction often takes the form of a trading range.

- This sequence repeats itself endlessly as large operators (strong hands) complete their buying and selling campaigns and small traders take poorly informed market positions. The sequence can be found in both short term (one minute charts) and long term (monthly and yearly) charts.



PRELIMINARY SUPPLY\DEMAND

- After a protracted downtrend, the market will often display a rally that is notably stronger than any preceding rally. This rally often occurs as the market approaches a preexisting price objective. The rally rarely manages to threaten the downtrend.

SELLING\BUYING CLIMAX

- The days leading to a selling climax are generally high volume days with expanding or wide ranges. The heaviest volume occurs either on or just before the highs. Generally speaking, a climax only occurs after a prolonged move and is often preceded by the market entering a parabolic advance/decline.

- In the case of a bear market climax, accounts that have resisted the idea of a bear market (weak hands) finally throw in the towel (panic) and sell while weak handed, poorly informed traders finally initiate speculative shorts. A selling/ buying climax may be complex (bonds usually are) and may prove temporary.

AUTOMATIC RALLY

- The selling climax exhausts the available supply and results in a reflex rally. This rally eventually attracts sellers who resisted selling as the market was falling to its climax and elicits profit taking from buyers who had the foresight to buy near the climax lows. The rally is typified by lower volume, generally fails to take out any important overhead resistance, and tends to lasts several days.

SECONDARY TEST

- The secondary test confirms the selling climax. The market declines back into the area of the selling climax. A classic secondary test will result in the market finding slightly higher support. The volume and the price spread should be noticeably lower than the volume during the selling climax.

TYPICAL RESULTS OF A SECONDARY TEST

- 1) Support is nailed down and confirmed. 2) The market will enter a fairly wide, lateral trading band in preparation for a corrective rally or a resumption of the decline. This range will have to be evaluated for clues of distribution or accumulation. 3) A sign of strength will often develop that takes the market above the high of the automatic reaction.

SIGN OF STRENGTH

- After the secondary test the market will enter a range of accumulation, and eventually, if the trend is changing, exhibit a show of strength. This show is characterized by wide daily price spreads, stronger volume, and a move above the top of the automatic rally. A sign of strength after accumulation is the final step in the trend change and almost always represents a "go with" situation.

NOTES:

- Climax structures can be found in any degree or perspective, but the importance of the climax is directly proportional to the degree in which it appears. For instance, a selling climax on the hourly chart can lead to a three to four day rally, after which the daily perspective downtrend can reassert itself.

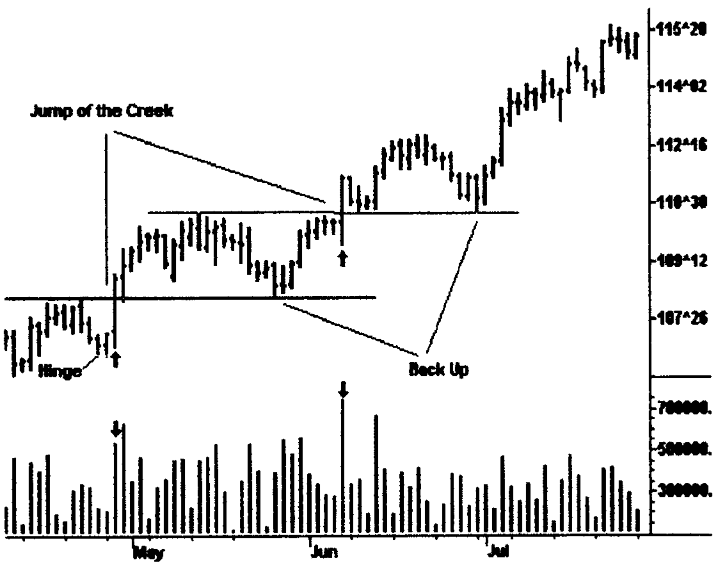
- No two sequences are the same. There are almost always variations on the theme.

- Bonds often make complex buying and selling climaxes. Often, the market closes on or near the low of the climax structure and then reverses the next day.

- Bonds tend to put in complex secondary tests. Often the selling/buying climax will be exceeded by a small amount (typically less than 1/2 point) before reversing (leaving in place an isolated spike).

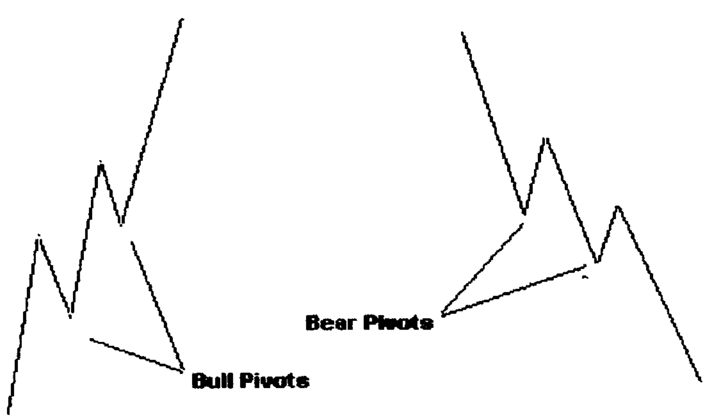
Jump of the Creek / Fall below the Ice

- After a period of preparation, the market jumps above the top of the trading range (the creek).
- Note that volume and price spread expand, and that the "back up to the creek" provides a low risk buying opportunity.
- Volume and price spread on the test of the creek should be lower and narrower than on the initial rally after breaking out of the creek.



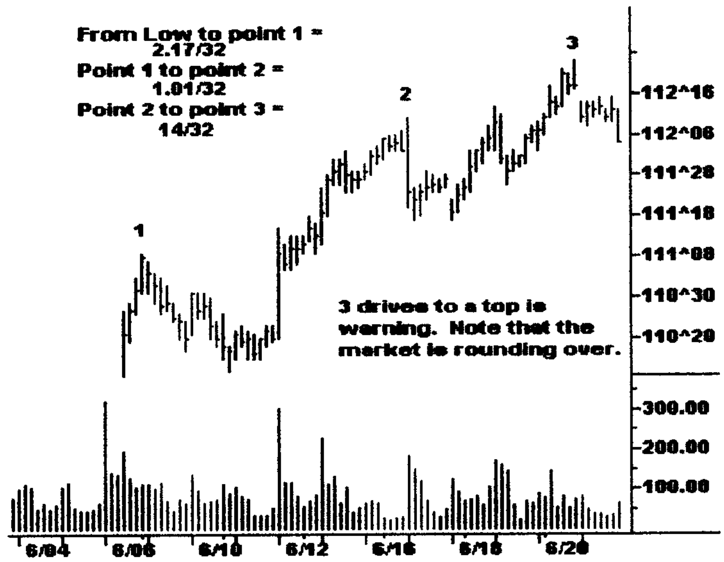
Pivots

- A pivot represents a chart point where supply overcame demand or demand overcame supply.
- The manner in which price approaches a prior pivot is important.
- Increasing volume suggests that the pivot will be taken out.
- Lighter volume suggests that the pivot will hold.
- Volume should decrease on the corrections and expand on the impulses.



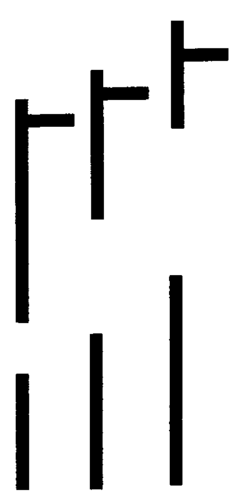
Three Drives To a Top/ Poor Result of Effort

- Despite solid effort, each drive covers less ground than the preceding drive.
- Remember that volume expended = effort and that price spread = result.
- The poor result is a strong indication of supply.



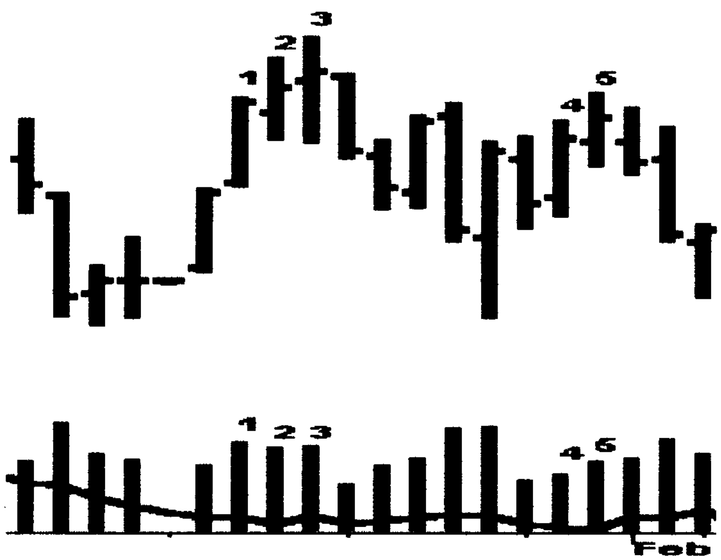
Poor Net Result of Effort

- Volume is expanding as the market moves higher.
- Net daily gain is small.
- Supply is overcoming demand.
- The market is vulnerable



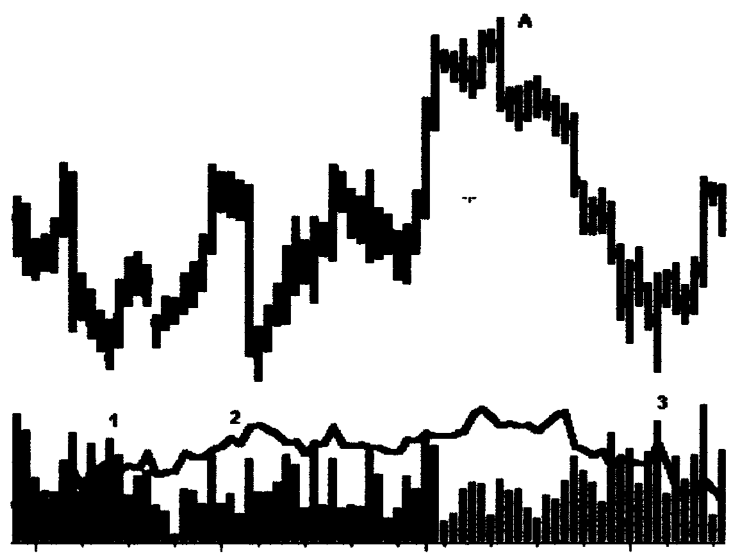
Retest & Poor Result of Effort

1) A high volume up day.
2 & 3) Volume stays high (2 day volume @ 800,000 contracts). Closing price only moves 12/32 higher over the two days of effort.
4&5) Market moves back toward the high but volume and price spread promptly pull back.



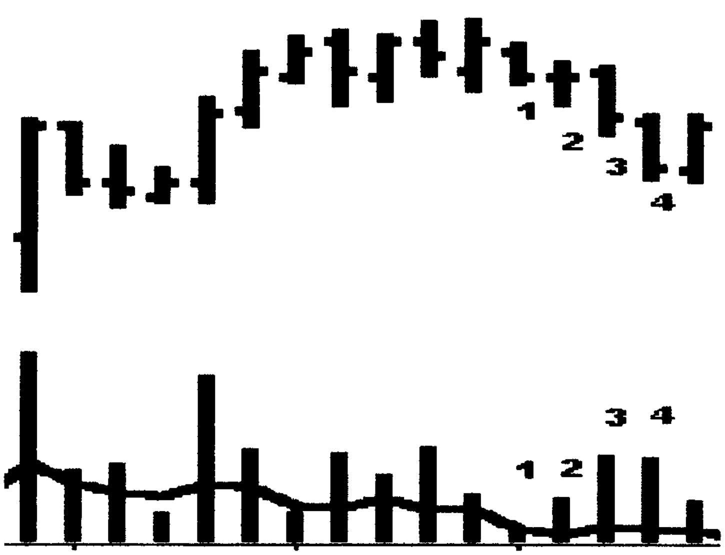
Light Volume Retest

1) The market bottoms. Note that the volume to the left of the low is quite high.
2) A wide bar down day, but note the generally lower volume and that the day after the wide bar down that the selling pressure was minimal. The next rally (to point A is on generally lower volume.
3) The decline to point 3 is on much lighter volume, and generally narrower price spread, than the decline to point 1. Sellers are less enthusiastic.



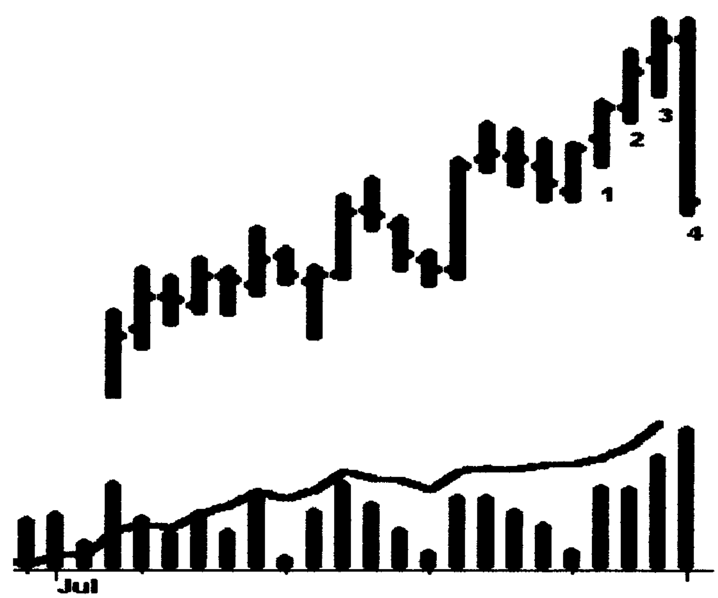
Correction

1) Volume promptly pulls back in comparison to the recent past.
2) Price spread narrows.
3) The correction finds support at approximately .382% of the prior rally.



Buying Climax and Poor Net result of Effort

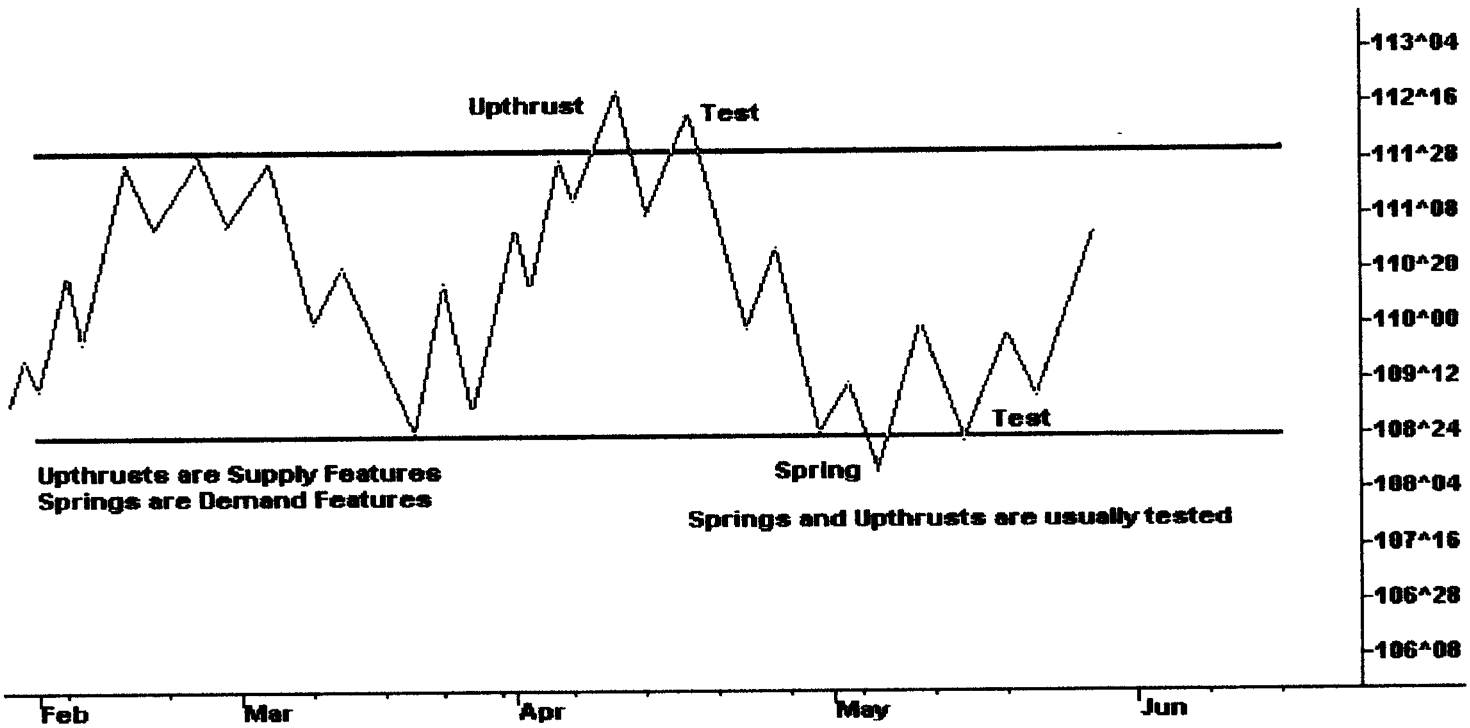
1) Prolonged Uptrend.
2) Days 1, 2, & 3 evidence very strong volume (three day total of 1.5mm contracts). Open interest increases almost 50,000 contracts over three days.
3) Poor net result of effort
4) Sign of weakness.

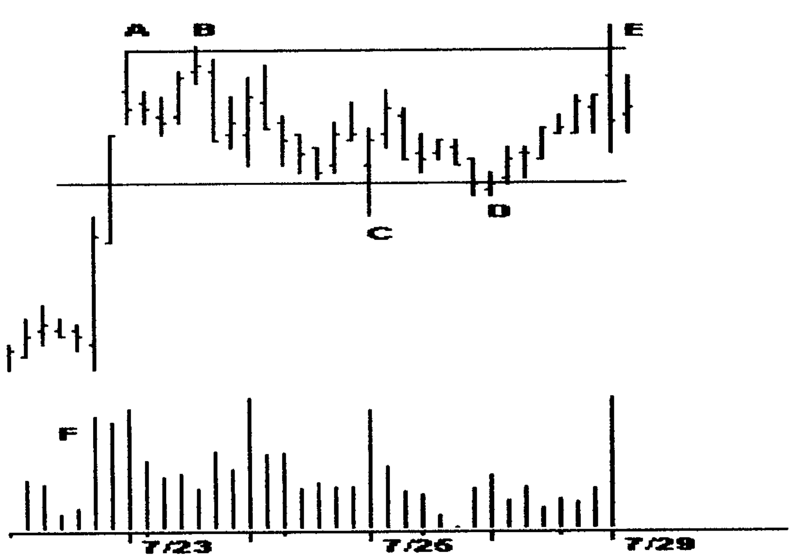


SPRING & UPTHRUST

- Springs and upthrusts occur as price moves above or below a strong pivot, or beyond the fringe of a trading range, and suddenly reverses. The appearance of an upthrust strongly suggests that quality supply is present. Springs can be classified as demand features. Upthrusts can be classified as supply features. Springs and upthrusts are usually tested.

  1) The structure should find support/resistance at a reasonable level.
  2) The structure should quickly reverse itself.
  3) The structure is usually tested on lower volume.
  4) The structure often marks an important turn.
  5) The action tends to shake positions from weak hands to strong hands.





Buying Climax, Spring and Upthrust

- Point A: Buying climax. Note the three consecutive high volume bars (F), the parabolic nature of the advance and the close well off the high of the bar.
- Point B: Test, note the lower volume.
- Point C: Spring.
- Point D: Test, note the lower volume.
- Point E: Upthrust.

Note: That the buying climax and the upthrust both appeared in the area around a prior bull pivot.

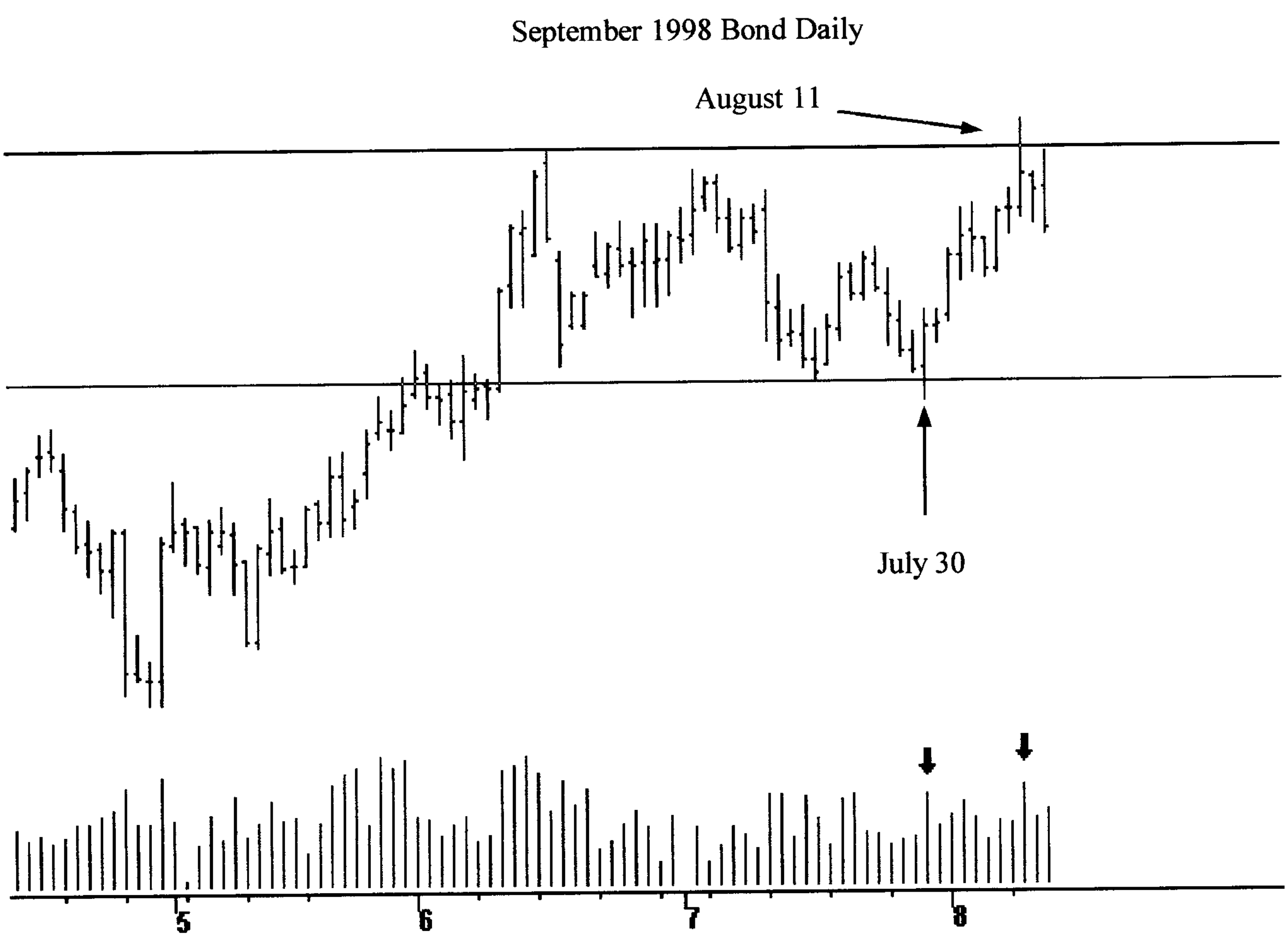
Spring and Upthrust

Exhaustion Spring and Upthrust

- The spring low was technically stronger than the upthrust high. The spring closed at the high of a wide price spread and above the high of the prior day. Contrast this behavior to the August 11 upthrust. The upthrust closed well off the low of the day, but failed to challenge the prior day's low. This particular upthrust failed to produce a significant decline (about 3/4 of a point from the August 11 close) and was subsequently violated 8 days later.

- The July 30 spring marked the beginning of the rally to the October high (@ 135.08).

- Volume posted significant increases at both the August 11 high and the July 30 low. July 30th volume @ 527,000 contracts can be contrasted to the 5 day average volume @ 325,000 contracts. August 11th volume @ 602,00 contracts can be contrasted to the 5 day average volume @ 371,000 contracts.



BREAKOUT FRUSTRATION

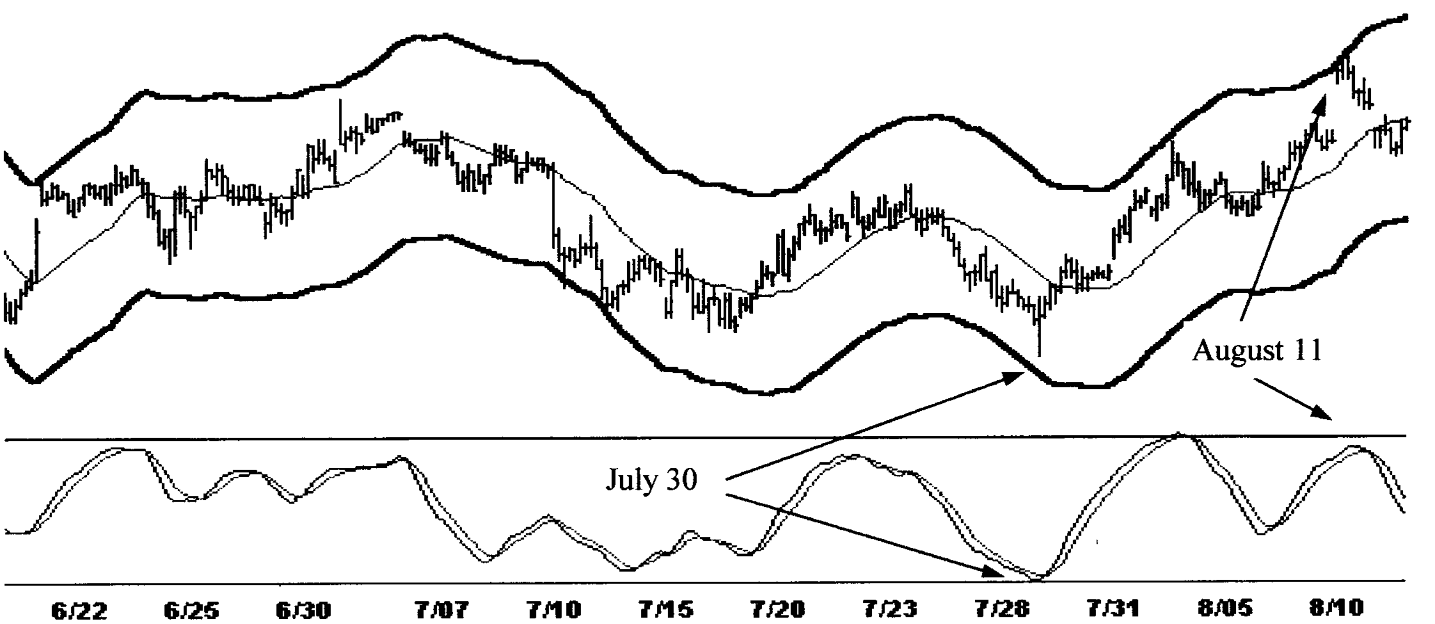
- Odds of a breakout failing or a spring/upthrust forming are very good if, immediately prior to breaking out, the market has accrued an hourly overbought or oversold condition.

- At the June 30 low, the hourly oscillator had pushed into oversold (June 29 close @ 20/22) and the bottom of the hourly moving average envelope came in just below the old low. The early morning push lower intensified the oversold and left the market very near the bottom of the moving average envelope.

- The market moved beneath the trading range support @ 121.29 (low @ 121.24) and then rallied strongly. Odds of a significant low forming were high.

- At the August 11 high, the hourly oscillator pushed into overbought (August 10 close @ 70/67) and the top of both hourly and daily moving average envelopes came in just above the old high. The overnight gap intensified the overbought and left the market at the top of both moving average envelopes.

- This pattern forms the basis for several trade entry and stop techniques.



SUPPLY & DEMAND LINES

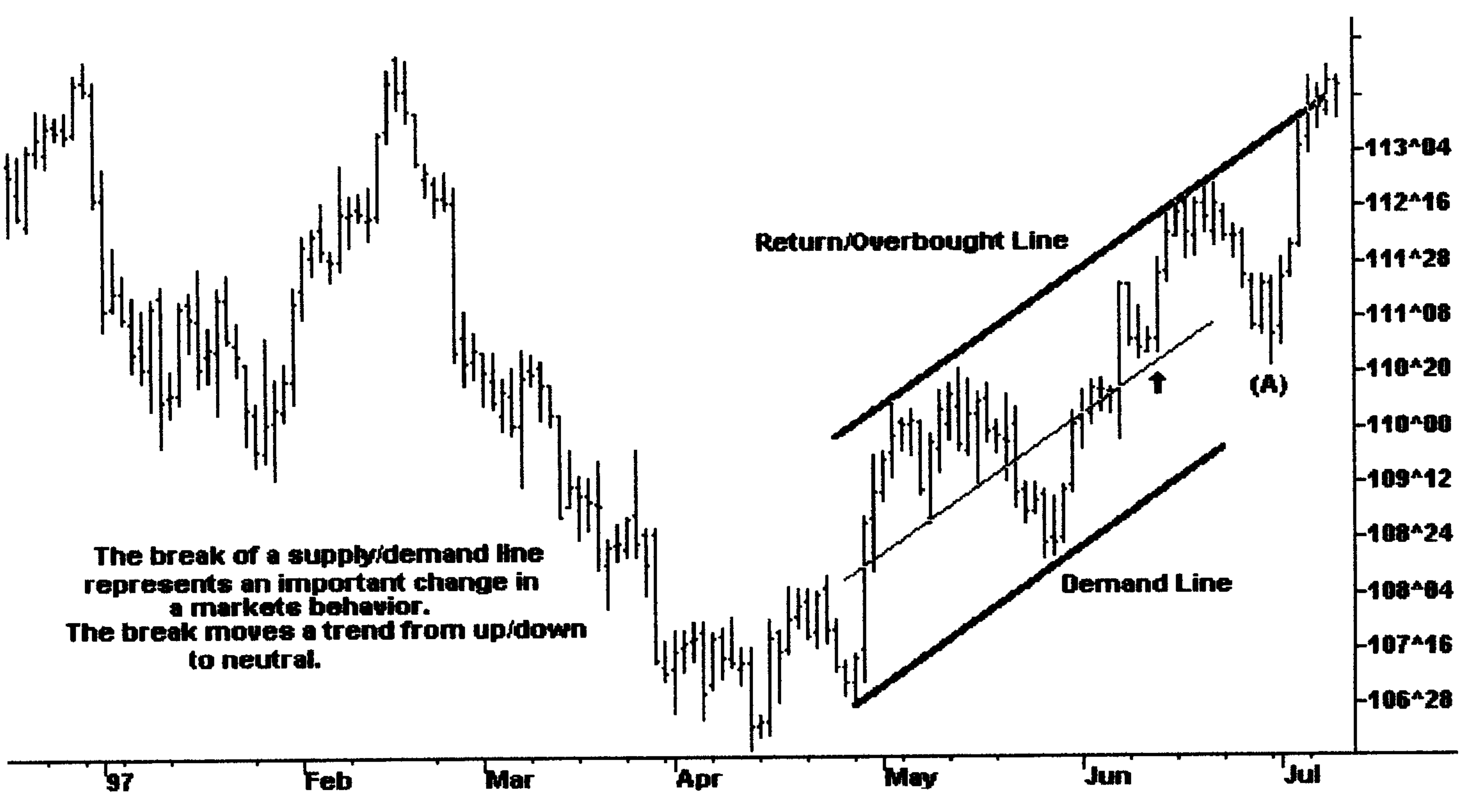
- Trend lines represent the composite man's willingness to follow the market. Moves beyond the stride of the advance/decline line represent important changes in the market's behavior.

- Pushes to a channel top put the market in an overbought condition. Channel tops usually represent good areas to take profit on longs (but not sell short against) and Channel bottoms represent good areas to take profit on shorts (but not buy long) against.

- The relationship of the market to the fringes of the channel is an important clue to the market's underlying strength or weakness. Failure to push to the overbought line is considered a sign that the trend is weakening. A failure (point A on the chart) to decline to the demand line is considered a sign of relative strength.

- The break of a shallow uptrend line doesn't usually represent a good trading opportunity. It does, however, speak volumes in terms of the change in a markets behavior.

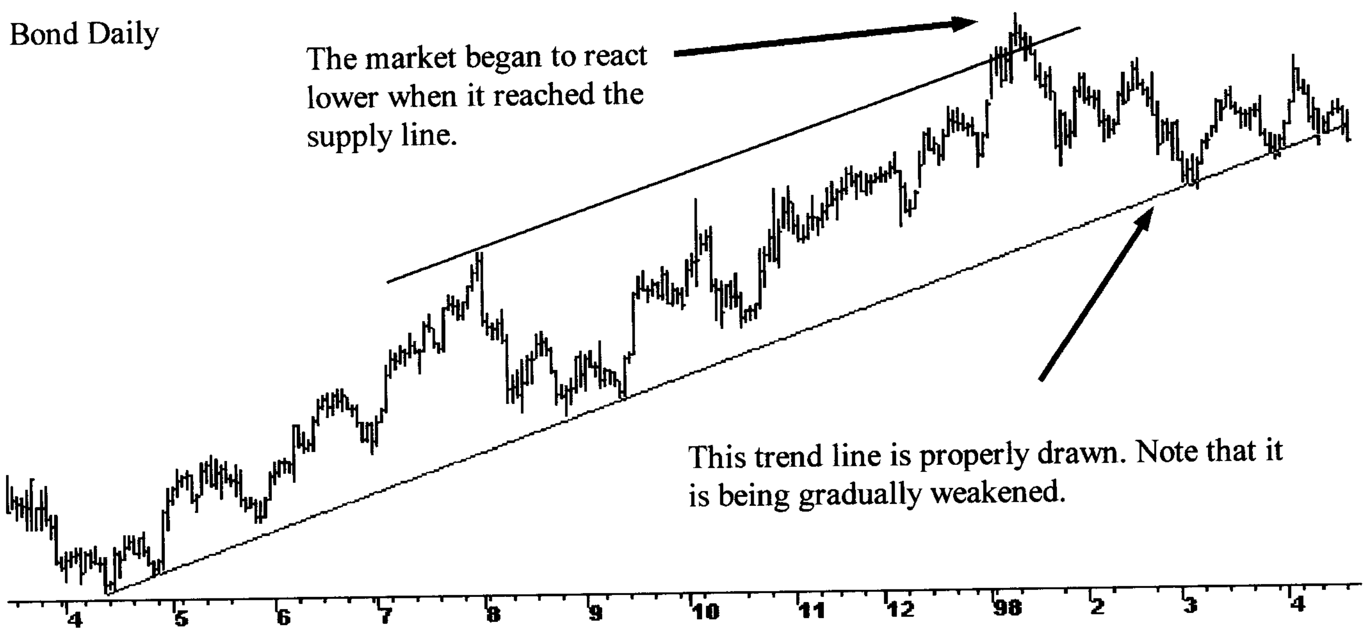
- The Break of a steeply sloping trendline can make an excellent entry trigger.



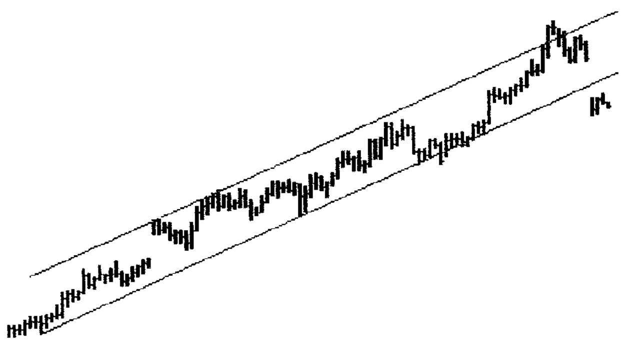
HOW TO DRAW A TRENDLINE

- Be consistent. Draw uptrends between intervening lows of the same magnitude. Draw downtrends between intervening highs of the same magnitude.
- Don't scatter meaningless trendlines all over your chart. Trend lines should never be forced. A trendline is not tradable if it does not follow the natural path of the market.
- "Trendlines should be pretty."
- To form the channel, draw a parallel off the intervening high/low of the same magnitude.

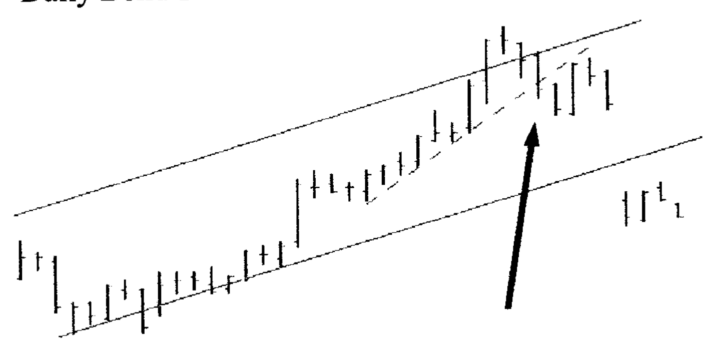
Bond Daily



15 Minute Bonds



Daily Bond Detail



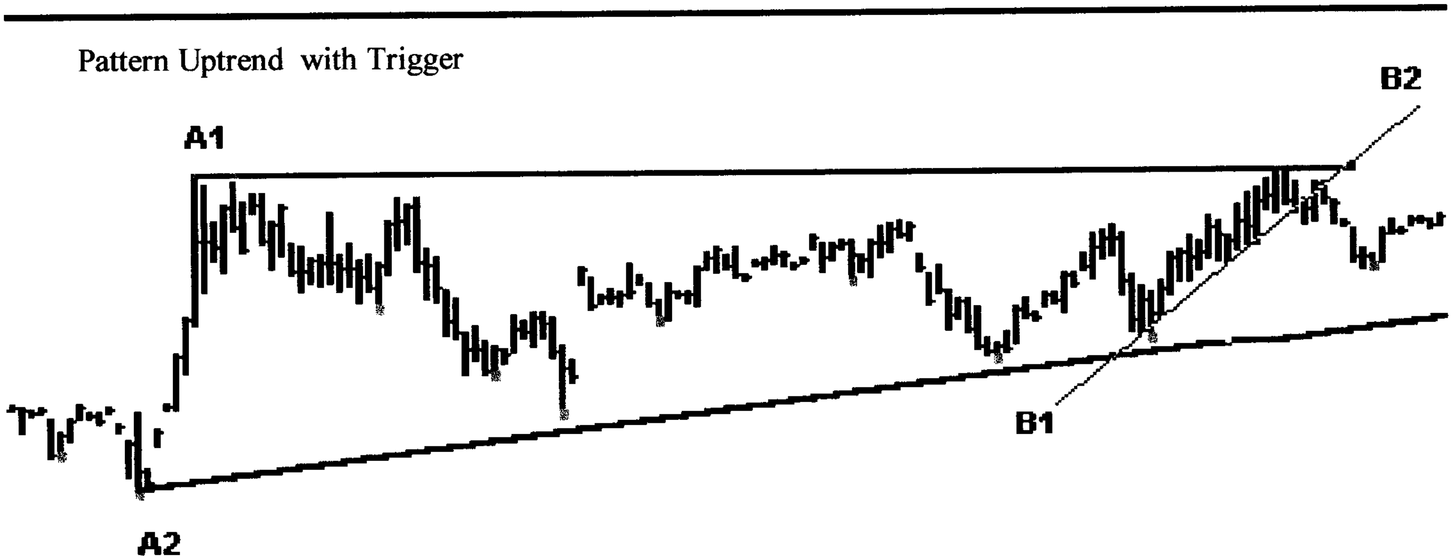
The rally to the October 5, 1998 high channelized nicely. Note that the break of the steep uptrend across the bar lows did a nice job of triggering profit taking.

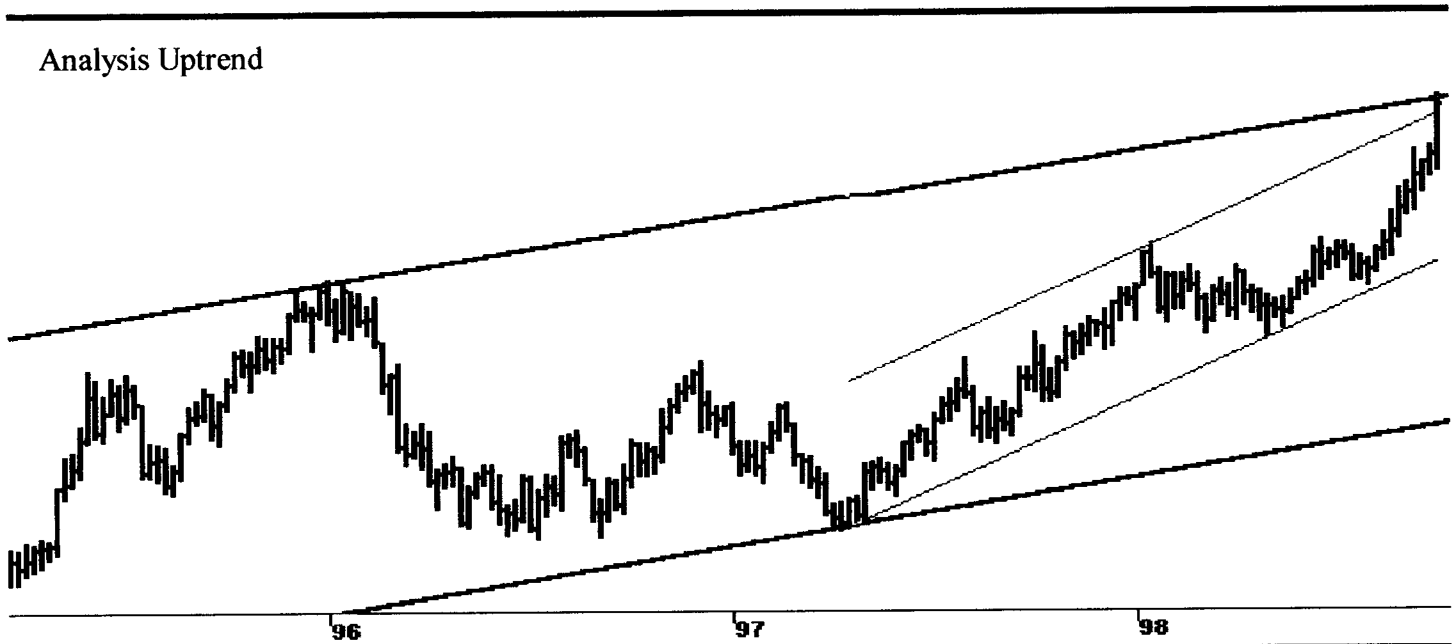
THREE TYPES OF TRENDLINES

- Type (1) These trendlines are shallow and take a significant number of bars to resolve themselves. They are more useful for defining the trend than for trading.

- Type (2) These trendlines define the bottom portion of a tradable pattern or formation. A pattern TL is more apt to provide tradable support or resistance, particularly if the market is overbought or oversold during a testing phase. The horizontal lines along the top of lateral congestion fall into this classification.

- Type (3) These trendlines are typically very steep and run along intraday or daily price lows or highs. These trendlines are very useful as entry triggers.





MISCELLANEOUS DEFINITIONS

Accumulation: The accumulation of a position by strong handed well informed investors from weak handed poorly informed investors in anticipation of bullish news that is not yet publicly known or anticipated.

Distribution: The distribution of a position by strong handed well informed investors to weak handed poorly informed investors in anticipation of bearish news that is not yet publicly known or anticipated.

Markup (execution): After a period of accumulation the market will begin to trend higher. This trend toward an eventual buying climax is called markup.

Markdown (execution): After a period of accumulation the market will begin to trend lower. This trend toward an eventual selling climax is called markdown.

Some Thoughts

Few markets set up a perfect Wyckoff sequence.

There are many facets of Wyckoff (including point and figure, wave and swing charts) that are not covered here.

Additional Reading

Charting the Stock Market, The Wyckoff Method. Hutson, Weis, Schroeder. (Available from Technical Analysis of Stocks and Commodities).

Volume and Open Interest, Ken Shaleen, Probus Publishing.

Volume Cycles in the Stock Market, Richard Arms III, Dow Jones Irwin.

Stock Market Institute in Phoenix Arizona, offers a comprehensive correspondence course.

SIMPLE IS....
SIMPLY BETTER

OBSERVATIONS

- Simple and obvious is *always* better than complex and convoluted.

- Genetic algorithms, chaos, neural networks, and astrology have become extremely popular over the last decade. Unfortunately, few of us have the background, time, or patience to understand and use them effectively.

- The more complex the methodology, the more psychological impediments develop to hinder trading. Misinterpreting the data or being confused to the point of inaction becomes more likely.

- There is a tremendous difference in trading and analyzing. The emotions involved in trading can render even the most well thought out analysis impossible to follow.

- The more complex a system or method, the more time is required to do the analysis and implement the strategy.

  To be successful you need:

  1) A simple risk management plan.
  2) A simple system of entry.
  3) A simple system to exit.
  4) A simple system of moving stops for protection.
  5) The discipline to carry out your plan.

- A trading plan can be as simple as buying against good support when an oversold condition has developed, and selling against good resistance when an overbought condition has developed.

- *Almost any technical system will work as long as it applied in a disciplined and consistent manner.*

FINDING LOW RISK TRADES

- Focusing on one market will give you the opportunity to learn its rhythms and idiosyncrasies.

- Use daily range projections in combination with basic patterns, a momentum oscillator, overbought/oversold conditions, Wyckoff patterns, and Fibonacci zones to set up low risk swing and day trades.

- When several methods conspire to produce a confluence of support or resistance, particularly in combination with an overbought or oversold condition, place a trade against it.

- If the background analysis is a generally bullish one, daily buy zones should be closer to yesterday's close. Daily sell zones should be farther from yesterdays close.

MONEY MANAGEMENT

- Develop a good money management plan and then stick with it. A good plan increases contract size as account equity grows and decreases contract size during periods of drawdown.

- Don't over-leverage.

EQUITY

- The nature of short term trading is such that the majority of your trades will end up being either a small win or a small loss. A few trades will be stopped out at the maximum allowable loss, while the bulk of your gains will be made on made on a very few *lucky* trades.

RISK

- When deciding to trade, risk is the first, last and ultimate consideration.

- If a protected stop loss isn't available within a standard or predefined dollar risk of the entry level, the trade is a pass.

- In terms of bonds, hide stops 3-4/32 above/below important chart support/resistance.

For Instance:

For bond day trades, I typically use 10/32 stops. Assume a solid buy zone exists @ 112.26, but that first decent support doesn't show up until 112.12 (-14/32). The stop would have to be placed in the 112.08-10 area (-18/32). There are only three choices. 1) Reduce the size of the trade to compensate for the risk to the stop. 2) Lower the buy zone (and reduce the chances of getting filled). 3) Don't do the trade.

- This risk adverse approach means that trades won't happen every day.

- Be picky. If you can't get a fill on your terms at your levels... pass. Never chase an entry fill.

- Every intraday wiggle and swing isn't necessarily a trading opportunity and doesn't necessarily mean anything. Sometimes a wiggle is just a wiggle.

- Don't ever widen your stop, but do have a plan to move the stop to reduce risk and lock in gains.

TRADING

"*Greet triumph and disaster and treat these two imposters just the same.*"

- Never leave yourself at the market's mercy. Avoid trading around events that have the potential to cause extreme volatility (I.E. The unemployment report in the bond market).

- Be patient. Wait for the juicy setups.

- When the market moves sharply in favor of a trade, it's time to take the profit. Always assume that "It ain't gonna get much better."

- Being stopped out at a loss, after a trade has become reasonably profitable, always represents a failure in judgement. If a trade isn't performing, dump it.

- Focus, focus, and focus. Cut out the distractions, turn off CNBC, don't take calls from lawyers, salespeople, gurus or anybody while you are managing your trade.

- Having a market opinion is mostly counterproductive for day and swing traders.

- Analyzing and trading are very different things. How else do you explain the great trader who never has a decent market opinion and the great analyst who never seems to make a solid trade.

- Every tick isn't a trading opportunity. If you find yourself living and dying by the tick, it's time to re-examine your approach.

- Don't fall for the psycho-babble. Find some trades you like and ....."*Just do them*"

- Be a grown up about it. It's not a personal thing and the market isn't malevolent. Learn to consider every trade as: "*Just another damn trade*"

PATTERNS

- Look for any technique or pattern that will typically produce technical buying and selling.

Lateral support and resistance.
Supply and demand Lines.
Pattern uptrends and downtrends.
Triangles.
Buying/Selling climaxs.
Low volume re-tests.
Back up to a creek.
Rally back to the ice.
Ringed highs and lows.
Gaps.

SUPPORT AND RESISTANCE CONFLUENCE

- If several different techniques project or produce support or resistance in a single area of the chart, there is a confluence.
- A resistance confluence should be sold.
- A support confluence should be bought.
- The more techniques that project support or resistance in a given zone, the stronger the support or resistance will be.

Overbought and oversold conditions at a support/resistance confluence increase the odds of the confluence holding.

TRIGGERING IN
The systemization of
discretionary trading
behaviors.

- Combines the best aspects of systematic and discretionary trading.
- Triggering in modestly reduces the profitability of many trades but drastically reduces the number of premature entries.
- Buying into a market decline or selling into a rally is counter intuitive and contrary to most conventional trading wisdom. Triggering in makes difficult decisions much easier.
- Trading triggers bring discipline to entry and stops.
- Potential triggers include thrusts, key reversals, Dojis, ledge breaks, up-thrusts, springs, and reversal bar patterns.
- Different triggers work better in different situations.
- Typically, the more conservative the trigger, the more risk there is to the stop.
- If the daily chart sets up a buy, you can often find an hourly setup and trigger.

PULLING IT ALL TOGETHER

THAT WAS FUN, BUT HOW THE HECK DO I USE THIS JUNK TO MAKE SOME MONEY?

Getting Ready to Trade
What I want to know going into the trading day

- Is the market trending strongly in the next higher perspective? If the trend is huge, I may want to avoid counter trend swing trades. If the daily trend is up and the daily oscillator has not accrued an overbought condition, I am going to look more closely at bullish setups and triggers.

- If the market is trending, are there congestion formations that I can trigger out of? If the market is range trading, how far away are the fringes of the range?

- Are there any support/resistance zones to hide a secure stop behind? Are there any nearby support/resistance confluences to set triggers against?

- Is the hourly oscillator overbought or oversold? If the market reaches a tradable support or resistance, will it arrive in an overbought or oversold condition? Are divergences beginning to build?

- Are there any triggers setting up?

- Are any Wyckoff or Elliott setups or relationships evident?

- Is the market poised for an upthrust or a spring?

- Is the market making regular highs and lows (in terms of time)?

- Was yesterday a buy day or a sell day (explore George W. Taylor's swing trading ideas)? Do I suspect either a swing high or low today?

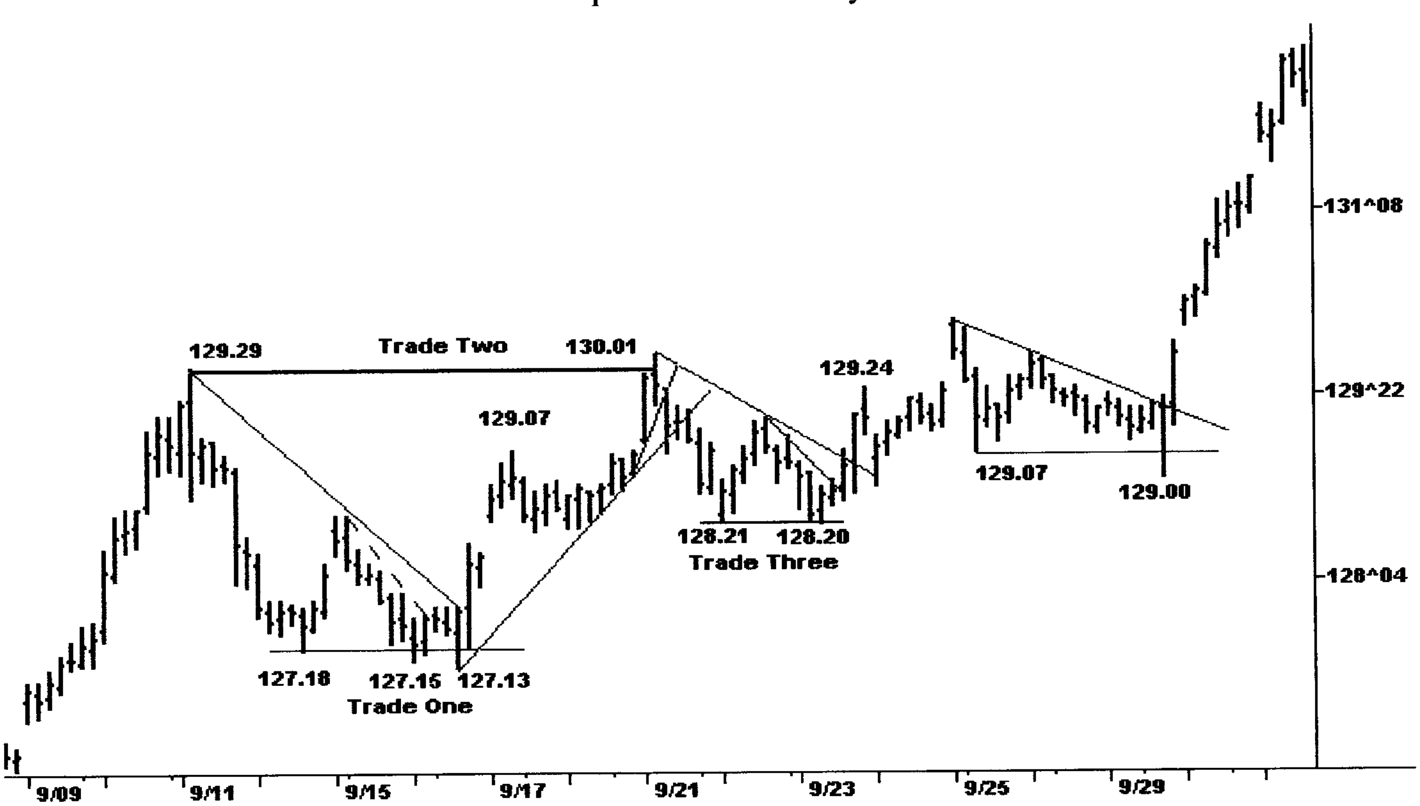
WYCKOFF TESTS AND TRENDLINE BREAKS

- This entry takes advantage of two very reliable patterns (test/retest and T-L break). It can be used on any chart perspective from one minute to monthly and across a wide variety of markets. The trade works extremely well on hourly charts, but I often find myself triggering in on daily and weekly trades.

- For a sell, the setup is formed when the market makes a well defined high, reacts lower and later tests the high. As the market rallies back toward the prior high a trendline is drawn beneath the rally. The entry is triggered when the market falls through the trendline *after* testing the prior high. A test should come close (within a few ticks) or slightly exceed (upthrust) the prior high.

- The aggressive trader can sell the break of a trendline, running along the individual bar lows of the rally, from the reaction low. The more conservative trader can wait to sell the break of a shallower trend line drawn across the reaction lows of the rally from the reaction low.

September Bond Hourly



STOPS

- Potential stops. (1) 2-4/32 above/below the pivot being tested. (2) 1-2/32 above the high/below the low of the bar preceding the break. (3) 1-2 ticks above/below the high/low of the bar containing the break.

TRADE ONE

- Aggressive entry @ 127.24, Conservative entry @ 127.30. The aggressive entry stopped out @ 127.13 (-11/32). The conservative entry had a maximum drawdown of 11/32. Subsequent high @ 129.07. Potential gain in the conservative trade of 41/32.

TRADE TWO

- Aggressive entry @ 129.20, Conservative entry @ 129.09. The aggressive entry had no drawdown. The conservative entry had a maximum drawdown of 10/32. Subsequent low @ 128.21. Potential gain in aggressive entry of 31/32. Potential gain in conservative entry @ 20/32.

TRADE THREE

- Aggressive entry @ 128.31, Conservative entry @ 129.06. Neither entry had a drawdown. Subsequent high @ 129.24. Potential gain in aggressive entry of 25/32. Potential gain in conservative entry @ 18/32.

NOTES

1) The trade is particularly effective if the oscillator is overbought/oversold and divergent when the market arrives in test position. 2) The trade is stronger when the market upthrusts/springs the prior pivot. 3) Often the market will break the trendline and react back to the underside of the trendline. 4) Watch for Wyckoff price/volume relationships (poor result of effort). 5) Profit objectives should be reasonable. 6) If the trade doesn't work quickly, close it and go to the next thing. 7) If you are stopped out on the more aggressive entry, the conservative entry often offers an excellent entry.

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EXAMPLE # 1

- The market rallied to 127.16 (a potential third drive) and momentum began to fade. A sell stop is placed one tick below the trend line (@127.31).

- There are three choices for the initial stop: (1) Above 127.16. (2) Above 127.11. (3) Above 127.03. The 127.16 high is too far away for a short-term trade (17/32). The 127.11 prior bar high still represented a significant risk (12/32) but the 127.03 high did not leave enough room. The best choice is to use the 127.13 stop and move it down aggressively.

- The market immediately followed through, allowing the stop to be aggressively lowered. Profit could be taken on the initial spike low (@126.19) for a net gain of 1/4 - 1/2 point or the position could be left open, hoping for larger break (the ultimate low @ 126.10).

EXAMPLE # 2

- The market had established a solid downtrend to work against. The initial entry stop is elected @ 126.16.

- Stop choices are 126.10, 126.11 and 126.14. In this case the most secure stop (@126.10) is very close to the original entry level. The market immediately moved in favor of the trade. Profit may be taken @ 126.22 (initial high) or can be held for a swing if the daily close is near the high of the day.

NOTES:

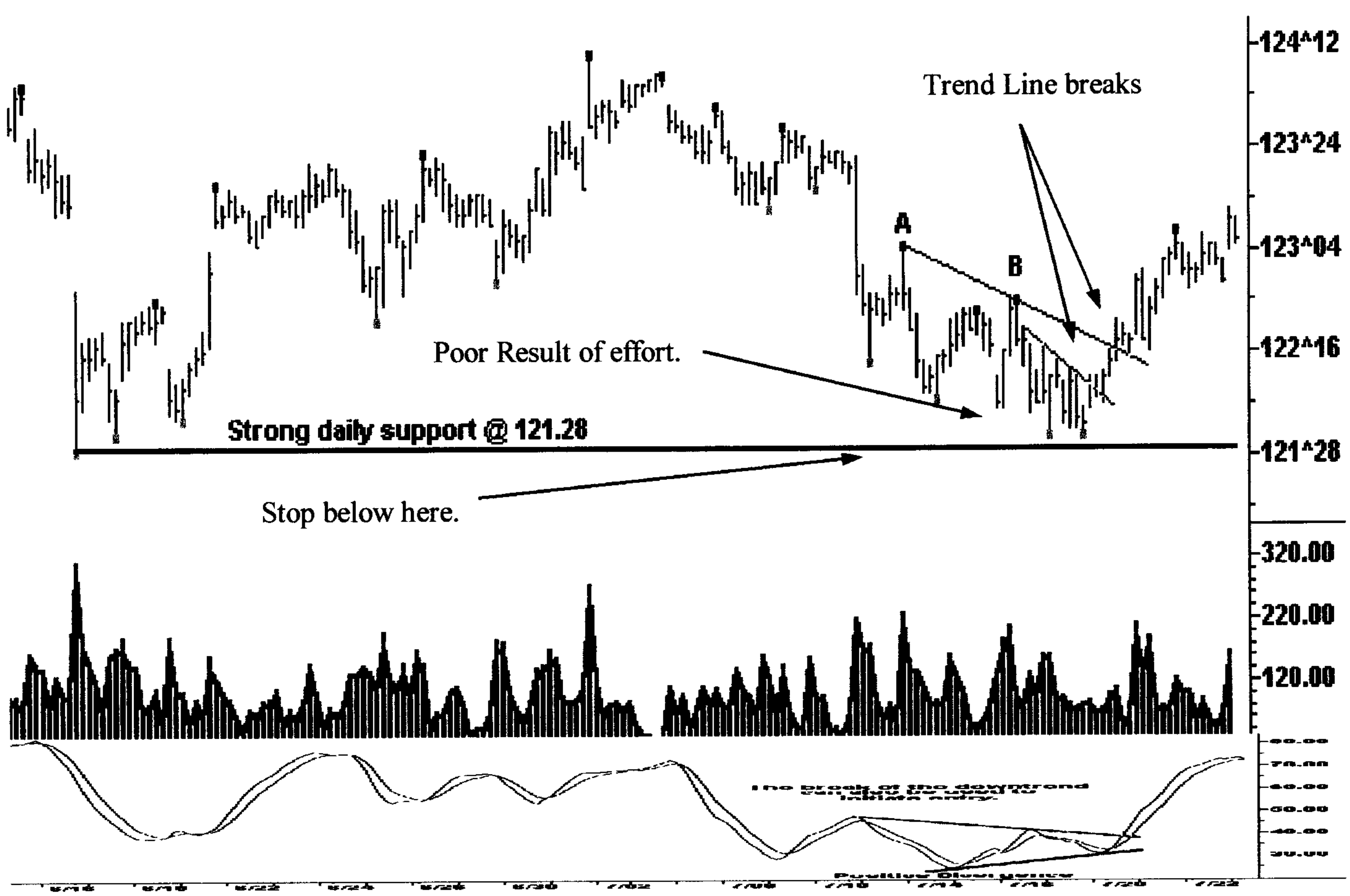
- There is a minor set up on the right side of the chart. There are clearly three drives to a low, but the momentum is increasing, no divergence is evident and there is no flagpole.

- More aggressive entry triggers work well with this setup (I.E. reversal bars and ledge breaks).

POOR RESULT OF EFFORT
WITH TREND LINE BREAK

- This trade offers a solid confluence of good setups and a solid stop. Several of the more important Wyckoff principles are evident.
- The market pulled back to the vicinity of strong hourly/daily support.
- The poor result of effort along the low as the market approached the prior pivot is obvious.
- The oscillator is oversold and posting a divergence.
- Three drives to a low are evident.
- There are solid pattern downtrends to use as triggers.

September 1998 Hourly Bars



1998 Long Yen Trade
Background

- Entering a position trade, I want to have technical *and* fundamental justification. I use intermarket technical analysis to build the fundamental framework.

Related Market Setup

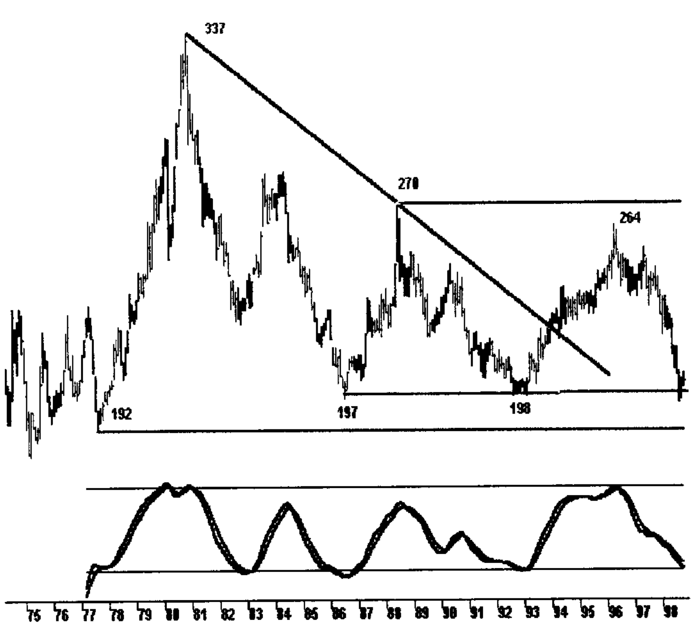
- In early 1998, several related markets were poised for important turns. The first harbinger of major change would likely be a turn in Dollar Index.

- The Dollar Index was resting at the top of a long- term trading range and had accrued a very strong overbought condition. Hedge funds and speculators continued to leverage huge positions in the Yen carry trade (Borrow Yen/Buy Dollars/Buy bonds) and financial commentators were generally characterizing the Dollar as extremely strong. Despite the good press, a "poor net result for effort expended" was appearing at the top of the trading range.

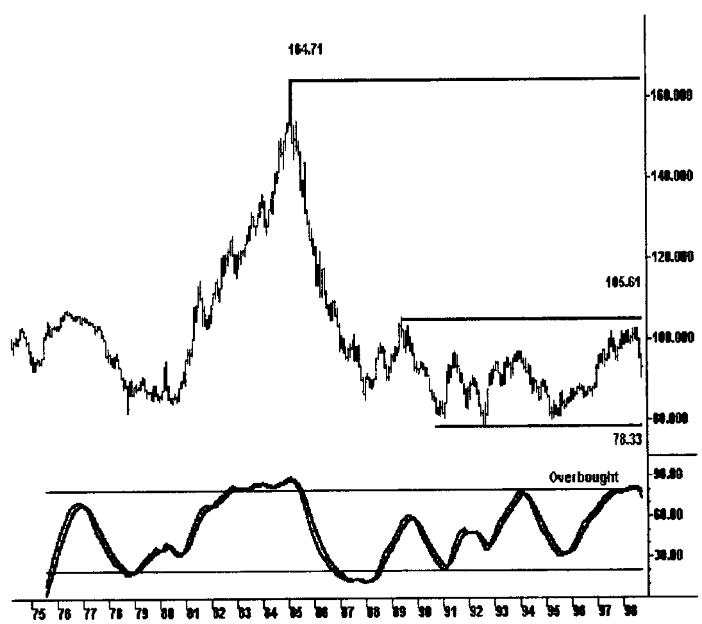
- Commodities were testing long-term support and had accrued a tremendously strong monthly perspective oversold condition.

- Odds of a Dollar top and a commodities bottom forming were very strong.

CRB Index Monthly Continuation

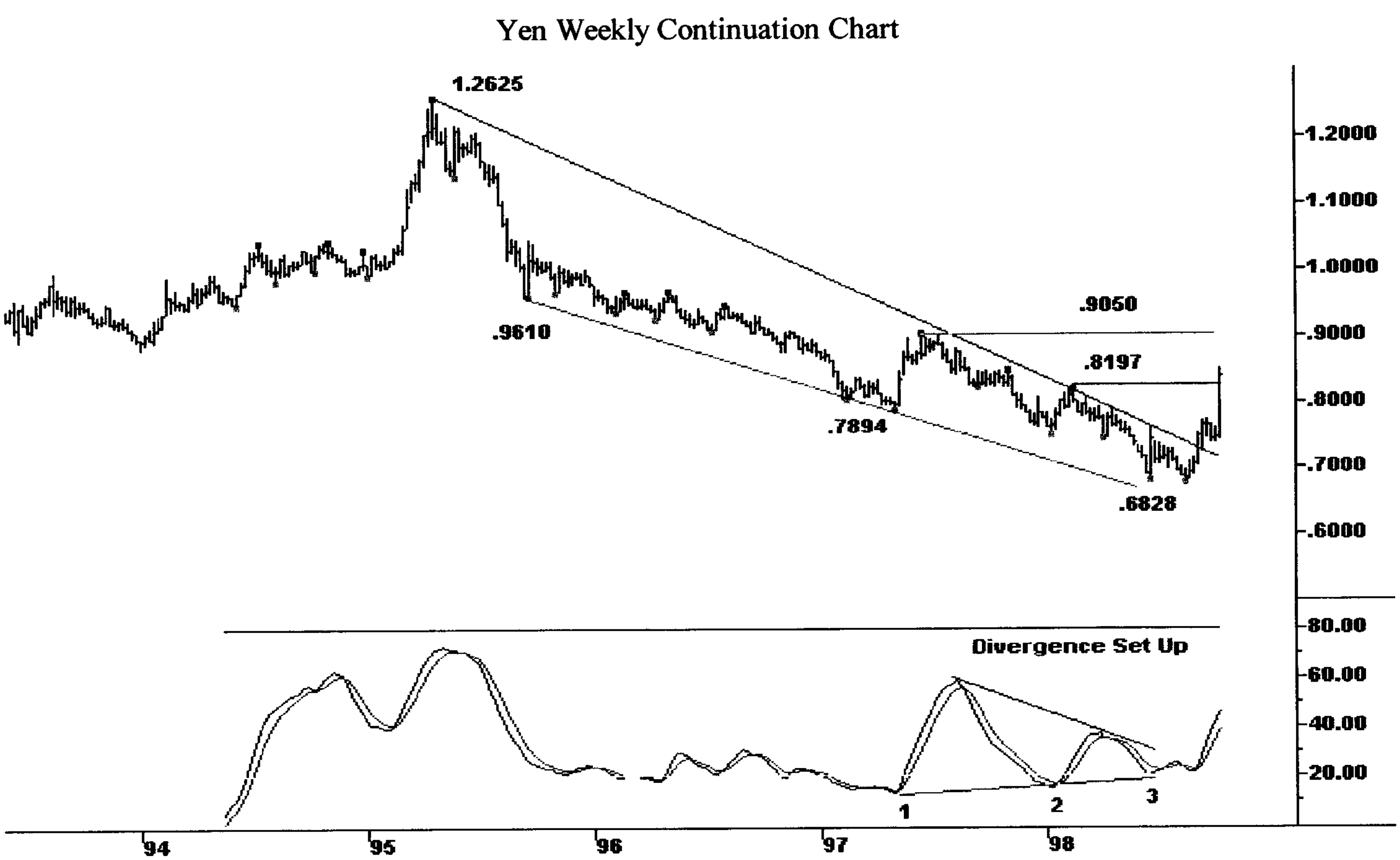


Dollar Index Monthly Continuation



WEEKLY TECHNICAL SETUP

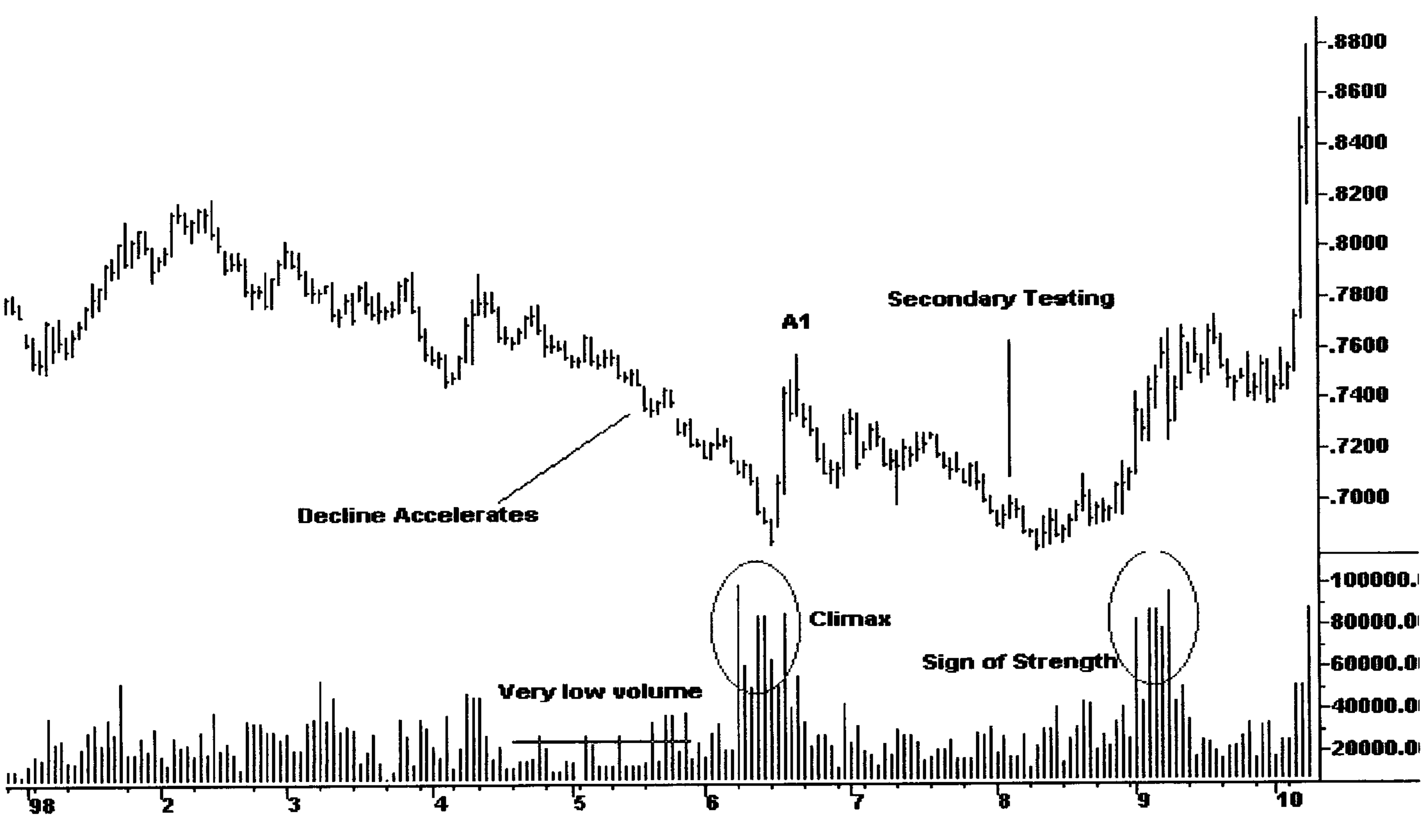
- The three-year decline from 1.2625 developed in a wedge pattern.
- The T-L from 1.2625 qualified as an analysis trend line and as a pattern trendline. In the later stages of the pattern, it also became a potential trigger mechanism.
- The final bottom produced a second oscillator divergence. The building divergence suggested a tradable low.
- Successive thrusts were smaller (1.262 - .96 - .78 - .68).
- The thrust higher from .6828 low represented a solid sign of demand.
- After retesting the low, price broke out of the weekly falling wedge pattern on 09/04/98. That week's close was .7486 (continuation chart). The lowest point after the thrust was .7235.



PRICE VOLUME DETAIL

- Continuation charts offer an excellent way to monitor for long-term price/volume relationships.
- In June 1996, the decline accelerated, but the volume leading to the June low was significantly lower than the volume generated in the February - May period (less supply).
- In early May, an increase in volume became evident. Volume at two to three times normal clearly marked a potential selling climax. The thrust to point A1 wiped out 35 days of downside effort in four trading days.
- From point A1, the market began the secondary-testing phase. Volume clearly declined, and the price spread narrowed, as the market moved toward the May low.
- The stage was set. Now the challenge was to find a way to participate.

Yen Daily Continuation



TRIGGERED IN

- Recognize conditions that lead to bottoms and tops, and have an appropriate tactic to enter.

- A solid daily trend formed along the highs as the market moved into the test zone.

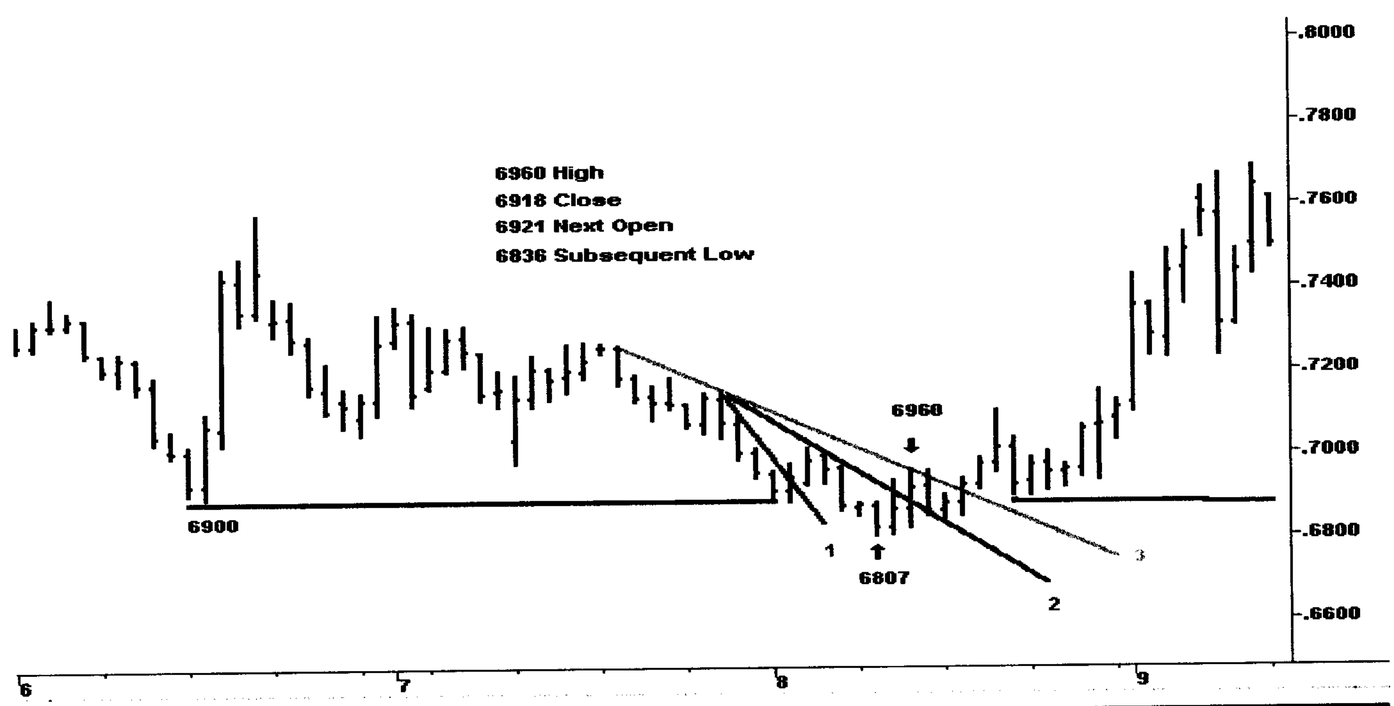
- The market washed out the support, but there was little evidence of selling interest.

THREE POTENTIAL TRIGGERS

- (1) The very steep T-L. Steep T-Ls comprised of only 3-5 bars tend to produce multiple whipsaws, but the distance to the stop is usually small.

- (2) The more moderate T-L. This T-L is going to need a reasonable thrust from the support to trigger. This was my preferred entry.

- (3) The shallow T-L. This is a conservative entry. Stop should be under the bar immediately preceding the breakout. This T-L will provide a backup entry if the other triggers are stopped out, or you missed entry on one of the more aggressive triggers.



TRIGGERING IN MORE

TRADE OF THE YEAR

(I'm so proud/lucky/whatever)

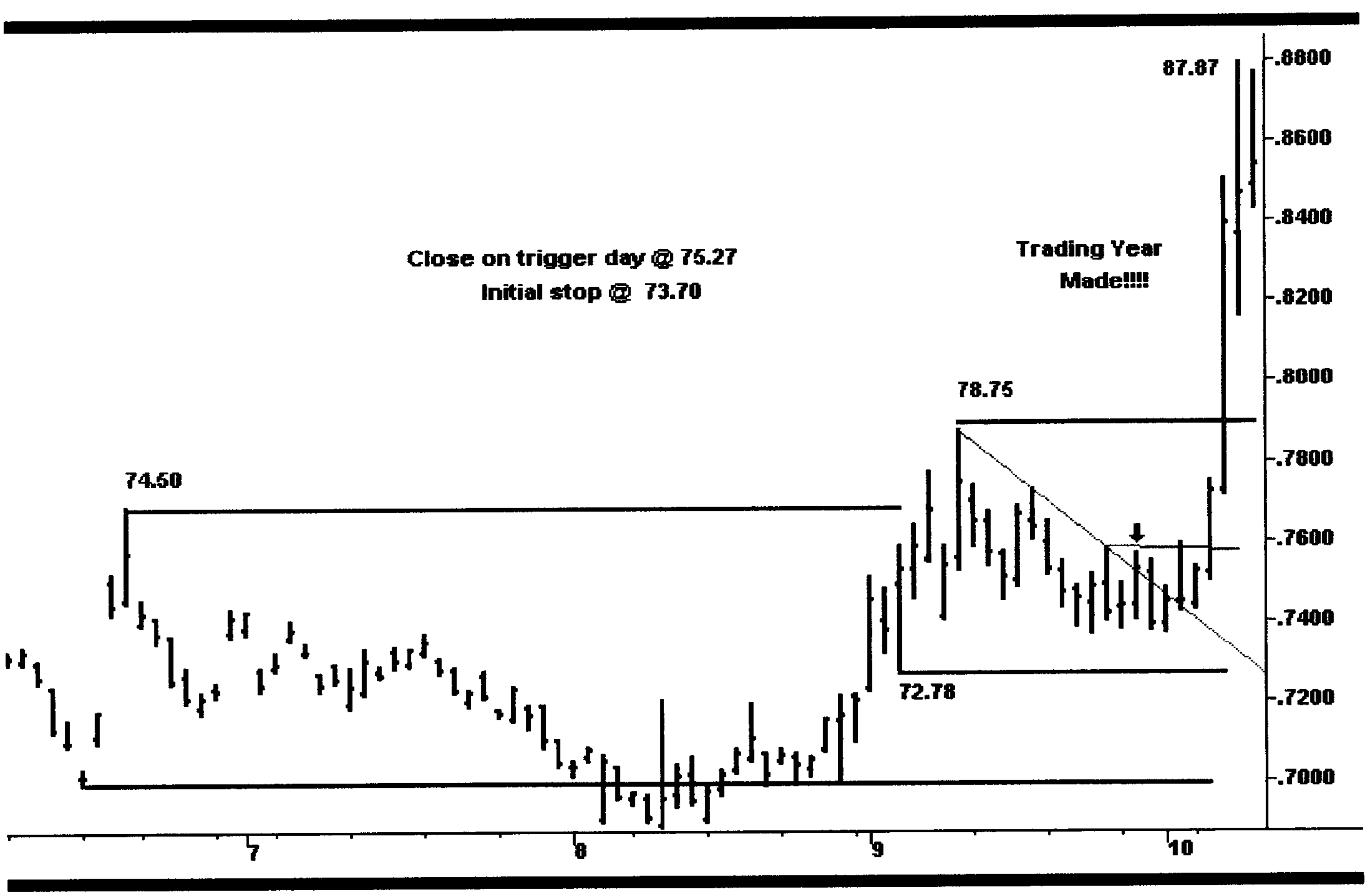
December Yen

- After posting a sign of strength into September, the market began to pull back. The sign of strength met with heavy volume, but the subsequent pull-back elicited low volume and narrowing price spread (A classic correction).

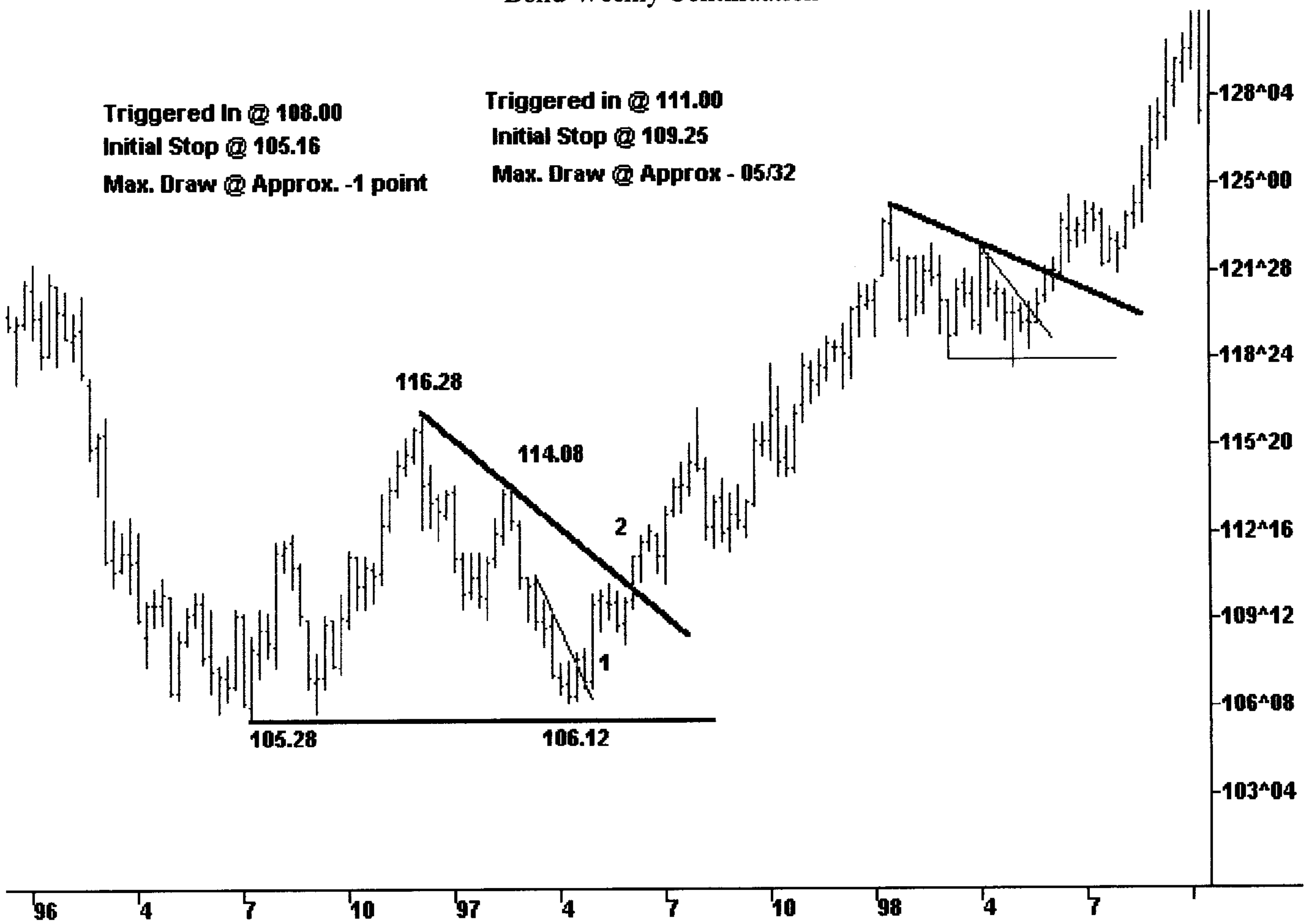
- The market was operating against a bullish background. The sign of strength from the August lows and friendly price volume patterns suggested that a pullback would offer a buying opportunity.

- By the middle portion of October, price had set back roughly 50%. Volume dropped and price spread narrowed on the pullback. The pattern was a classic flag. As the market vacillated in a narrow range, the lack of selling pressure became obvious.

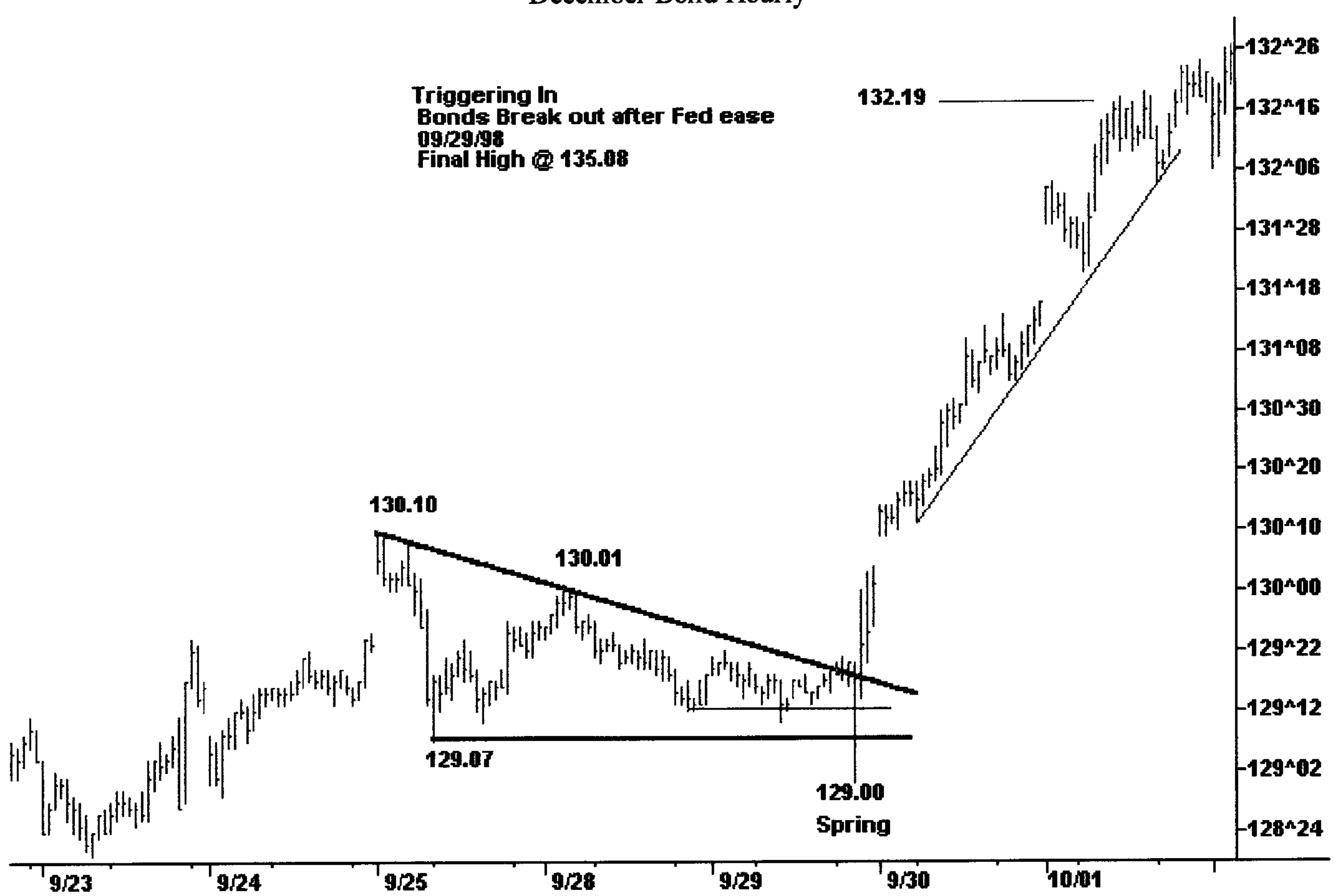
- Triggered in again on September 29th.



Bond Weekly Continuation

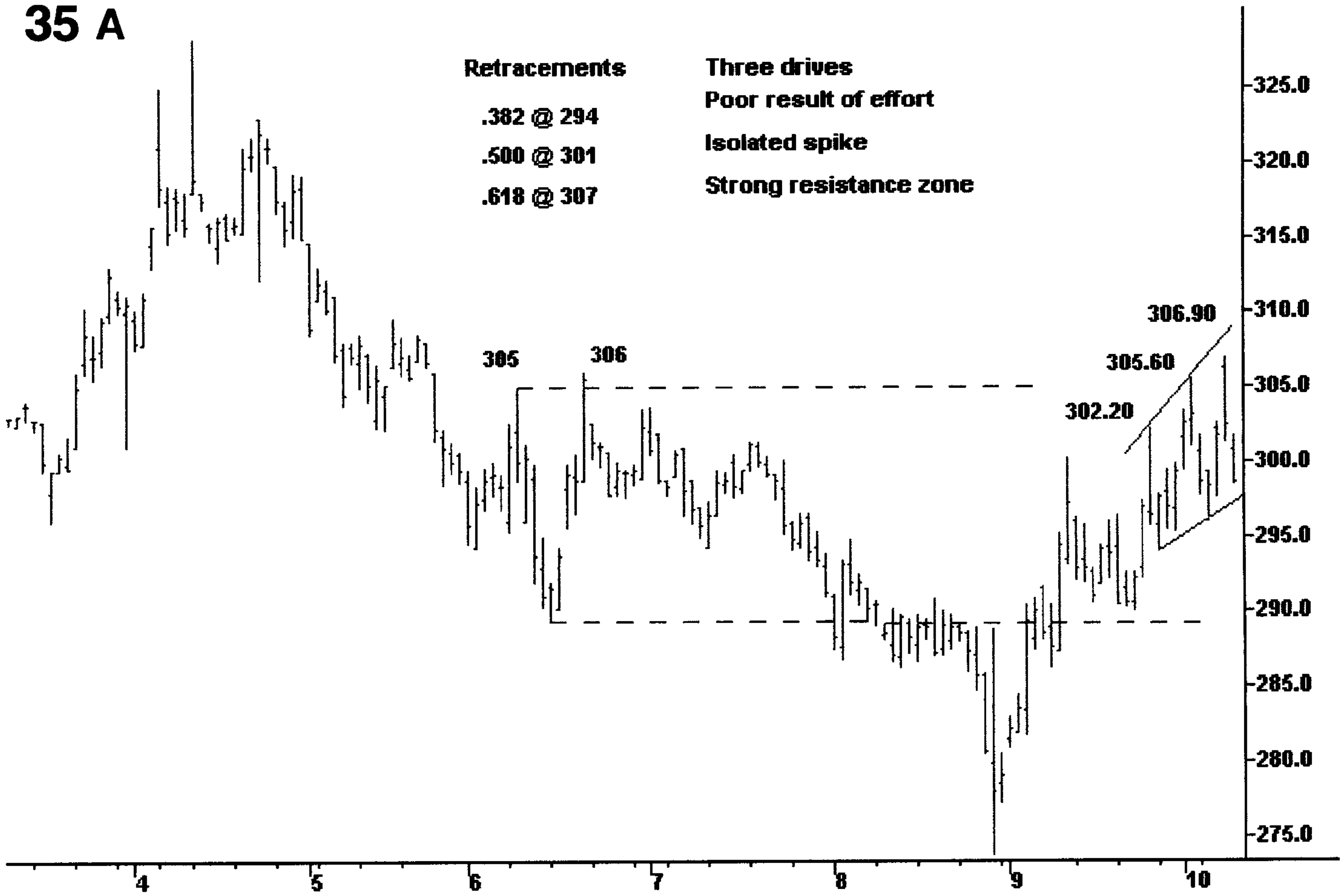


December Bond Hourly



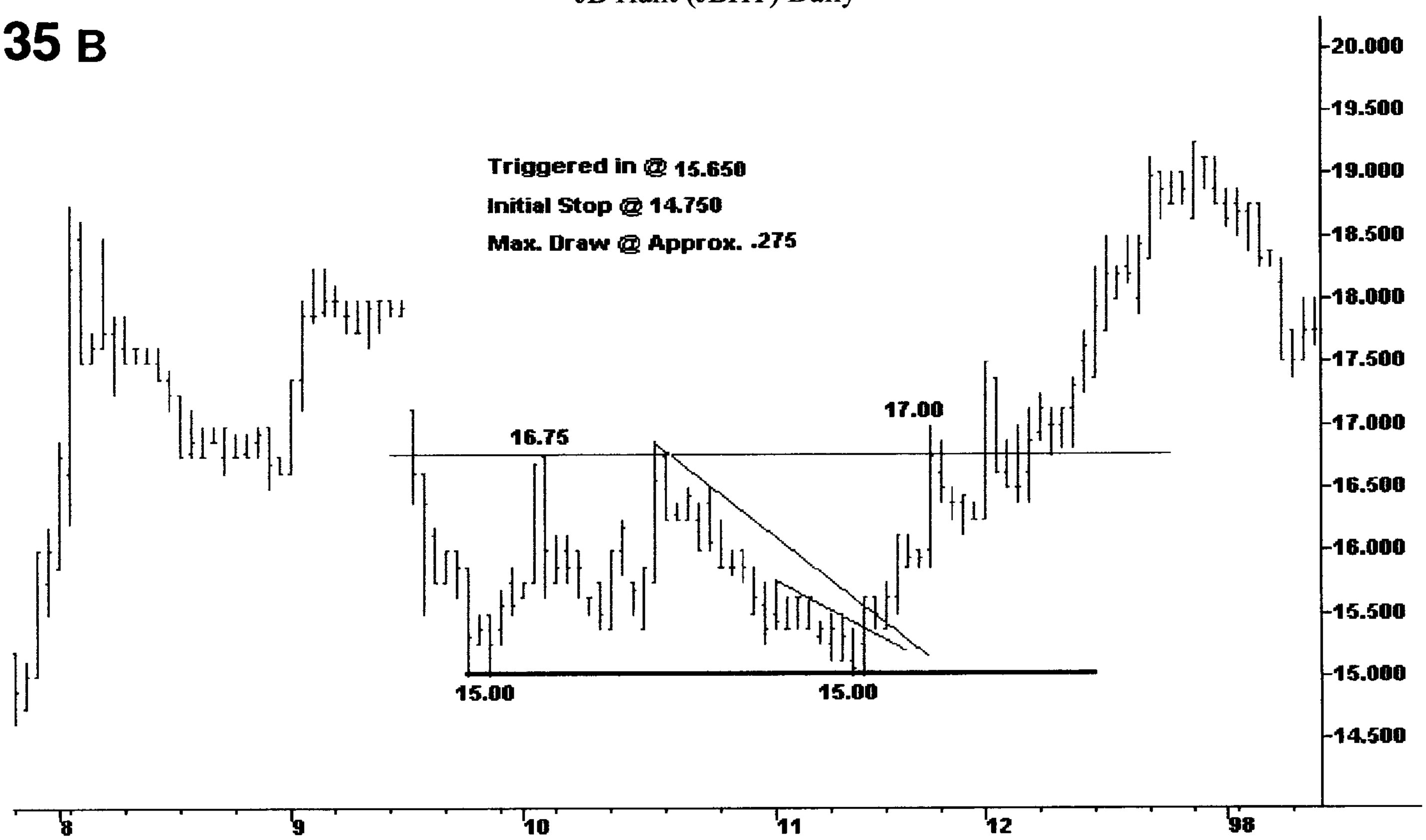
December 1998 Gold Daily

35 A

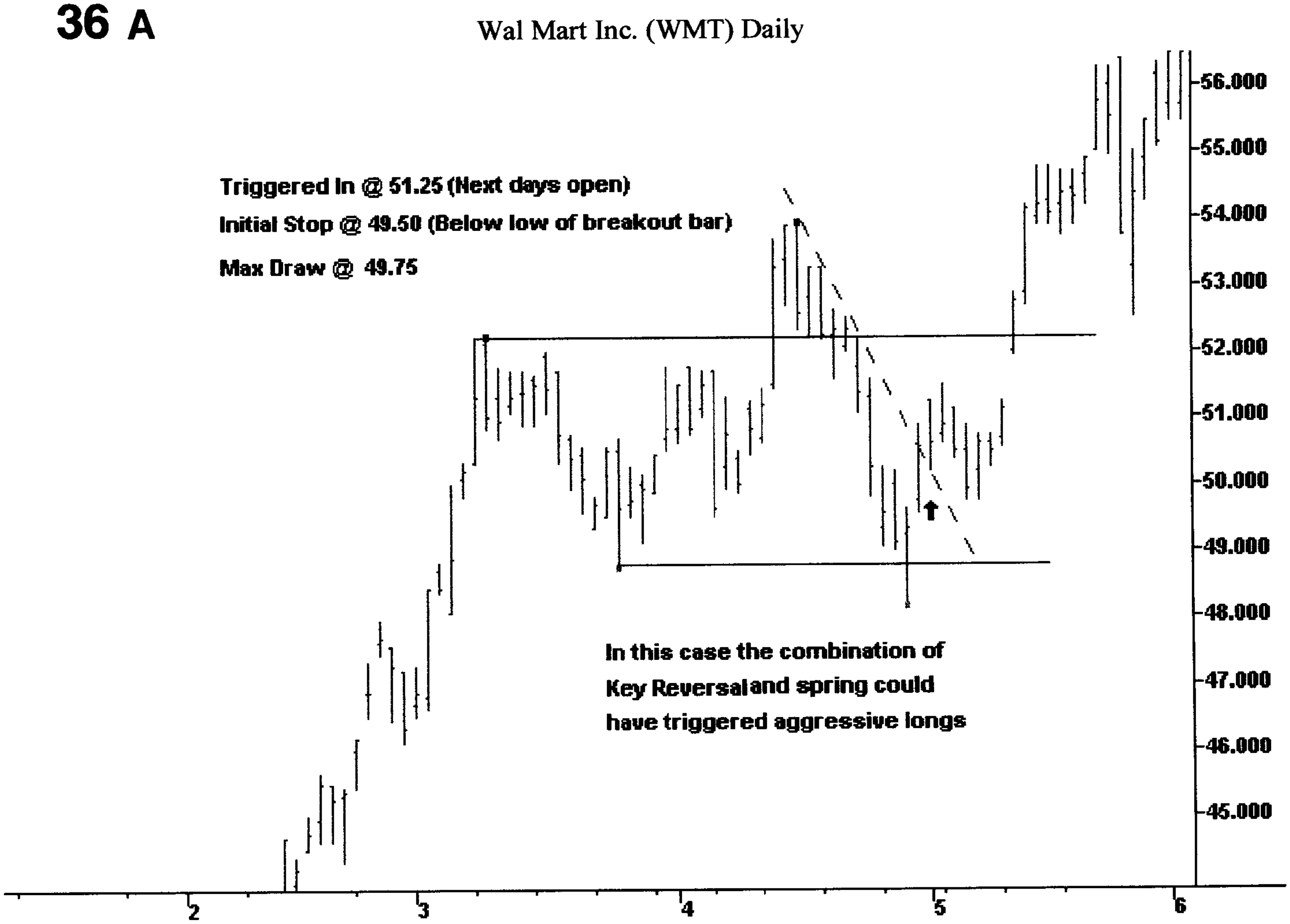


JB Hunt (JBHT) Daily

35 B



36 A


Wal Mart Inc. (WMT) Daily
Triggered In @ 51.25 (Next days open)
Initial Stop @ 49.50 (Below low of breakout bar)
Max Draw @ 49.75
In this case the combination of
Key Reversaland spring could
have triggered aggressive longs
56.000
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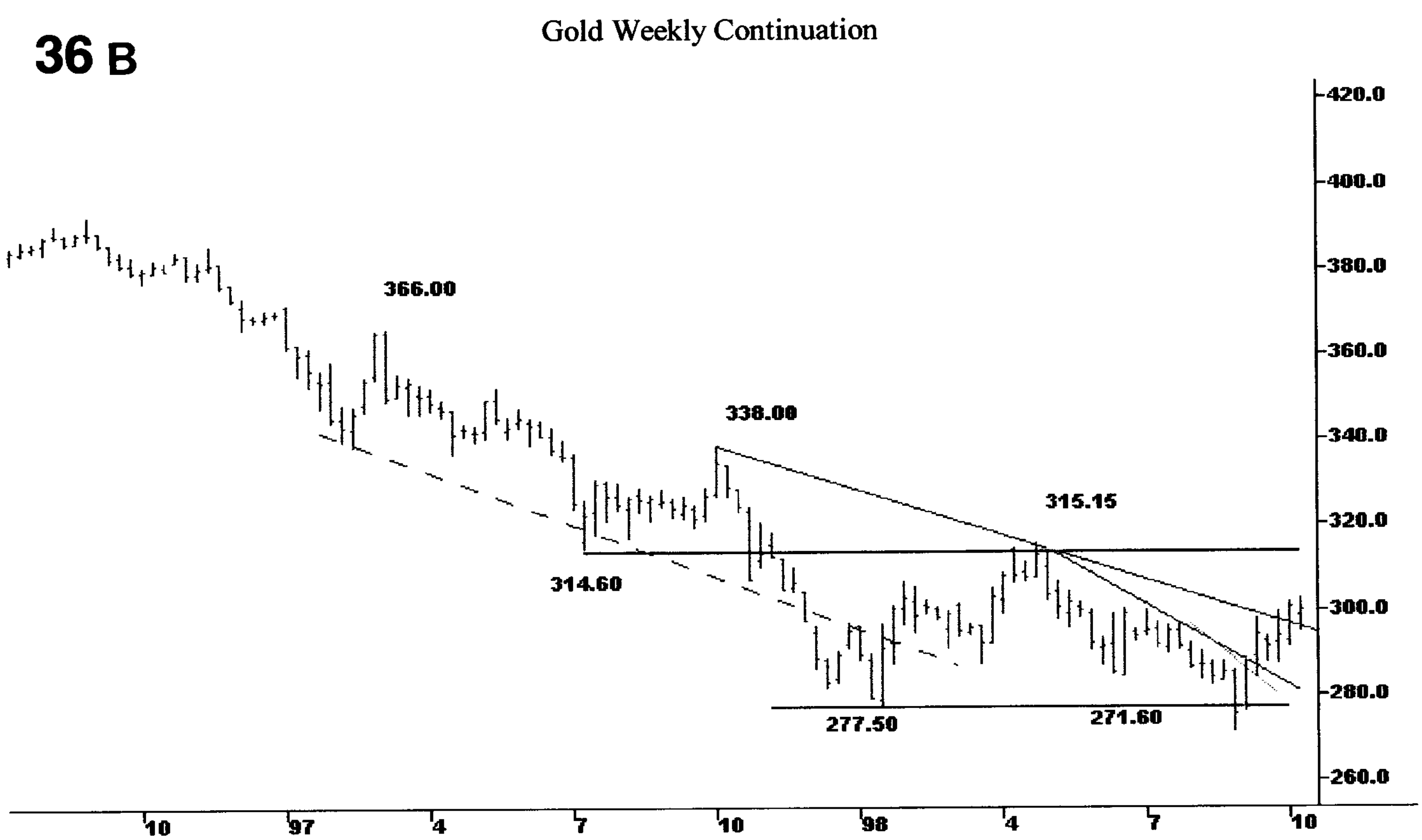
36 B


Gold Weekly Continuation
366.00
338.00
315.15
314.60
277.50
271.60
420.0
400.0
380.0
360.0
340.0
320.0
300.0
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97
4
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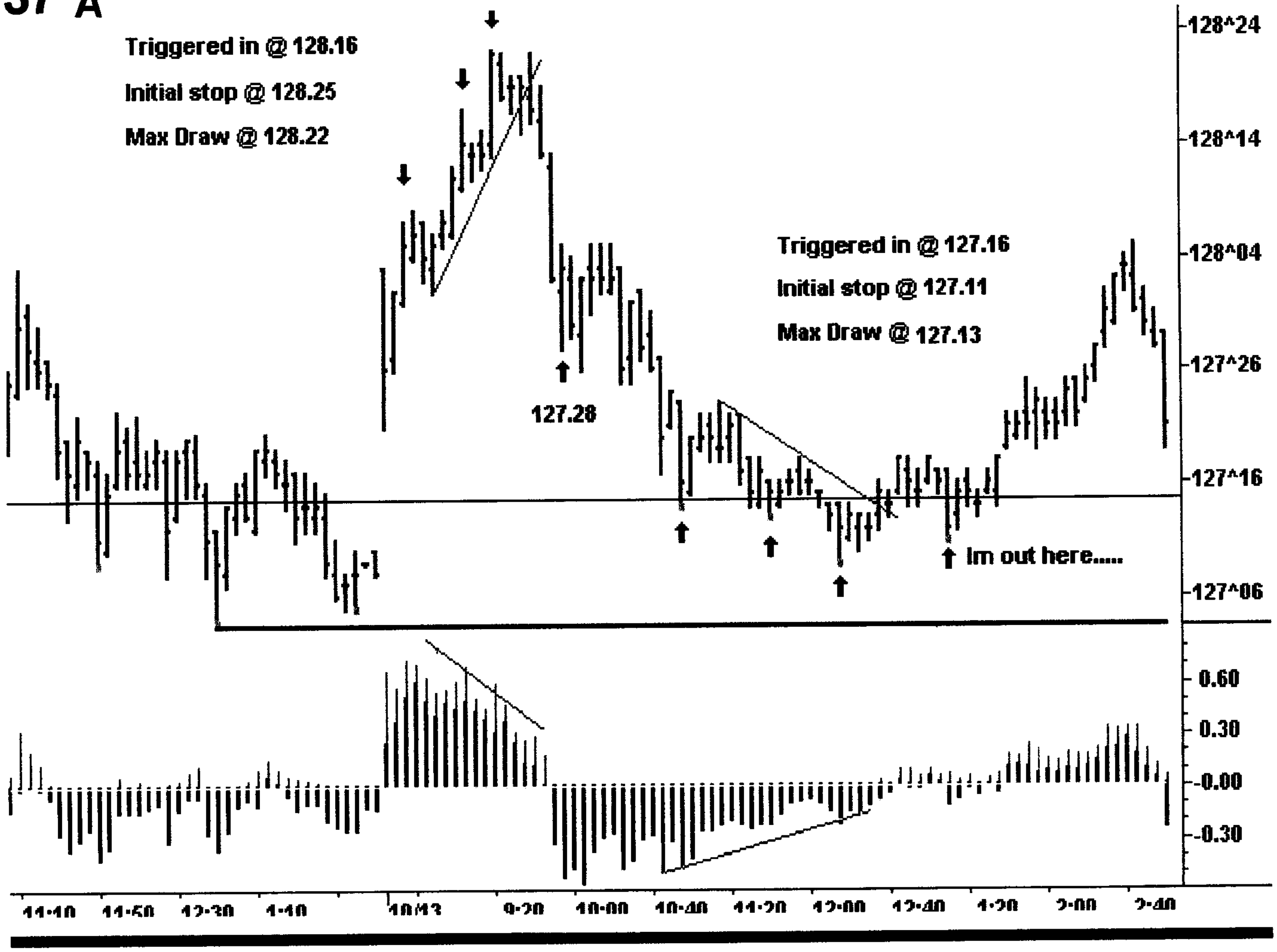
98
4
7
10

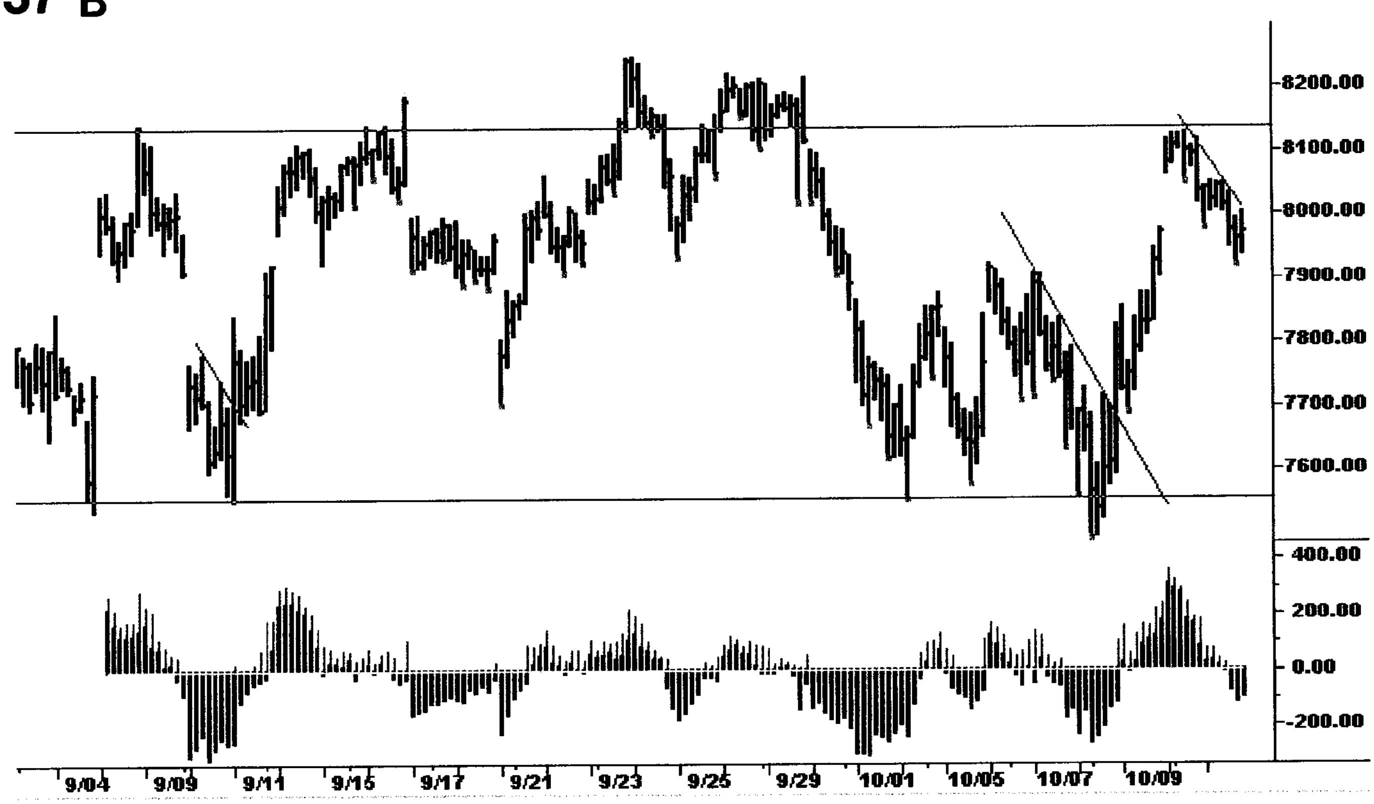
37 A

Dec. Bonds Five Minute



37 B

Dec. Dow Jones Hourly



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