HOW & WHEN TO INVEST IN THE **STOCK MARKET**

HOW & WHEN TO INVEST IN THE STOCK MARKET

Winning Market Trading Strategies

by

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How & When To Invest In The Stock Market

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To my readers:

Thank you for purchasing (or considering the purchase of) this book, "How & When To Invest In The Stock Market". **It is designed to help all of us to get the most out of our investments with the least amount of effort**. I've written this book with both the novice and the experienced investors in mind.

Please allow me to make a few suggestions:

- Do not become an impulse buyer either for investment or consumption, it is disastrous.
- Learn to save and invest wisely. Never borrow money to invest.
- Always believe in yourself. Do not compete. Stick with what you know.
- Never, ever, invest in anything that you don't understand regardless of lucrative promises.
- Do not chase the stock market and act emotionally. Remain patient. If you miss one train, there is always another coming.
- Don't be pushed by human emotions or feelings about the situation, and don't get influenced by the media and friends. The market has no feeling. Remember, the overall trend of the market determines whether or not you will make money.
- Don't let your profit turn into a loss; Don't turn your loss into a bigger loss.
- Invest reasonably of your time and effort to master the techniques described in this book. Be self-disciplined. Stick with the investment plan described in this book. Don't try to "outguess" the plan or the market. They are always right.
- Follow all the rules all of the time. Rules are not made for framing.

This book provides us with a plan to become a successful investor. This book tells us when to get in the market and when to step aside. It addresses the damaging effect of emotions from the investing process.

Nothing is impossible to those who are persistent, sincere and willing to work hard, have self confidence, and trust in themselves and accept the authority of the Almighty Great Lord. These and other good virtues bring the blessing of the Great Divine force closer, the key element required for the successful completion of all projects.

Do not be envy of others if they are doing better in the market than you are in spite of you working hard and diligently at it. Because they have inherited or earned something that you don't have or acquired. Don't be disappointed, you can too!

With the grace and blessing of H. D. H. Hariprasad Swamiji, I am pleased to put this book in your hands, and hope that it will serve as a valuable tool in timing your investments in the great market of America.

Net proceeds from the sale of this book will be donated to the Yogi Divine Society, a non-profit organization registered in India and in U.S.A., founded by H. D. H. Hariprasad Swamiji, and devoted to serve all human kind, regardless of race, creed or religion, in all aspects of life and, to enrich all by enhancing the social, moral and spiritual values for a more contented life. A few of the many objectives of the society are listed below.

- A drug-free society,
- The importance of non-violence,
- The importance of vegetarianism,
- The importance of positive thinking,
- The promotion of social and moral ethic,
- The physical, mental and spiritual betterment of youth,
- The inevitability of spiritual master in life.

My whole point in writing this book was never to make money from the sale of this book. Sincerely, I made the effort to write this book to make sure my methodology didn't retire with me and to help investors like me.

Ten Rules For Investing

(1) *I will spend at least one hour a week to collect, tabulate and analyze the market data.*

(2) *I will include a checklist in my "week-end review" to make sure I don't miss any signal that is generated or is about to be generated by the methodology.*

(3) *I will not buy anything based on rumors, advertisements, recommendations or performance figures and lucrative tempting articles published, advertised or received in the mail until I verify and test the issue in question using the methodology described in this book.*

It is better I spend more time now to investigate, rather than being sorry later if the investments were found to be questionable.

(4) *I will act according to the actions generated by the signals. However, I will not expect action generated by every signal to be profitable.*

(5) *I will not pay any attention to the level of the market at which the signal is generated.*

(6) *I will not hesitate to take losses if so warranted by the signal. If my decision based on the signal is proved to be wrong, I will not get disturbed in anyway.*

(7) *I will ban all wishful thinking, guesswork, emotional feeling and get-rich-quick notion in exercising buy and sell actions.*

(8) *I will use mental stop loss (MSL) limit technique as often as necessary to protect profits and cut losses.*

(9) *I will follow the guidelines on managing risk all of the time.*

(10) *I will refrain from making guesswork or judgment about the market, in that:*

- *Why is the market going up?*
- *Why is the market going down?*
- *How high the market can advance?*
- *How low the market can decline?*
- *Duration and extent of the advance in a bull market.*
- *Duration and extent of the decline in a bear market.*

DEDICATION

To my Divine Charioteer,
the giver of all wisdom.

&

To my parents,
who worked hard during their lifetime saving penny after penny for their children's education. Their pocketbooks were empty, but their hearts were filled with love and joy.

Acknowledgments

The best part about writing this book is to give credit to whom it belongs. First, I wish to acknowledge the single most important person without whom it would not have been possible to create this book. The person is my long-time companion and beloved wife, Kaumudiben, who greatly influenced and inspired me to put the market trading methodology on paper for the benefit of investors like me, and who patiently waited during my many years of study and research.

I wish to acknowledge my sons, Pravinkumar and Ajaykumar, who encouraged me to turn this project into a reality by providing a personal computer and a printer to help me to transform my hand written scattered notes into this book.

I thank my children for reading the draft and making valuable suggestions. I also thank Mr. Bernard Kotalik for his assistance in editing initial draft of some of the chapters.

Blessing

To my beloved children and grandchildren, may the future they inherit by this book be one that is creative, full of excitement and innovations. May Lord Swaminarayan bless them in theirs thrive for a financially independent life.

TABLE OF CONTENTS

CHAPTER 3: STOCKS, MUTUAL FUNDS & OPTIONS

CHAPTER 4: STRATEGIC TRADING DISCIPLINE

WHY THIS BOOK?

Why another book on the stock market when there are so many books on the store shelves? If you went to a book store, you would find a number of books, all written by people who have claimed to have been right on predicting trends of the stock market, and have published market letters.

Most books offer very little to the individual investor who wants to manage his or her investments in the stock market and who is willing to devote some time and effort to achieve superior investment returns. This book has been written keeping such investors in mind and is well suited to all types of investors whether they are traders, speculators or conservative investors.

In the early 60s, I was introduced to the stock market by a friend of mine who was a veteran investor. I bought few shares of a company recommended by him and made some money in a relatively short period of time. Based on this experience, investing in the stock market became very appealing to me.

I knew nothing about the stock market and how it works. I began investing blindly based on the recommendations from brokers, friends and investment advisory services. I never bothered to investigate those recommended stocks because I did not know how. I was afraid of missing the opportunity if I had spent some time learning how to investigate them. I was tossing the dart in the dark and hoping to hit it right for the big bucks.

All advisory services' recommendations sounded very good and tempting to me, but they were too many. It was not practical for me or for anyone, as a matter of fact, to invest in all of them. I was facing a dilemma. One of the brokers on the street once told me that if I went to all the advisory services in the country and tabulate their bad and good recommendations, I would find that a majority of the stocks listed on the major exchanges would be on a buy list because if one service recommended to sell the other recommended it to buy.

[*Comment:* Most advisory services are generally right in good times—that is when the market is advancing in full force. Those who are right consistently during the declining stock prices should be the ones whose advice is worth paying for.]

I began investing in the stocks of various companies based on the recommendations offered by brokerage and advisory services. I believed in and trusted them. All those resulted in accumulation of losses after losses. Occasionally, I made a little profit, but losses remained at large.

When the recommended investment went sour, I turned to a broker or a friend for advice. A typical scenario usually went this way:

- I became worried and asked the broker. What did broker say—Well the market was currently sluggish and was consolidating for a further move and the stock was reacting normally to the general market.
- After a couple of weeks, market began moving up but my stock did not. I called the broker and asked, what was happening—Broker replied, "the stock is a laggard because the industry in which it belongs isn't moving up so it is a normal reaction. Once the industry group

begins to move up, the stock will participate with it." So I decided to hold the loser a little longer.

- The industry group began moving up, but the stock kept declining. So I called the broker third time and asked the same question. Broker then replied that the company announced that it would not meet the estimated earning projection and it would likely report a lower earning, etc.

I could not understand why the recommendations did not work as they should have. I was astonished and unable to understand what was really happening. I was lost in the wilderness of confusion, promise, temptation, etc. The only person who made money out of me was my broker. This left me no choice but to develop my own theory for detecting market trends and to weed out potential poor performers.

Finally, I realized that my actions, although were consistent with the recommendations, but were not consistent with the market's anticipated trends. The experience taught me a lesson. I must look somewhere else for an answer. But where? I realized I must become my own teacher, I must be my own advisor, and I must believe no one except the market because it is the only one who knows where it is going.

Therefore, I concluded that I should not invest until I have acquired sufficient knowledge about the stock market and formulated a system. I realized that I needed a set of clear and concise rules to direct me when to be in the market and when not to be. That's why I wrote this book to present the methodology of how and when to invest in the stock market.

It is therefore very important and vital for investors that those recommendations and opinions should be filtered through a pre-designed and pre-tested system before an action is taken. Remember, it's your money and only yours, not theirs.

To make money in the stock market requires some knowledge and understanding of where the market is headed overall. An attempt is made here to find a methodology that can help investors to detect market trends by generating buy and sell signals.

I also recognized that it was necessary to have more than one kind of signal. One kind of signal can fail but with different kinds of signals, we would have better chance of success in detecting changes in the path of the market. To protect against unanticipated surprises while working with these signals, we need safety guards, watchdogs to watch over those signals to alert us if the market begins to move against the signal.

Therefore, I wrote this book to present a system, a methodology that can keep the investors in the market for enough time to build profits; that can alert investors when to cut losses; and that can guard against recommendations, opinions, etc. expressed by others. Realizing that no system can be perfect, a need for such a system cannot be over-emphasized.

This book describes that system (methodology) which is developed using the market data collected and analyzed for over more than fifteen years. The book contains many actual examples, to demonstrate the procedures described in the methodology, that investors can follow and practice. The examples and case studies reflect actual trading situations regarding losses and profits.

One must remember that the methodology is the mean to accomplish a goal. Its timely and skillful application is equally important. In general, the goals are:

- To achieve maximum returns while minimizing risks and losses.

- To avoid the notion of being fully invested in the market at all times.
- To recognize the bull and bear market periods.
- To avoid the temptation of predicting the market tops and bottoms.
- To demonstrate the importance of cultivating good habits and self-discipline to become a successful investor.

Note losses and profits are two sides of the same coin; one doesn't exist without the other. That is to say losses are sometimes unavoidable. Therefore, the objective of investing should be to incur little or no loss as few times as possible. Too many little losses or a single large loss can eat away the initial capital set aside for investment.

This book is intended to serve those goals that can be achieved by mechanically following the methodology. To achieve this, one must be self-disciplined to stick with the methodology long enough to allow it to work.

A word of caution—*One must refrain from guesswork and must not render judgment against the buy and sell signals generated by the methodology. Without the buy and sell signals, we won't know which way the market is going. One must also have courage to accept losses if so indicated by the signals. One must not insist to stay in the market all of the time. Let the market signals be our guide since neither the duration nor the extent of a bull or a bear market phase can be predicted. The case studies and examples presented will serve as a guide, and one must create a habit of reviewing them as often as necessary.*

No magic formula is offered here for overnight riches because there none exist. The key to successful investing requires self-discipline, a reasonable of time and effort and, sticking with the methodology and the principles discussed in this book all of the time.

I wish you good luck. I hope that as a reader and as an investor you can benefit by learning and applying the methodology presented herein, and learn to modify it by including new parameters to suit the changing market conditions. In the field of investment, nothing is static; it is a fast moving and changing field. *For example, tracking of cumulative sum of up volume minus down volume (Vcs) was discontinued in 1996, as it was not found to be useful (refer to Table 205A in Appendix B.)*

May Great Lord bless you!

GETTING STARTED

Prerequisite

This book has been written for individuals who want to manage their own investments and who are willing to devote some time and thought to achieve superior investment returns.

This book assumes that the readers have general knowledge of the stock market, stocks, mutual funds, and market indexes, such as DJIA (Dow Jones Industrial Average), DJTA (Dow Jones Transportation Average), S&P 500 (Standard and Poor's 500 Index), S&P 100 (Standard and Poor's 100 Index which is commonly referred to as OEX) and the Value Line Geometric Index and some familiarity with business newspapers, such as *Barron's*, *Investor's Business Daily*, and *The Wall Street Journal*.

Readers should also be willing to spare at least one hour of their time every week for collecting market data, and tabulating and analyzing them in accordance with Chapter 2.

How to study this Book?

The following study procedure is suggested to quickly grasp an understanding of the methodology behind trading stocks, mutual funds and index options:

1. First read Introduction, then briefly review chapters in the following order, whether you completely understand or not:
   Chapter 4, Chapter 5, Chapter 6, Appendix A, Chapter 3, Chapter 2, Chapter 1 and Chapter 7.
2. Then read all chapters in a chronological order.
3. In order to become thoroughly familiar with the methodology, it is necessary to Study Chapters 1, 2 and 3 as often as necessary.

If, however, it is hard to grasp the concept of buying and selling stocks, mutual funds, and trading index options, it is suggested to study these chapters section by section until the concept is completely understood before moving to the next section of the chapter.

Note: Abbreviations are explained separately under Section titled "Nomenclatures". Refer to "Table of Contents".

What's Next?

Now having read the book and become familiar with the methodology of trading stocks, mutual funds and index options, you may be wondering how and when to begin.

It is relatively easy to implement the methodology. Any time is better than no time. It is never too late.

One can begin from week one for collecting the market data listed in Table 200 (Appendix B), and then continue thereafter, every week to build a file necessary to generate short and long term signals described in Chapter 1. Refer to Chapter 2 on how to tabulate and analyze the data. Necessary calculations can be performed using a hand-held calculator. However, use of software designed for performing these calculations will facilitate the process if a personal computer is available.

In order to generate market signals discussed in Chapter 1, at least the last 40 weeks of market data is required; under normal situation, one can get by with only 30 weeks of market data unless a long term signal is in the horizon. Many local libraries generally retain past newspapers, such as *The Wall Street Journal*, *Barron's* and other local newspapers on micro films, which will be helpful.

◆ Caution/Suggestion ◆

It is easy to fall in love with the stock market and get addicted
Therefore, one should know his or her dollar & risk tolerance limits
within the budgetary constrictions
and should invest within those limits.

It happened to me
and I don't want it to happen to you,
that's why I wrote this book.

INTRODUCTION

In the economic environment, many conditions exist that have influence on the investors' behavior and the behavior of the stock market in general. People act and react differently to each or similar situations creating trends in the stock market, creating a "road map" of the market. The purpose of this book is to detect those trends and learn how to use them. As the saying goes—you can't create an opportunity in the stock market, but you can recognize one and take advantage of it.

It is just not possible for any individual investor to track, to evaluate and to conclude all economic indicators affecting the trend of the market. It is even more difficult to interpret them when they contradict each other. Therefore, some economic indicators and political events are not recorded, followed or analyzed.

Any changes in the economic indicators, positive or negative, should generally be evidenced by the market actions several months ahead of the forthcoming changes in the economic arena. Therefore, a tool or a methodology is necessary to feel the pulse of the market weekly, or sometimes daily, and to forecast the onset of the trend. No attempts will be made to predict market tops or bottoms, or length of the bull, bear or hog (stagnant) market conditions. Because no one can predict them consistently and accurately. Therefore, to attempt is shear guess work and a waste of time and effort.

As there are many streets and roads to direct us to our destinations, there are various phases in the stock market to indicate us when to invest. As there are warning, regulatory, etc. signs installed on the road to warn drivers the presence of hazards ahead, as there are exceptions and warnings on the road leading to the stock market trading. This book is intended to serve as a road map for investors. Therefore, a simplified textbook like format is selected to limit the unnecessary details that may distract the investors from the real world. The principles and methodology described in this book will be easy to understand and simple to follow and it will require about one to two hours of time to collect, analyze and tabulate the market data each week. Remember all investments require certain amount of time and effort.

The purpose of this book is to illustrate how and when to invest in stocks, mutual funds and index options as safely as practical. We all want to invest our hard earned savings to make money for needs, such as to stay ahead of inflation, to provide for college education, to provide better living standards for the family, and to build funds for the rainy days and the golden years.

To invest successfully in the stock market, one has to decide on a methodology based on the past performance of the stock market and which can mirror the possible changes in the market trends, such as the one described in this book and one should be persistent to stick with that methodology long enough to allow it to work, even when the market is static or stagnant (moving sideways). One must be self-disciplined to adhere to the plan generated by the methodology when an action, particularly a sell action, is warranted.

Remember, no one is immune from losses all of the time; everyone incurs losses at times. Too many small losses are as bad as one single large loss. By following the methodology described in

this book, one should be able to minimize the number of loss situations and avoid large losses because of the built-in safety guards.

The following is a brief summary of each chapter:

Each chapter is organized in a manner that would make it easy for readers to understand, and grasp the overall concept of the methodology including the assumptions, if any, and the parameters involved.

This book assumes that the readers have general knowledge of the stock market, stocks, mutual funds, and market indexes, such as DJIA (Dow Jones Industrial Average), DJTA (Dow Jones Transportation Average), S&P 500 (Standard and Poor's 500 Index), S&P 100 (Standard and Poor's 100 Index which is commonly referred to as OEX) and the Value Line Geometric Index and some familiarity with business newspapers, such as *Barron's*, *Investor's Business Daily*, and *The Wall Street Journal*.

The reader will notice in Chapter 1, that a market cycle is divided into many zones, and different rules apply in each zone. Long and short term buy and sell signals are developed to predict the market's future course of action based on the level of each indicator described in Chapter 2. Without such a signal, we would become victims of excitement, tips, gossip, news, recommendations, hopes, etc.

The process of investing is never static. The same things are different at different times. Therefore, any method or procedure may require occasional adjustments due to changing economy and technological environments. As the investor gains experience working with the methodology presented in this book, one can easily adjust the parameters described herein.

Market movements generate buy and sell signals;
signals do not create market movements.

Chapter 2 serves as the nucleus for Chapter 1. Market key data collected and analyzed weekly are tabulated and summarized in this chapter. The result from this analysis is used in Chapter 1 to develop buy and sell signals.

No pain, no gain; Work smart, Don't work hard.
Don't get buried under the overwhelming information.

Chapter 3 discusses subjects such as where and how to find information on stocks, pitfalls associated with such findings, and when to buy and sell stocks and mutual funds. A special section is devoted on trading index options.

Never ever consider buying anything without a buy signal
Key is to avoid buying at or near the top.

Chapter 4 includes guidelines for the investors to follow in order to negate as many mistakes as possible to increase potential for profit.

To stick with the methodology is the key and
it is the toughest part of investing.

Chapter 5 covers what investors should do if and when a decision is made to invest funds based on the buy and sell signals generated in Chapter 1.

Profits and losses are two sides of the same coin;
one doesn't exist without the other.

Chapter 6 includes a summary of market signals which are compiled from Chapter 1, and each signal is summarized with resulting profits and losses for information and reference.

No one is immune from losses all of the time;
everyone incurs losses at times.

Case studies using actual market data are presented in Chapter 7. Lessons learned from such studies should be recorded by investors for future use and to modify the trading rules if it should be necessary. Lessons from these and other similar case studies will hopefully make us better investors.

Although case studies are not necessarily indicative of future results, they
do help in making educated investment decisions.

Pertinent information is included in Appendix A for reference. Filled-in tables and examples are included in Appendix B.

In conclusion:

The main objective of the system presented in this book is to minimize losses majority of the time as much as possible. **Table 602 lists all buy and sell signals generated by the system from January 1986 to July 30, 1999. Note that signals generated 88 short-term and 24 long-term buy and sell actions which are listed in column titled "Short-Term Trading Scenario" of Table 602 in Appendix B; only five of which led into some or little loss situations.** They were:

(1) S3 buy signal of 8/19/88,
(2) L3 (long-term) buy signal of 5/11/90 and L3 (long-term) sell signal of 8/3/90,
(3) S7 buy signal of 11/16/90,
(4) S3 buy signal of 9/24/93, and
(5) S5 buy signal of 10/14/94

However, it should be noted that the future results could differ because the process of investing is never static and is constantly changing as the market conditions, and the economic and political environments change.

High lights about the buy and sell signals:

Long-term signals are suitable for long term investments such as mutual funds. Refer to Chapters 3 and 5 for details.

Short-term signals are suitable for trading index options in accordance with Section 304 in Chapter 3, and they may be used for adding funds to existing long term positions if the market conditions are favorable.

Observation reveals that the market never remains steady. It usually moves like a small tidal wave creating minor bottoms and tops. To take advantage of these short ups and downs, investors may trade index options with the money they can afford to lose. Review Section 304 in Chapters 3. Study

case studies included in Section 704 in Chapter 7 to gain better understanding of trading options before making a final decision.

To invest in stocks—one should decide first which stocks to buy then when to buy and when to sell. Which stock to buy or to sell is important, but when to buy or to sell is far more important and also the most difficult task.

It should be noted that stocks do not always move in tandem with the market. Each stock has its own characteristics and has its own timing for buying and selling. Buy and sell signals for stocks are discussed in Section 302 in Chapter 3. Review of the case studies included in Section 702 in Chapter 7 and becoming familiar with the examples in Tables 300 will facilitate the decision making process.

❖ *Market movements generate buy and sell signals;*
signals do not create market movements ❖

Chapter 1

TECHNICAL INDICATORS & SIGNALS

(Making Investing Scientific)

OBJECTIVE

Investing is an art or a skill, not a science. The methodology presented in this chapter makes investing scientific.

At the conclusion of this Chapter, you will be able to understand the methodology leading to various market signals, exceptions, warnings, etc.

OVERVIEW

How various market key indicators are combined to generate market movement zones, buy and sell signals, exceptions, etc. are covered in this chapter. Note that this chapter uses data from Chapter 2.

This Chapter is divided into following Sections:

SECTION 100
INTRODUCTION TO MARKET SIGNALS

(A) What Are Signals?

When various indicators are combined in a certain fashion, a buy or a sell signal may be developed. Signals detect changes in the market's short-term or long-term trends. They do not predict the length of the trends. To make predictions or to set goals of market tops or bottoms is like diving into uncharted water. For making proper investment decisions, the only thing necessary to know is the beginning and ending of the market trends.

To some extent, we can have knowledge of the present condition of the market, but not the future. Therefore, we should learn to travel with the present condition by changing strategy as the condition changes along the road. For example, if we are waiting for a train at the station, we are not sure if the train is going to arrive on time. We would only know when the train actually arrives at the station. The destination time of the train to the next station will also be uncertain. Anything could happen along the way to the next station. It may get stuck due to engine problems or other unforeseen conditions. As a passenger, we should be alert and be prepared for the worst. We should have a contingency plan in the event if it should be necessary to take proper action. It is always better to get on a moving train going in the right direction, and be prepared for any consequences, rather than getting on a waiting train and not knowing when and where it is destined.

Therefore, it is resolved here that signals do not detect trends before they begin. They will detect trends once the trend is in progress or about to begin. Sometimes they can miss the trends. If the trend is going to get stalled, signals will warn the investors in a majority of the cases. However, no method exists that consistently pinpoints beginning and ending of every trend in a market cycle.

Short-term signals (S1 to S9 and SZ) are discussed in Section 102. Long-term signals (L1 to L3) are covered in Section 103. They are listed in the following Table:

	S1	S2	S3	S4	S5	S6A	S6B	S6C	S7	S8	S9	SZ	L1	L2	L3
Buy	√	√	√	√	√	√	√	√	√	√	√	√	√	√	√
Sell	√	√	√	√	√	-	-	-	-	√	√	-	√	√	√

√ Indicates whether the signal is a buy or a sell signal.

(B) How Signals Can Help Investors

By following the signals and associated rules when investing, investors should be able to maximize profits and minimize losses. No one on the earth can avoid losses all of the time; key is to avoid losses majority of the time.

Investors must be willing to devote at least one hour weekly in collecting data, tabulating and analyzing them (refer to Chapter 2). No pain, no gain. Don't rely on others to do your homework

because others may have a different motivation and objectives. Others surrounding you are only interested in commissions whether you make money or you don't.

SECTION 101
MARKET MOVEMENT ZONES

Based on the DJIA's 30-week and 40-week moving averages and their rates of movement, the market forms various zones, namely A through F. For examples, the market is considered to be in Zone A if both the moving averages and their rates of movement are rising, and in Zone B if they all are falling. There are four parameters determining various zones, they are:

- DJIA 30-week Moving Average = D30
- DJIA 40-week Moving Average = D40
- DJIA 30-week Rate of Movement = R30
- DJIA 40-week Rate of Movement = R40

The following Table shows the **market movement zones** depending on the above four parameters whether they are rising (UP) or declining (DN). For details, refer to Section 209 in Chapter 2.

R30	UP				DN				DN				UP			
R40	UP				UP				DN				DN			
D30	DN	UP	DN	UP	UP	DN	UP	DN	UP	DN	UP	DN	DN	UP	DN	UP
D40	DN	DN	UP	UP	UP	UP	DN	DN	UP	UP	DN	DN	DN	DN	UP	UP
ZONE	F1	F2	F3	**A**	C1	C2	C2	C3	D1	D2	D3	**B**	E1	E2	E2	E3

Based on the points assigned to each zone as shown in the Table below, zone may indicate ongoing market sentiment and which, in certain cases, influences the validity of the buy and sell signals. Zones A, C1, E3, F2 and F3 generally indicate bullish sentiment where as zones B, C3, D2, D3 and E1 reveal bearish sentiment; zones C2, D1, E2 and F1 are neither bullish nor bearish and therefore they should be considered neutral.

ZONE	F1	F2	F3	**A**	C1	C2	C2	C3	D1	D2	D3	**B**	E1	E2	E2	E3
Points	0	3	4	7	4	1	0	–3	0	–3	–4	–7	–4	–1	0	3

SECTION 102
SHORT-TERM SIGNALS

(A) S1 Signals

1. General

S1 Signals are based on the status of IO and VI indicators. S1 signals are generated when IO and VI indicators are combined as shown in the following Table.

Rules For S1 Signals

Market Zones	Indicators (Indexes)		**S1 Signals** {See Notes (1) & (2) below}	Rule #	**S1 Signals Designation**
	IO	VI			
A, A+, C1 or F3	IN	---	Buy	1	S1/BY/1
B, B–, D3 or E1	OT	---	Sell	2	S1/SL/2
All	IN, IN1, IN2	Bbc	Buy	3	S1/BY/3
All	OT, OT1, OT2	Sbc	Sell	4	S1/SL/4

Notes: (1)When S1 signals occur before the end of the week, it is suggested to wait until the week is concluded per Section 213, Chapter 2.

(2)IO & VI or VI & IO indicators cannot be used to generate a S1 Signal if there is an opposite nature of S1 Signal between them. For examples, refer to Table 102A in Appendix B.

IO and VI indicators are discussed in sub-sections 2 and 3 below. For market data required for the development of IO and VI indicators, refer to Tables 201A, 201B, 205A and 205B in Appendix B.

For a sample log of S1 signals, refer to Table 102A in Appendix B.

2. IO-Indicator

(a) General

IO-Indicator consists of IN, a bullish index and OT, a bearish index. They are further divided as follows:

- IN, IN1 and IN2 are bullish indexes, and
- OT, OT1 and OT2 are bearish indexes.

They are determined from Tables 201A and 201B in Appendix B as described in (b) and (c) below.

(b) IN, IN1 and IN2 Indexes

1. Determine the low point (LP) of 5-sum of 10-day ms (moving sum) of Ia–d (refer to column F in Table 201A). Low point (LP) is established when the 5-sum of 10-day ms of Ia–d in column F rises more than 1500. Post LP in column G of Table 201A.
2. From column C in Table 201A, select the **first occurrence** of "5-day ms" now (i.e., day under consideration) greater than "5-day ms" prior (i.e., 5 days ago). This condition can occur before or after the low point (LP) is posted in column G of Table 201A. If the difference between "5-day ms now" and "5-day ms prior" is five or greater, go to step 3 below.
3. The conditions described in the following Table determine whether the index is IN, IN1 or IN2:

	Conditions	IN	IN1	IN2
i	Direction of last three 5-day ms in column C of Table 201A, is up with tolerance of no more than five (5) points down	Yes	Yes	No
ii	Column E2 > Column E1 (Table 201B)	Yes	Yes	Yes
iii	Column F2 > Column F1 (Table 201B)	Yes	Yes	Yes
iv	$\frac{\text{DJIAn minus DJIAp (Col. B, Table 201A)}}{\text{5-dmsn minus 5-dmsp (Col. C, Table 201A)}}$ is	> 0.90	≤ 0.90	> 0.90

Legend: DJIAn = DJIA now; DJIAp = DJIA prior (i.e., 5 days ago)
5-dmsn = 5-day ms now; 5-dmsp = 5-day ms prior (i.e., 5 days ago)

(c) OT, OT1 and OT2 Indexes

1. Determine the high point (HP) of 5-sum of 10-day ms (moving sum) of Ia–d (refer to column F in Table 201A). High point (HP) is established when the 5-sum of 10-day ms of Ia–d in column F declines more than 1500. Post HP in column G of Table 201A.
2. From column C in Table 201A, select the **first occurrence** of "5-day ms" prior (i.e., 5 days ago) greater than "5-day ms" now (i.e., day under consideration). This condition can occur before or after the high point (HP) is posted in column G of Table 201A. If the difference between "5-day ms prior" and "5-day ms now" is five or greater, go to step 3 below.
3. The conditions described in the following Table determine whether the index is OT, OT1 or OT2:

	Conditions	OT	OT1	OT2
i	Direction of last three 5-day ms in column C of Table 201A, is down with tolerance of no more than three (5) points up	Yes	Yes	No
ii	Column E2 < Column E1 (Table 201B)	Yes	Yes	Yes
iii	Column F2 < Column F1 (Table 201B)	Yes	Yes	Yes
iv	DJIAn minus DJIAp (Col. B, Table 201A) / 5-dmsn minus 5-dmsp (Col. C, Table 201A) is	> 0.90	≤ 0.90	> 0.90

Legend: DJIAn = DJIA now; DJIAp = DJIA prior (i.e., 5 days ago)
5-dmsn = 5-day ms now; 5-dmsp = 5-day ms prior (i.e., 5 days ago)

3. VI-Indicator

(a) General

VI Indicator consists of B, a bullish index and S, a bearish index. They are further divided as follows:

- Bs, Bm and Bb are bullish indexes, and
- Ss, Sm and Sb are bearish indexes.

They are determined from Table 205B in Appendix B as shown in (b) and (c) below.

(b) Bs, Bm and Bb Index Rules

1. Bs-Index
   If "V% – I%" is less or equal to "1.40" (no tolerance) at low points (LP) of both the moving averages (V% and I%) concurrently, it is then called a Bs index.
2. Bm-Index
   If "Vm% – Im%" is less or equal to "1.40" (no tolerance) at low points (LP) of both the moving averages (Vm% and Im%) concurrently, it is then called a Bm index.
3. Bb-Index
   Bb index is when both the Bs and Bm indexes occur. Bs and Bm indexes can occur concurrently or separately.
4. Index Confirmation:
   The B-index is confirmed when the moving average line (I+N)/2 (refer to Table 205A in Appendix B) rises by more than 500 from its most recent low. *However, during the bull phase (refer to Section 603) of the market, B-index can be confirmed if (I+N)/2 line rises by more than 300 provided (I+N)/2% line (refer to Table 205B in Appendix B) also rises by more than 0.05.*

   Confirmation becomes voided if the line (I+N)/2 falls later, by more than the values specified above, which will then make the B-index void generating a Warning WB. Refer to Warning WB in Section 105 for details.

(c) Ss, Sm and Sb Index Rules

1. Ss-Index
   If "V% – I%" is greater or equal to "3.00" (no tolerance) at high points (HP) of both the moving averages (V% and I%) concurrently, it is then called a Ss index.

2. Sm-Index
   If "Vm% – Im%" is greater or equal to "3.00" (no tolerance) at high points (HP) of both the moving averages (Vm% and Im%) concurrently, it is then called a Sm index.
3. Sb-Index
   Sb index is when both the Ss and Sm indexes occur. Ss and Sm indexes can occur concurrently or separately.
4. Index Confirmation:
   The S-index is confirmed when the moving average line (I+N)/2 (refer to Table 205A in Appendix B) falls by more than 500 from its most recent high. *However, during the bear phase (refer to Section 603) of the market, S-index can be confirmed if (I+N)/2 line falls by more than 300 provided (I+N)/2% line (refer to Table 205B in Appendix B) also falls by more than 0.05. Example is 9/16/94 S1/SL in Table 102A.*

   Confirmation becomes voided if the line (I+N)/2 rises later, by more than the values specified above, which will then make the S-index void generating a Warning WB. Refer to Warning WB in Section 105 for details.

(d) Terminology

Bbc = Bb is confirmed, similarly Bsc and Bmc.
Sbc = Sb is confirmed, similarly Ssc and Smc.
Note that B-index (Bs, Bm and Bb) and S-index (Ss, Sm and Sb) by definition, are not revealed until a week after they have occurred. Therefore, suffix 'r' is used to denote where appropriate if and when a index is revealed. Suffix 'r' is replaced by 'c' when the index receives confirmation unless the confirmation has occurred before. It is so noted in Tables 102A and 205B in Appendix B.

(B) S2 Signals

1. General

The S2 signal is similar to S1 signal. Since VI-indicator required for a S1 signal does not occur as often as IO-indicator, this signal is developed to capture signals missed by the S1 signal conditions. The S2 signal is generally good for one week; it may be good for two or more weeks depending on the market conditions and other indicators.

The S2 signal should only be considered if conditions for S1 signal do not exist. That is to say: There is no need to check conditions for S2 signal if S1 signal occurs during the same week.

For market data required for S2 signals, refer to Tables 201A, 201B, 205A, 205B, 206 and 209 in Appendix B.

For a sample log of S2 signals, refer to Table 102B in Appendix B.

2. S2 Buy Signal

A buy signal is generated when the following conditions (a) and (b) **exist** during the same week, or few (say, one to three) weeks apart **in the order listed**:

(a) IN, IN1, IN2 or Bbc-Index occurs.

(b) This condition consists of the following three parts which must be satisfied by end of the same week:

1. Zone ≠ B, B–, C3, D2, D3 or E1
2. MC = 0/5 or 1/4
3. (I+N)/2 is up by at least 150 points from the *previous* week. (Note: If (I+N)/2 is not up by at least 150 points from the previous week, then (I+N)/2% should be up by at least 1.00% in order to meet this part of the condition.)

3. S2 Sell Signal

A sell signal is generated when the following conditions (a) and (b) **exist** during the same week, or few (say, one to three) weeks apart **in the order listed**:

(a) OT, OT1, OT2 or Sbc-Index occurs.

(b) This condition consists of the following three parts which must be satisfied by end of the same week:

1. Zone ≠ A, A+, C1, E3, F2 or F3
2. MC = 5/0 or 4/1
3. (I+N)/2 is down by at least 150 points from the *previous* week. (Note: If (I+N)/2 is not down by at least 150 points from the previous week, then (I+N)/2% should be down by at least 1.00% in order to meet this part of the condition.)

(C) S3 Signals

1. General

During an advancing or declining market, reactions (up and down waves) in the market can occur. As a result, a short-term buy or sell signal is occasionally developed.

This signal is based on a Call-Put (C/P) ratio combined with the difference between the percentages based on the advance-decline issues from week-to-week (A) and advance-decline issues for the week (B).

C = Ratio of Call Volume to Call Open Interest for the week

P = Ratio of Put Volume to Put Open Interest for the week

$$A = WIa\% = \frac{WIa}{(WIa+WId)}$$

$$B = Ia\% = \frac{Ia}{(Ia+Id)}$$

For the above market data, refer to Table 200 in Appendix B.

For a majority of the cases, this signal is good for one week or less unless other indicators and/or signals are developing to support the action generated by S3 signal. However, investors should remain alert during the week; supporting signals or indicators may or may not occur. It is a speculative (buy on Monday, sell on Friday) signal.

This signal may be used for trading options in accordance with Section 304 in Chapter 3. Since the signal is good for one week only, it is necessary to take a position before noon of the next trading day (Monday) and dissolve the position on or before the last trading day (Friday) of the week, regardless of profit or loss, unless other indicators or signals have occurred during the week to support the action initiated.

For a sample log of S3 signals, refer to Table 102C in Appendix B.

2. S3 Buy Signal

A buy signal is generated when all of the following conditions (a) through (g) are met:

(a) This signal is valid in zone A (including A+) and zone B (including B–). It is also valid, within seven weeks after the end of these (A, A+, B or B–) zones, but in no case greater than the length of these A, A+, B or B– zones.

(b) C/P < 1.20 and (A–B) = 0 through –6.00, **or**
C/P < 1.00 and (A–B) = 0 through –7.00 and SSR < 36.00,

Note: If the above condition (b) occurs consecutive weeks, only the first condition in such occu-rrence should be evaluated for a buy signal; the 2nd, 3rd, etc. conditions in such occurrence should be ignored.

For example, refer to C/P and (A–B) conditions in Table 102C for week endings 10/28/88, 11/4/88 and 11/11/88.

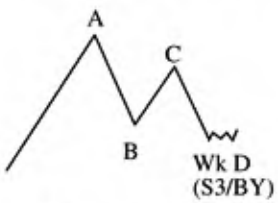
Special (b) condition:

(A–B) sub-condition shown above may occur within 2 to 3 weeks after a C/P sub-condition, and if the ratio C/P during those weeks remain below 1.80.

For the following conditions, refer to Table 102C in Appendix B for column information:

(c) Column F (DJIA) should be the **lowest** since the last most recent top (crest) in DJIA (Column J) as defined in Figure 102(C)2 below based on the DJIA chart constructed using the **daily** closing prices.

Figure 102(C)2—Chart of DJIA Daily Closing



Note: 'A' > 'C'

'A' is considered top if % change from 'B' to 'C' less than 2.70%; otherwise 'C' is considered top.

If 'A' is the top then 'B' should not be lower than the lowest point in Wk D (S3/BY). If 'B' is lower, then 'C' is the top. Refer to Example below.

If 'A' < 'C', 'C' is considered top.

Example: WkEd 10/11/91 S3/BY (Refer to Table 102C in Appendix B)

WkEd	Day	DJIA	Top/Btm	Point	% Change	Remarks
8/30/91	Wed	3055.60	Top	A	----	
9/13/91	Tue	2982.56	Btm	B	2.39 *	* For information only
9/27/91	Tue	3029.07	Top	C (A > C)	B → C = 1.56	% Change from B to C is < 2.70. Therefore, A is top
10/11/91	Mon Friday	2942.75 (Low) 2983.68	----	Wk D (S3/BY)	----	Point B is higher than the lowest point (2942.75) in Wk D. Therefore, point A is top. (#)

(#) If point B were lower than the lowest point in Wk D, then the point C would have been considered top.

(d) Week ending in Column H should not be the same week ending in Column A.
(e) Column K: Column E minus Column F should not exceed 1.40% of Column E.
(f) Column L: Column J minus Column F should be more than 2.70% of Column E.
(g) Column M: Ratio of Column L to Column K should be more than 2.50.

3. S3 Sell Signal

A sell signal is generated when all of the following conditions (a) through (g) are met:

(a) This signal is valid in zone A (including A+) and zone B (including B–). It is also valid, within seven weeks after the end of these (A, A+, B or B–) zones, but in no case greater than the length of these A, A+, B or B– zones.

(b) C/P > 1.80 and (A–B) = 0 through +2.50, **or**
C/P > 2.00 and (A–B) = 0 through +4.00, **or**
C/P > 2.20 and (A–B) = 0 through +6.00

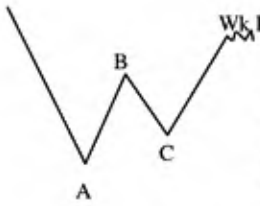
Note: If the above condition (b) occurs consecutive weeks, only the first condition in such occurrence should be evaluated for a buy signal; the 2nd, 3rd, etc. conditions in such occurrence should be ignored.

Special (b) condition:
(A–B) sub-condition shown above may occur within 2 to 3 weeks after a C/P sub-condition, and if the ratio C/P during those weeks remain above 1.20.

For the following conditions, refer to Table 102C in Appendix B for column information:

(c) Column F (DJIA) should be the **highest** since the last most recent bottom (valley) in DJIA (Column J) as defined in Figure 102(C)3 below based on the DJIA chart constructed using the **daily** closing prices.

Figure 102(C)3—Chart of DJIA Daily Closing Prices



'A' is considered bottom if % change from 'B' to 'C' is less than 2.70%; otherwise 'C' is considered bottom.

If 'A' is the bottom then 'B' should not be higher than the highest point in Wk D (S3/SL). If 'B' is higher, then 'C' is the bottom.

If 'A' > 'C', 'C' is considered bottom.

Note: 'A' < 'C'

(d) Week ending in Column H should not be the same week ending in Column A.
(e) Column K: Column F minus Column E should not exceed 1.40% of Column E.
(f) Column L: Column F minus Column J should be more than 2.70% of Column E.
(g) Column M: Ratio of Column L to Column K should be more than 2.50.

(D) S4 Signals

1. General

S4 signal is based on the ratio of the lesser of week-to-week new highs (WNh) or new lows (WNl) to total number of issues traded (WIt). Refer to Table 200 for WNh, WNl and WIt.

As the market is declining, at certain point along its down-trend, week-to-week new highs (WNh) will begin to expand, but still remains below week-to-week new lows (WNl).

When the ratio of WNh to total issues traded for the week (WIt) is expanding, it indicates strength in the market.

Similarly during the market advancing period, at certain point along its up-trend, week-to-week new lows (WNl) will expand, but still remains below week-to-week new highs (WNh).

When the ratio of WNl to total issues traded for the week (WIt) is expanding, it indicates weakness in the market.

This signal may be classified into a medium to long-term signal category. Market turn-around can occur immediately or within few weeks after the signal.

For a sample log of S4 signals, refer to Table 102D in Appendix B.

2. S4 Buy Signal

A buy signal is generated when the market is at or near its bottom, declining or moving sideways, and if one of the following conditions exists:

(a) The ratio WNh/WIt is increasing consecutively for two weeks with the last (second) ratio over 6.50%.

Caution: Buy signal per condition (a) is not valid *unless it occurs with* MC = 0/5, 1/4 or 2/3 and the market is forming a bottom or has formed a valley as depicted by the DJIA bar chart (refer *to Wall Street Journal*).

(b) The ratio WNh/WIt is greater than 8.00% for any single week.

3. S4 Sell Signal

A sell signal is generated when the market is at or near its top, rising or moving sideways, and if one of the following conditions exists:

(a) The ratio WNl/WIt is increasing consecutively for two weeks with the last (second) ratio over 6.50%.

Caution: Sell signal per condition (a) is not valid *unless it occurs with* MC = 5/0, 4/1 or 3/2 and the market is forming a top or has formed a crest as depicted by the DJIA bar chart (refer to *Wall Street Journal*).

(b) The ratio WNl/WIt is greater than 8.00% for any single week.

(E) S5 Signals

1. General

This signal is based on the ratio of the Specialists shorts to total shorts (SSR) shown in Table 200 or 211 in Appendix B. Most important limits influencing the market behavior are:

- SSR < or = 35.00% which is considered bullish, and
- SSR > or = 55.00% which is considered bearish

Low SSR does not necessarily mean bullish and high SSR does not mean bearish. Specialists shorting mechanism is very complex, hence it is difficult to guess what the specialists would or would not do.

The Specialists action depends on supply and demand. For the market to go up demand for buying must exceed the demand for selling which would force the specialists to short at higher prices. A formation of a valley in the DJIA's bar chart (refer to *Wall Street Journal*) could indicate this situation.

When the ratio is low, there is a room for the specialists to absorb some selling pressure, and specialists will not rush into taking the market higher as long as most of the selling pressure is absorbed by the public. The following example illustrates this situation:

Example

WkEd	SSR	DJIA	OEX	Remarks
6/21/96	28.95	5705.23	646.17	Note DJIA & OEX prices declining in spite of low SSR values
6/28/96	26.32	5654.63	647.53	
7/5/96	31.89	5588.14	633.44	
7/12/96	36.24	5510.56	623.49	
7/19/96	30.90	5426.82	616.72	

On the other hand, when the ratio is high, specialists would be forced to cover their shorts before it gets out of their hands, and hence a need arises for them to take the market down to cover the shorts. A formation of a crest in the DJIA's bar chart could indicate this situation.

For a sample log of S5 signals, refer to Table 102E in Appendix B.

2. S5 Buy and Sell Signals

The following Tables depict buy and sell signal conditions generated by the SSR ratios:

Buy Signal Conditions

SSR	DJIA'S Daily Bar Chart Condition	Signal
< or = 35.00	Market could rise if it has formed a valley (V) within the last two weeks during its down (D), sideways (S) or zig-zag (Z) mode as depicted by the DJIA Daily Bar Chart published in *The Wall Street Journal.* See Footnote (a)	S5/Buy See Footnote (b)

Sell Signal Conditions

SSR	DJIA'S Daily Bar Chart Condition	Signal
> or = 55.00	Market could fall if it has formed a crest (C) within the last two weeks during its up (U), sideways (S) or zig-zag (Z) mode as depicted by the DJIA Daily Bar Chart published in *The Wall Street Journal.* See Footnote (a)	S5/Sell

Footnote (a)

In general, the DJIA daily bar chart indicates the sentiments or the moods of the investors and the results obtained by the signals could differ depending on the bar chart configuration. This is generally important for S5 and S9 signals.

Refer to *Table 102(E)2 on page 1-15* for symbols assigned to various configurations of the DJIA Daily Bar Chart. A great deal of judgment (experience) sometimes may be required in identification of the bar chart to match with the symbols as closely as possible.

Footnote (b)—Special S5/BY Condition

A S5 buy signal generally indicates a long-term buying opportunity if it coincides with the 5-wk moving average of SSR being 35.00 or less. The examples below illustrate this condition.

Example 1

Week Ending	SSR	5-wk MA	Short-term Signal	Remarks
11/18/94	34.18	34.11		
11/25/94	34.49	34.86		EB-wk, Section 105(B)2
12/2/94	34.35	34.31		
12/9/94	34.34	34.23		
12/16/94	35.06	34.48	S5/BY signal	Long term buying opportunity

Example 2

Week Ending	SSR	5-wk MA	Short-term Signal	Remarks
6/28/96	26.32	31.29		L2/SL Signal (*)
7/5/96	31.89	30.46		
7/12/96	36.24	30.71		EB-wk, Section 105(B)2
7/19/96	30.90	30.86		EB-wk, Section 105(B)2
7/26/96	34.61	31.99	S5/BY signal	Long term buying opportunity

(*) From Table 602 in Appendix B

Example 3

Week Ending	SSR	5-wk MA	Short-term Signal	Remarks
3/21/97	36.82	36.60		
3/28/97	34.92	36.54		
4/4/97	33.65	35.70		EB-wk, Section 105(B)2
4/11/97	35.09	35.26		EB-wk, Section 105(B)2
4/18/97	31.47	34.39	S5/BY signal	Long term buying opportunity

Table 102(E)2—DJIA Bar Chart Configuration Symbols

DJIA'S Bar Chart Trend Near the Vicinity of the Signal	Trend Symbols (Described below)
Moving Up	U
Moving Up and formed a Crest	UC
Moving Up and formed a Crest then down or not down, but formed a Valley	UCV
Moving Up then Sideways or Zig-zag and formed a Crest	USC or UZC
Moving Up then Sideways or Zig-zag and formed a Valley	USV or UZV
Moving Down	D
Moving Down and formed a Valley	DV
Moving Down and formed a Valley then up or not up, but formed a Crest	DVC
Moving Down then Sideways or Zig-zag and formed a Valley	DSV or DZV
Moving Down then Sideways or Zig-zag and formed a Crest	DSC or DZC
Moving Sideways or Zig-zag and formed a Crest, etc.	SC or ZC SVC or ZVC
Moving Sideways or Zig-zag and formed a Valley, etc.	SV or ZV SCV or ZCV
Moving Sideways or Zig-zag then Down and formed a Valley	SDV or ZDV
Moving Sideways or Zig-zag then Up and formed a Crest	SUC or ZUC

Trend Symbols-Description:

- Up Mode (U): DJIA's bar chart shows that market is generally moving up.
- Down Mode (D): DJIA's bar chart shows that market is generally moving down.
- Sideways Mode (S): DJIA's bar chart shows that market is generally moving sideways without forming distinct crests and valleys, and **lacks definite direction**.
- Zig-zag Mode (Z): DJIA's bar chart shows that market is generally moving sideways in a zig-zig fashion forming **a narrow band of series of crests and valleys**.
- Crest (C): DJIA's bar chart shows that market has formed or is showing signs of forming a crest (fC) during its up, sideways or zig-zag modes. (Tip: A minimum of five days of daily bars should be considered in order to determine if a crest has formed.)
- Valley (V): DJIA's bar chart shows that market has formed or is showing signs of forming a valley (fV) during its down, sideways or zig-zag modes. (Tip: A minimum of five days of daily bars should be considered in order to determine if a valley has formed.)

(F) S6 Signals

1. General

During a period when both (I+N)/2% (see Table 205B) and the market are moving more or less in the same general direction, a buy signal is generated when (I+N)/2% falls below 45.00% and the conditions stated in 2, 3 or 4 below are met.

This signal may be classified into a short to medium-term signal category. Market turn-around can occur immediately or within few weeks after the signal.

For market data required for S6 signals, refer to Tables 201A, 201B, 205A, 205B and 206 in Appendix B.

For a sample log of S6 signals, refer to Table 102F in Appendix B.

2. S6A Buy Signal

A buy signal is generated when (I+N)/2% is below 30.00% for two weeks in a row and if the following conditions ar/e met:

(a) IO-index (IN, IN1 or IN2) or VI-index (Bbc) occurs or has recently occurred, **and when**
(b) (I+N)/2 and (I+N)/2% respectively changes by at least +500 and +0.25%, and also MC = 0/5, 1/4, 2/3 or 3/2

3. S6B Buy Signal

A buy signal is generated when (I+N)/2% is below 45.00% for three weeks in a row and if the following conditions are met:

(a) IO-index (IN, IN1 or IN2) or VI-index (Bbc) occurs or has recently occurred, **and when**
(b) (I+N)/2 and (I+N)/2% respectively changes by at least +500 and +0.25%, and also MC = 0/5, 1/4 or 2/3

4. S6C Buy Signal

A buy signal is generated when (I+N)/2% is below 45.00% and if the following conditions are met:

(a) (I+N)/2% establishes lows below 40.00% for two or more times at intervals without rising above the 45.00% mark, **and when**
(b) MC = 0/5, 1/4 or 2/3.

(G) S7 Signal

1. General

This signal is a speculative short-term buy signal. It is based on changes in the values of Nh% from week-to-week (see Table 205B in Appendix B) after it (Nh%) has declined below 45% *during a period when the market is declining or advancing, or moving sideways or zig-zag without market (DJIA) setting a 52-week new high within four weeks before the week of signal.*

For market data required for S7 signals, refer to Table 205B in Appendix B.
For a sample log of S7 signals, refer to Table 102G in Appendix B.

2. S7 Buy Signal

A buy signal is generated at the end of (n+2)nd week as shown in the following Table if the value $\frac{AC}{BB}$ is between 1.00 and 2.50.

Week Ending	Nh%	Notation	$\frac{AC}{BB}$	Signal
nth week	< 45.00% & Dn	= A		
(n+1) week	.....% Up	= B		
(n+2) week	(#) .....% Up	= C	> 1.00 and < 2.50	S7/BY

(#) This Nh% should be at least 15%.

(H) S8 Signals

It appears that DJIA generally fluctuates around its 5-week moving average (D5) line and forms a channel with upper and lower bound limits. Under certain conditions, the lower bound limit provides an opportunity for buying and the upper bound limit provides for selling.

Short-term buying may be considered when DJIA (Friday's closing price) is at 3.00% or more below its 5-week moving average line (i.e., D/D5 < or = 0.970) and short-term selling may be considered when DJIA (Friday's closing price) is at 3.00% or more above its 5-week moving average line (i.e., D/D5 > or =1.030) subject to the conditions listed in the Table below.

Conditions ⇒	(a)	(b)	(c)	(d)
	D/D5	Zone	MC	Status of D5 Line
S8/BY Signal	D/D5 < or = 0.970	A, A+, C1, or F3	MC = 0/5 or 1/4	Not Applicable
		B, B–, D3, or E1	Not Applicable	See Note (1)
S8/SL Signal	D/D5 > or = 1.030	A, A+, C1, or F3	Not Applicable	See Note (2)
		B, B–, D3, or E1	MC = 5/0 or 4/1	Not Applicable

Notes:

(1) 5-week moving average (D5) line of DJIA has formed a bottom, has been moving sideways or has **just** begun to move **up**.

(2) 5-week moving average (D5) line of DJIA has formed a top, has been moving sideways, or has **just** begun to move **down**.

S8 is a short-term buy or sell signal and should be considered highly speculative.
For market data required for S8 signals, refer to Tables 204A, 206 and 209 in Appendix B.
For a sample log of S8 signals, refer to Table 102H in Appendix B.

(I) S9 Signals

1. General

For a majority of the cases, this signal is good for one week or less unless other indicators and/or signals are appear to be developing to support the action generated by S9 signal. However, investors should remain alert during the week; supporting signals or indicators may or may not occur. It is a speculative (buy on Monday, sell on Friday) signal.

This signal may be used for trading options in accordance with Section 304 in Chapter 3. Since the signal is good for one week only, it is necessary to take a position before noon of the next trading day (Monday) and dissolve the position on or before the last trading day (Friday) of the week, regardless of profit or loss, unless other indicators or signals have occurred during the week to support the action initiated.

For market data required for S9 signals, refer to Tables 201A, 203 and 206 in Appendix B.

For a sample log of S9 signals, refer to Table 102I in Appendix B.

2. S9 Buy Signal

A buy signal is generated by a TICK index (Table 201A) when all of the following conditions (a) through (d) are met and the signal is validated per condition (e):

(a) MC = 0/5 (or may be 1/4)

(b) Pt/Fg portion (Table 203) of MC-indicator (Section 206) must meet one of the following conditions:

1. DJTA must establish a "O" on its Pt/Fg chart plus there must be at least two other indexes also establish "O" on their Pt/Fg charts (refer to Table 203).
2. At least four of the five indexes must establish "O" on their Pt/Fg charts (refer to Table 203).

(c) TK (10-day moving sum of NYSE closing Ticks) must be up for two days in a row within the last eight trading days. Refer to Column J in Table 201A.

(d) TK (Column J, Table 201A) must be up and MC (Table 206) must be 0/5 (or may be 1/4) at the end of the week.

The signal is valid only if the following condition (e) is also met:

(e) During the last few weeks if the market trend is down (D), or **within the last two weeks** if the market has formed a valley (V), or is showing signs of forming a valley (fV), as depicted by the DJIA bar chart in *The Wall Street Journal* (refer to *Table 102(E)2 on page 1-15*)
And
In order to eliminate the periods of abnormal behavior in the market, the maximum fluctuation in DJIA during the week of signal, expressed as the ratio of Friday's Close to the lowest DJIA determined using the daily closing prices for the week should be greater than 1.000 but less or equal to 1.025. See example below.
The ratio = Friday's close/Lowest DJIA = 9037.71/8803.80 = 1.027 based on the daily closing prices shown in the following Table for week ending 6/5/98:

Monday	Tuesday	Wednesday	Thursday	Friday
8922.37	8891.24	8803.80	8870.56	9037.71

3. S9 Sell Signal

A sell signal is generated by a TICK index (Table 201A) when all of the following conditions (a) through (d) are met and the signal is validated per condition (e):

(a) MC = 5/0 (or may be 4/1)

(b) Pt/Fg portion (Table 203) of MC-indicator (Section 206) must meet one of the following conditions:

1. DJTA must establish a "X" on its Pt/Fg chart plus there must be at least two other indexes also establish "X" on their Pt/Fg charts (refer to Table 203).
2. At least four of the five indexes must establish "X" on their Pt/Fg charts (refer to Table 203).

(c) TK (10-day moving sum of NYSE closing Ticks) must be down for two days in a row within the last eight trading days. Refer to Column J in Table 201A.

(d) TK (Column J, Table 201A) must be down and MC (Table 206) must be 5/0 (or may be 4/1) at the end of the week.

The signal is valid only if the following condition (e) is also met:

(e) During the last few weeks if the market trend is up (U), or **within the last two weeks** if the market has formed a crest (C) or is showing signs of forming a crest (fC), as depicted by the DJIA bar chart in *The Wall Street Journal* (refer to *Table 102(E)2 on page 1-15*)
And
In order to eliminate the periods of abnormal behavior in the market, the maximum fluctuation in DJIA during the week of signal, expressed as the ratio of Friday's Close to the highest DJIA determined using the daily closing prices for the week should be greater than 0.975 but less or equal to 1.000. See example below.
The ratio = Friday's close/Highest DJIA = 4430.56/4430.56 = 1.000 based on the daily closing prices shown in the following Table for week ending 5/12/95:

Monday	Tuesday	Wednesday	Thursday	Friday
4383.87	4390.78	4404.62	4411.19	4430.56

(J) SZ Signal

SZ is a speculative short-term buy signal. Market could rebound when all of the following conditions are met:

- Zone = A or A+
- MC = Almost flat i.e. MC = 0/5 or 1/4, or fluctuating within MC = 0/5 and 1/4 for several weeks.
- DJIA closes by the end of the week successively higher for three weeks while the MC level remains as defined above.

For Zone, MC and DJIA, refer to Table 211 in Appendix B. For a sample log of SZ signals, refer to Table 102J in Appendix B.

SECTION 103
LONG-TERM SIGNALS

(A) General

Three types of long-term signals are developed here. They are as follows:

1. L1, a long-term signal which is based on the comparison of 30-wk moving average lines of Dow Jones Industrial Average (DJIA), Dow Jones Transportation Average (DJTA), Value Line Geometric (VLG), S&P 500 (SPX) and S&P 100 (OEX) indexes with their Friday's (end of the week) closing prices and the average of daily closing prices for the week.
2. L2, a long-term signal which is based on the point and figure (Pt/Fg) chart of the Value Line Geometric index. Formation of certain Pt/Fg patterns reveals a buy or a sell condition.
3. L3, a long-term signal which is based on the Mutual Fund Index chart shown in *Investor's Business Daily* published by the Investor's Business Daily, Inc.

As L1, L2 or L3 signal occurs, it should be recorded in Tables 103B, 103C or 103D in Appendix B for ready reference. Summary of all long-term signals is shown in Table 103S in Appendix B.

(B) L1 Signals

1. General

In order to evaluate L1 buy and sell conditions, Friday's closing prices and the average of daily closing prices for the week should be compared with the 30-wk moving averages of DJIA, DJTA or VLG, and SPX (S&P 500) indexes.

Form 103A on page 1-45 may be used as a work sheet for this purpose. Refer to examples in Table 103A in Appendix B to learn how to compare the 30-wk moving averages with Friday's closing prices and the average of daily closing prices for the week in order to evaluate L1 buy or sell condition.

For a sample log of L1 signals, refer to Table 103B in Appendix B.

2. L1 Buy Signal

L1 Buy signal is generated when the following conditions (a) and (b) are met:

(a) The relations shown in the Table below for DJIA, DJTA or VLG, and SPX (S&P 500) indexes occur during the bear phase of the market.

Description	DJIA	DJTA or VLG (*)	SPX
Friday's (end of the week) Closing Price	> 30-wk MA	> 30-wk MA	> 30-wk MA
Average of Daily Closing Prices for the week	> 30-wk MA	> 30-wk MA	> 30-wk MA

(*) To be certain, any two of the three indexes (DJTA, VLG and OEX) should meet the condition in lieu of either DJTA or VLG.

(b) 5-wk, 10-wk and 40-wk moving averages of DJIA are rising or showing signs of forming a bottom, as revealed by examining the last 3 to 5 weeks' moving average readings.

3. L1 Sell Signal

L1 Sell signal is generated when the following condition (a) is met:

(a) The relations shown in the Table below for DJIA, DJTA or VLG, and SPX (S&P 500) indexes occur during the bull phase of the market.

Description	DJIA	DJTA or VLG (*)	SPX
Friday's (end of the week) Closing Price	< 30-wk MA	< 30-wk MA	< 30-wk MA
Average of Daily Closing Prices for the week	< 30-wk MA	< 30-wk MA	< 30-wk MA

(*) To be certain, any two of the three indexes (DJTA, VLG and OEX) should meet the condition in lieu of either DJTA or VLG.

(C) L2 Signals

1. General

Long-term buy and sell signals are developed using the point & figure (Pt/Fg) chart of Value Line Geometric (VLG) index (refer to Section 203 in Chapter 2 for details). It is found that certain patterns of point and figure charts are indicative of weakness or strength in the market.

For a sample log of L2 signals, refer to Table 103C in Appendix B.

2. L2 Buy Signal

The Point/Figure charts 1, 2, 3. 7, 8, 8A, 8B and 11 in *Figure 103(C) on page 1-23* are bullish and generate a buy signal if:

- The VLG index closes above its 10-wk moving average line on Friday of the week (i.e., end of the week). If the index is below the 10-wk moving average line, the signal becomes "Buy Wait" until it closes above the 10-wk moving average line, but before the X-column changes to O-column on the Pt/Fg chart, or

- The ratio of momentum (V/V30) this week to that of the previous week is 1.05 or greater. The momentum V/V30 is calculated in Table 204C in Appendix B.

Exception for Pt/Fg chart #11:

The above requirements may be waived for Pt/Fg #11 buy condition if both the bottom and top slopes on the Pt/Fg chart #11 are up.

A buy signal generated by Pt/Fg chart #11 is generally invalid (false) if it occurs adjacent (i.e., within 8 columns of Pt/Fg chart) to a 52-week new high X-column on the Pt/Fg chart with a top slope generally down. See Pt/Fg chart #E in *Figure 103(C) on page 1-23.*

Comment:

Buy signals during the period of high volatility in the market (which is normally peculiar during the topping process of the bull market) **are generally false if there exists a bearish divergence between DJIA index and the advance-decline cumulative (Ics) line**. For details, refer to M3-Index in Section 104(B).

3. L2 Sell Signal

The Point/Figure charts 4, 5, 6, 9, 10, 10A, 10B and 12 in *Figure 103(C) on page 1-23* are bearish and generate a sell signal if:

- The VLG index closes below its 10-wk moving average line on Friday of the week (i.e., end of the week). If the index is above the 10-wk moving average line, the signal becomes "Sell Wait" until it closes below the 10-wk moving average line, but before the O-column changes to X-column on the Pt/Fg chart, **or**
- The ratio of momentum (V/V30) this week to that of the previous week is 0.95 or less. The momentum V/V30 is calculated in Table 204C in Appendix B.

Exception for Pt/Fg chart #12:

The above requirements may be waived for Pt/Fg #12 sell condition if both the bottom and top slopes on the Pt/Fg chart #12 are down.

A sell signal generated by Pt/Fg chart #12 is generally invalid (false) if it occurs adjacent (i.e., within 8 columns of Pt/Fg chart) to a 52-week new low O-column on the Pt/Fg chart with a bottom slope generally up.

Comment:

Sell signals during the period of high volatility in the market (which is normally peculiar during the bottoming process of the bear market) **are generally false if there exists a bullish divergence between DJIA index and the advance-decline cumulative (Ics) line.** For details, refer to M3-Index in Section 104(B).

4. Caution

A great deal of judgment (experience) would be necessary in order to interpret certain complex formation of Pt/Fg patterns. If in doubt, do nothing. Experience is a great teacher.

FIGURE 103(C)—PT/FG CHARTS

Legend: "B" denotes buy signal and "S" denotes sell signal on Pt/Fg charts shown below.
Note: For interpretation of the Pt/Fg charts, refer to Table 103(C) on page 1-27.

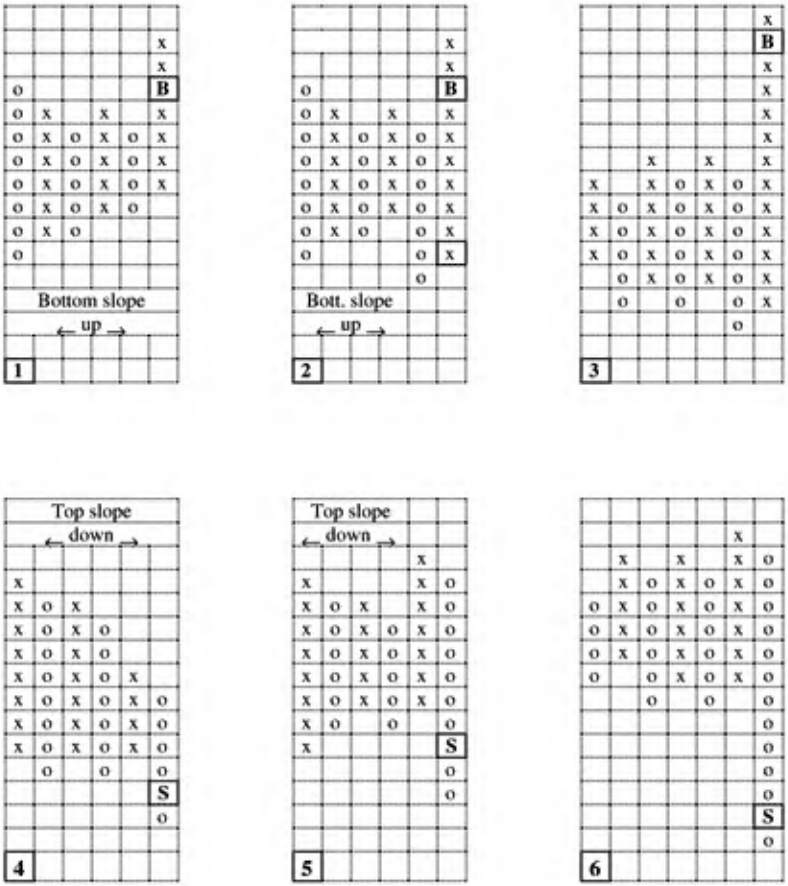
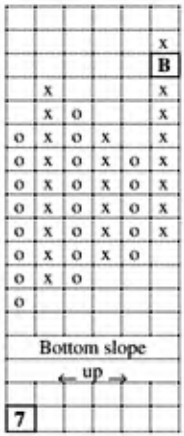
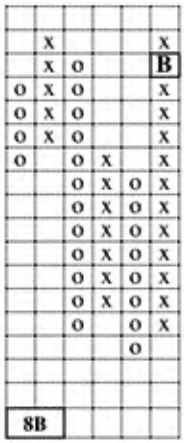


Figure 103(C)—Pt/Fg Charts (continued)

Figure 103(C)—Pt/Fg Charts (continued)





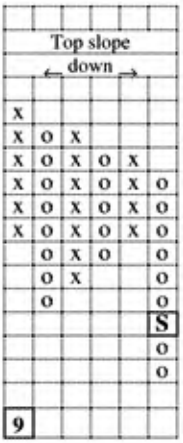


Figure 103(C)—Pt/Fg Charts (continued)

Figure 103(C)—Pt/Fg Charts (continued)

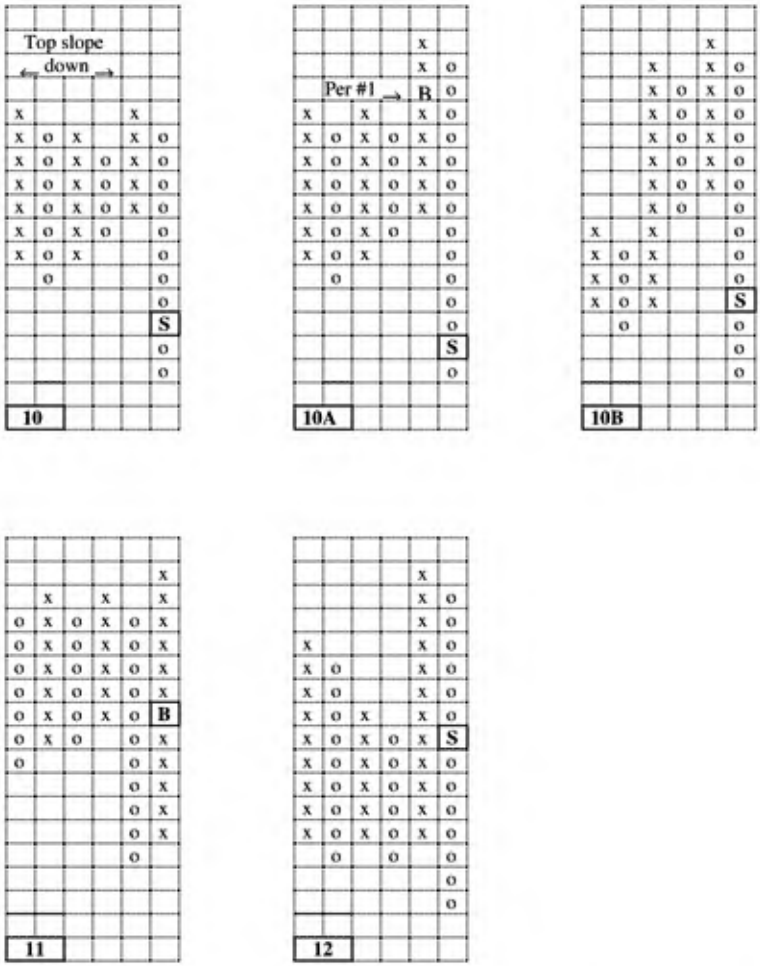
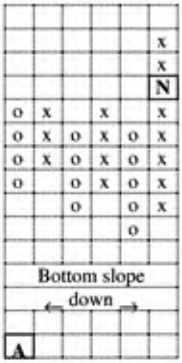


Figure 103(C)—Pt/Fg Charts (continued)

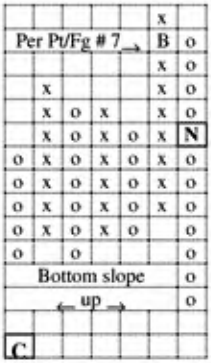
Figure 103(C)—Pt/Fg Charts (continued)

The following are few examples of Pt/Fg charts which are considered neither bullish nor bearish, and therefore, generate no signals:

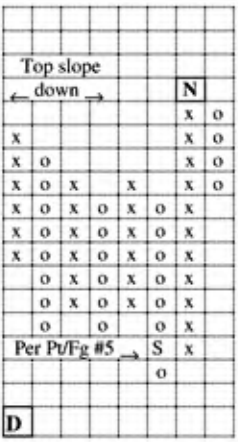


N = Pt/Fg #2
Buy/CNM

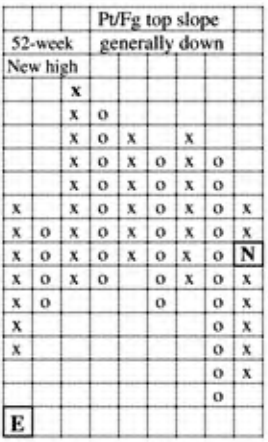
N = Pt/Fg #10
Sell/CNM



N = Pt/Fg #12
Sell/CNM



N = Pt/Fg #3
Buy/CNM



Pt/Fg #11 Buy Cond. not met per Section 103(C)2

N= Pt/Fg #11
Buy/CNM

Legend: "CNM" denotes Pt/Fg (buy or sell) Condition Not Met.

Table 103(C)—Interpretation of Pt/Fg Charts

{Reference is made to Fig. 103(C)}

Chart #	Description of Pt/Fg Charts (Refer to notes 1 and 2 below)				Signal
	Status of Last column	Status of Previous Column(s)	Last 6 columns (a) Configuration at Bottom	Top	
1	TTB	Without DB, DBB, TB or TBB	Up	----	Buy
2	TTB	With DB or DBB	Up	----	Buy
3	TTB > 4	With TB or TBB	NA	----	Buy
4	TBB	Without DT, DTB, TT or TTB	----	Down	Sell
5	TBB	With DT or DTB	----	Down	Sell
6	TBB > 4	With TT or TTB	----	NA	Sell
7	DTB > 2	Without DB, DBB, TB or TBB	Up	----	Buy
8	DTB > 3	With DB or DBB	Up	----	Buy
8A	DTB > 4	With TB or TBB	NA	----	Buy
8B	DTB > 3	With DB or DBB by no more than 2 blocks	(b)	----	Buy
9	DBB > 2	Without DT, DTB, TT or TTB	----	Down	Sell
10	DBB > 3	With DT or DTB	----	Down	Sell
10A	DBB > 4	With TT or TTB	----	NA	Sell
10B	DBB > 3	With DT or DTB by no more than 2 blocks	----	(c)	Sell
11	"X" column moves up more than 50% of the last "O" column. This last "O" column should extend downward by 3 or more O's below the previous "X" column and meets the condition stated in FtNt. (d).				Buy
12	"O" column moves down more than 50% of the last "X" column. This last "X" column should extend upward by 3 or more X's above the previous "O" column and meets the condition stated in FtNt. (d).				Sell

Legend: DB = Double Bottom; DT = Double Top; TT = Triple Top; TB = Triple Bottom; DBB = Double Bottom Breakout; DTB = Double Top Breakout; TTB= Triple Top Breakout; TBB = Triple Bottom Breakout; NA = Not Applicable.

Note 1: Charts that do not match with those shown in this Table should be considered to be neither bullish nor bearish.

Note 2: Select only the first occurrence of a buy or a sell signal. For example, after the first buy signal, Pt/Fg chart can generate buy signal after buy signal as the market advances higher and higher. Therefore, after the first buy signal, watch only for the sell condition to occur, and vice versa.

FtNts.:

(a) For determining bottom and top slopes of Pt/Fg charts: Use only the last six columns except exclude the last two columns for Pt/Fg charts 2, 5, 8 and 10.

(b) Slope requirements are not applicable if a valley-like bottom as shown on Pt/Fg chart 8B is formed by only four columns.

(c) Slope requirements are not applicable if a crest-like top as shown on Pt/Fg chart 10B is formed by only four columns.

(d) The sum x + y should be greater than 15 in which x = number of O's in the last "O" column (Pt/Fg #11) or number of X's in the last "X" column (Pt/Fg #12) and y = number of O's below the previous "X" column (Pt/Fg #11) or number of X's above the previous "O" column (Pt/Fg #12). For examples, x + y = 11 + 6 = 17 in Pt/Fg #11 and x + y = 12 + 7 = 19 in Pt/Fg #12 shown on page 125.

(D) L3 Signals

1. General

L3 buy and sell signals are based on the status of the IBD (Investor's Business Daily) mutual fund index in relation to its 200-day (40-week) moving average and the condition of its 50-day (10-week) moving average. For Mutual Fund Index chart, refer to *Investor's Business Daily*.

For a sample log of L3 signals, refer to Table 103D in Appendix B.

2. L3 Buy Signal

L3 Buy signal conditions exist when 50-day moving average of the Mutual Fund Index is showing signs of forming a bottom (fBm) or has turned up and the Index closes above its 200-day moving average. Refer to Mutual Fund Index chart shown in the Mutual Funds Section of *Investor's Business Daily*.

Comment:

Buy signals during the period of high volatility in the market (which is usually peculiar during the topping process of the bull market) **are generally false if there exists a bearish divergence between DJIA index and the advance-decline cumulative (Ics) line**. For details, refer to M3-Index in Section 104(B).

3. L3 Sell Signal

L3 Sell signal conditions exist when 50-day moving average of the Mutual Fund Index is showing signs of forming a top (fTp) or has turned down and the Index closes below its 200-day moving average. Refer to Mutual Fund Index chart shown in the Mutual Funds Section of *Investor's Business daily*.

Comment:

Sell signals during the period of high volatility in the market (which is usually peculiar during the bottoming process of the bear market) **are generally false if there exists a bullish divergence between DJIA index and the advance-decline cumulative (Ics) line**. For details, refer to M3-Index in Section 104(B).

(E) Use of Other Indexes

1. NASDAQ Composite Index and Lipper Growth Fund Index

A limited study reveals that the use of these indexes, alone or in conjunction with other indexes, does not generate signals any timelier than those indexes used in generating "L" signals.

2. Dow Jones 65 Composite

This index has been found to be useful when applied in accordance with Section 302 in Chapter 3. In that, it might indicate whether the pull back in the DJIA during the bull phase of the market is a correction or it is the end of the bull market. Conversely it might also indicate if the rally during the bear phase is the end of the bear market.

(F) Interest Sensitive (IS) Indexes

1. General

During a period when the market is sensitive to interest rate changes, a limited study of the moving averages of the following indicators may trigger a buy or a sell signal:

- The DJ-Utility Average Index
- The 13-week T-bill Coupon Yield
- The 3-year Treasury Note Yield

The DJ-Utility Average Index is listed in *Barron's* under Market Laboratory-Stocks Section. The 13-week T-bill Coupon and the 3-year Treasury Note yields are listed in *Barron's* under Section titled "Money Rates".

The results of this study are summarized in sub-section 5 below. From this study, it is concluded that the "L" buy and sell signals discussed above are generally sufficient for making a long-term buy and sell decisions and they govern over these signals. The study is included here for information only.

2. The DJ-Utility Average Index: IS1 Signals

(a) IS1 Buy Signal

A buy signal is generated when one of the following conditions is met:

1. The DJ-Utility Index closes above its 30-wk moving average (MA) on a weekly basis by at least 1.00 point and if
   - The DJ-Utility Index > 10-wk MA > 20-wk MA
2. The DJ-Utility Index closes above its 10-wk and 50-wk moving averages (MA) on a weekly basis.

(b) IS1 Sell Signal

A sell signal is generated when one of the following conditions is met:

1. The DJ-Utility Index closes below its 30-wk moving average (MA) on a weekly basis by at least 1.00 point and if
   - The DJ-Utility Index < 10-wk MA < 20-wk MA
2. The DJ-Utility Index closes below its 10-wk and 50-wk moving averages (MA) on a weekly basis.

For examples of IS1 sell signals, refer to Table 103(F)2 below.

Table 103(F)2—Example of IS1 Sell Signals

WkEd	DJUtilty Index	10-wk MA	20-wk MA	30-wk MA	50-wk MA	Remarks	IS1 Signals
2/21/97	229.74	234.04	231.85	226.68	220.62		
2/28	227.29	233.27	232.14	227.19	220.93		
3/7	226.66	232.34	232.25	227.69	221.17		
3/14	224.22	231.62	232.29	227.91	221.40	Sell Condition 1 met.	Sell
3/21	221.21	230.11	232.03	228.09	221.56	Sell Condition 2 met.	Sell Repeat
3/28	219.12	228.09	231.25	228.25	221.79	Prime Rate +1/4 to 8.50	
4/4	214.85	225.82	230.24	228.28	221.94		

3. The 13-week T-bill Coupon Yield: IS2 Buy Signal

A 13-week T-bill Coupon Yield generates a buy signal in accordance with the following criteria. Refer to *Table 103(F)3/4 on page 1-46* for column information.

Column C = 13-week T-bill Yield

Column D = 3-week simple moving average of values in column C (= 3-wk smaC)
For example, $Dn+2 = (Cn + Cn+1 + Cn+2) \div 3$

Column E = Special modified moving average of values in column D (= Special mmaD)
For example, $En = 0.25 \times Dn + 0.75 \times En-1$

Column F : Ratio D/E—It is the ratio of Column D to Column E.

Column G : **After an IS3 sell signal:**-If the ratio D/E in Column F begins to fall below 1.000 for 3 weeks in a row **after it has been over 1.000 for at least 4 consecutive weeks**, an IS2 buy signal is generated and it is recorded in Column G.

4. The 3-Year Treasury Note Yield: IS3 Sell Signal

A 3-year Treasury Note Yield generates a sell signal in accordance with the following criteria. Refer to *Table 103(F)3/4 on page 1-46* for column information.

Column I = 3-year Treasury Note yield

Column J = 3-week simple moving average of values in column I (= 3-wk smaI)
For example, $Jn+2 = (In + In+1 + In+2) \div 3$

Column K = Special modified moving average of values in column J (= Special mmaJ)
For example, $Kn = 0.286 \times Jn + 0.714 \times Kn-1$

Column L : Ratio K—It is the ratio of this week's K to that 12 weeks earlier.
e. g., $Kn+12 / Kn$

Column M : **After an IS2 buy signal:**-If the ratio K in Column L begins to rise above 1.000 for 4 weeks in a row **after it has been below 1.000 for at least 3 consecutive weeks**, an IS3 sell signal is generated and it is recorded in Column M.

Column N : Buy signals generated by IS2 from Column G and sell signals generated by IS3 in Column M are both listed in Column N for ready reference.

5. Summary of Buy and Sell Signals

Buy and sell signals generated by the above criteria are summarized in (a), (b) and (c) below for study and reference only.

(a) Summary of IS1 Signals

Suggested Action	IS1 Signals		Signal Conditions	Remarks
	WkEd	DJIA		
Sell	4/5/96	5682.88	1	Near the top, but later DJIA set new high of 5778.44 on 5/22/96.
Buy	8/16/96	5689.45	1 & 2	
Sell	3/14/97	6935.46	1	Near the top of he market.
Buy	5/9/97	7169.53	2	
Sell	9/4/98	7640.25	1 & 2	Signal too late.

(b) Summary of IS2 & IS3 Signals

Suggested Action	Signal Type	WkEd	DJIA	Remarks
Sell	IS3	4/26/96	5567.99	Premature signal. DJIA new high of 5778.44 on 5/22/96.
Buy	IS2	8/30/96	5616.21	
Sell	IS3	3/7/97	7000.89	Near the top of the market.
Buy	IS2	5/16/97	7194.67	Late buy, but OK.
Sell	IS3	5/22/98	9144.44	

(c) Combined Summary of IS1, IS2, IS3 & L Signals

Week End. (Date)	Zone	MC	Signals			DJIA	How occurred?			Remarks
			IS1	IS2	IS3		On the way	From	By ? Points	
4/5/96	A+	2/3	Sell			5683	Near the top.			
4/26	D1	3/2			Sell	5568	Dn	5690	122	
6/28			L2 sell signal			5648				From Table 601, App. B
8/16/96			L2 buy signal			5689				From Table 601, App. B
8/16	D1	4/1	Buy			5689	Up	5347	342	
8/30	D1	3/2		Buy		5616	Up	5347	309	
3/7/97	A+	3/2			Sell	7001	Near the top.			
(3/12)			L3 sell signal			7039				From Table 601, App. B
3/14	A+	2/3	Sell			6935	Dn	7001	66	
5/2/97			L2 buy signal			7071				From Table 601, App. B
5/9	A+	4/1	Buy			7169	Up	6391	778	
5/16	A+	3/2		Buy		7195	Up	6391	804	
5/15/98			L2 sell signal			9096				From Table 601, App. B
5/22	E3	0/5			Sell	9114	Zig-zag near the top			
9/4	E1	0/5	Sell			7640	Dn	9337	1697	Signal too late

SECTION 104
MARKET MOOD INDICATORS

(A) Overview

1. General

When a majority of the technical indicators are consistent with one another, the market's current trend will likely to continue. However, when they rife with divergence, the market's *short-term* direction may be reversing.

When the technical indicators are not consistent with one another—it is termed as divergence. Divergence occurs in several ways. Examples are:

- Cumulative advance-decline line lags with the market advancing or market making a new high. A chart of NYSE cumulative daily breadth (advance-decline issues) vs. DJIA is shown in *Barron's*.
- Market Condition (MC) indicator lags with the market advancing or market making a new high.
- Point & Figure (Pt/Fg) charts of DJTA, S&P 500 index, Value Line Geometric index and S&P 100 (OEX) index are inconsistent with the Pt/Fg chart of DJIA or with the DJIA making a new high or a new low.
- Number of advancing issues and/or new highs do not expand with the market advancing or market making a new high.

2. What Could Happen?

(a) DJIA after several attempts may lose its strength and falls in line with the other indicators or the indicators eventually will catch-up with the DJIA—thus wiping out the divergence.

The process could last for several weeks. Therefore, when divergence occurs, do not expect the market to change its trend immediately. One of the many examples is May-July 1990.

(b) As long as the new highs are expanding and the new lows are shrinking, one can generally expect the market to keep advancing.

If the market is advancing and the new highs are shrinking or the new lows are expanding, one can generally expect the market to reverse its trend.

Again the process could last several weeks. Therefore, it is not prudent to commit funds unless other signals suggest to do so.

(c) Some other widely followed indicators, such as price-to-earning (PE) ratio, dividend yield, and market-to-book value ratio, by historical standards, may indicate whether the market is over-valued (over-bought) or under-valued (over-sold). Even these conditions can prevail for sometime, and it is likely that the market could eventually mark time and wipe out these conditions without market going up or down appreciably.

The terms over-valued or under-valued are relative to the time period. That is to say what was considered over-valued or under-valued in the past may not necessarily be the same today. It

depends on who is interpreting the condition of the overall market. The market is the final authority to interpret its own condition. However, historic data are useful to gauge the market condition when interpreting the terms over-valued and under-valued in context with the time.

Therefore, the market mood indicators are developed to gauge the immediate condition of the overall market. The market mood indicators could be bearish or bullish depending on the changes in their status from week-to-week and the direction of the overall market.

Direction: The direction of the overall market is determined by the direction set by a majority of the indexes, viz.: DJIA, DJTA, S&P 500, VLG and OEX from week-to-week (i.e., from the previous Friday's to this Friday's) closing prices.

The market mood indicators are generally applicable to short-term to medium-term buy and sell signals. However, they will not apply to S3 and S9 buy and sell signals. They serve as an useful tool when trading options {Section 304(B)2, Chapter 3.}

(B) Market Mood Indicators

1. M1-Index

M1-Index is determined based on the changes in the values of (1) Vu%, (2) Ia%, (3) Nh%, (4) WIa% and (5) WNh% from week-to-week whether they are positive or negative. For Vu%, Ia% and Nh%, refer to Table 205B; for WIa% and WNh%, refer to Table 200 or 211 in Appendix B.

If changes in the majority of the above values from weak-to-weak are against the direction of the overall market, it could mean that the M1-index may or may not be consistent (i.e., bearish or bullish) with the buy or sell signal based on the Table below.

Status of M1-Index	**&** if the market direction is	**and** the M1-Index coincides with	**then** the M1-Index should be considered as
Negative	Up	a sht-term buy signal	bearish
Positive	Down	a sht-term sell signal	bullish
Negative	Up	a sht-term sell signal	bearish
Positive	Down	a sht-term buy signal	bullish
Negative	Down	———	normal
Positive	Up	———	normal

The examples below illustrate how to determine and interpret the M1-Index in context with a buy or a sell signal.

Example 1

	Direction from wk-to-wk						Components of M1-Index				
WkEd	D	T	S	V	O	Signal	Vu%	Ia%	Nh%	WIa%	WNh%
12/9/94	----	----	----	----	----		38.46	38.04	4.34	27.06	6.53
12/16/94	Up	Up	Up	Up	Up	S5/BY	64.96	59.25	8.97	67.82	8.02
	Majority is Up						Up	Up	Up	Up	Up
	Overall market is up					Buy	M1 = (All five ups) = +5				
Market Condition: Normal.											

Example 2

	Direction from wk-to-wk						Components of M1-Index				
WkEd	D	T	S	V	O	Signal	Vu%	Ia%	Nh%	WIa%	WNh%
12/16/94	----	----	----	----	----		64.96	59.25	8.97	67.82	8.02
12/23/94	Up	Up	Up	Up	Dn	S7/BY	50.19	51.92	23.63	54.39	21.77
	Majority is Up						Down	Down	Up	Down	Up
	Overall market is up					Buy	M1 = (2 Ups – 3 Downs) = –1				
Market Condition: Bearish (refer to Remark #94/12 in Section 213, Chapter 2)											

Example 3

	Direction from wk-to-wk						Components of M1-Index				
WkEd	D	T	S	V	O	Signal	Vu%	Ia%	Nh%	WIa%	WNh%
10/13/95	----	----	----	----	----		53.81	51.79	73.91	55.96	73.73
10/20/95	Up	Dn	Up	Dn	Up	S1/BY S3/SL	46.65	47.53	78.24	49.85	78.45
	Majority is Up					Buy or	Down	Down	Up	Down	Up
	Overall market is up					Sell *	M1 = (2 Ups – 3 Downs) = –1				
Market Condition: Bearish for the buy signal, but bullish for the sell signal * Refer to Case Study #95/B in Chpter 7											

Example 4

	Direction from wk-to-wk						Components of M1-Index				
WkEd	D	T	S	V	O	Signal	Vu%	Ia%	Nh%	WIa%	WNh%
12/22/95	----	----	----	----	----		51.71	51.47	80.68	53.50	77.53
12/29/95	Up	Up	Up	Up	Up	S1/BY	58.68	57.77	58.19	65.34	83.82
	Majority is Up						Up	Up	Up	Up	Up
	Overall market is up					Buy	M1 = (All five ups) = +5				
Market Condition: Normal.											

Example 5

	Direction from wk-to-wk						Components of M1-Index				
WkEd	D	T	S	V	O	Signal	Vu%	Ia%	Nh%	WIa%	WNh%
6/14/96	----	----	----	----	----		47.63	46.14	64.91	43.12	61.31
6/21/96	Up	Up	Up	Dn	Up	S5/BY	50.34	46.04	51.16	44.28	53.53
	Majority is Up						UP	Down	Down	UP	Down
	Up					Buy	M1 = (2 Ups – 3 Downs) = –1				
Market Condition: Bearish (refer to Remark #96/6 in Section 213, Chapter 2)											

2. M2-Index (OB/OS Condition)

M2 = 20-day moving sum of Ia-d. It is obtained by adding two 10-day moving sums, ten days apart. Refer to column E in Table 201A for 10-day moving sums.

If M2 is greater than +4000, the market condition may be considered overbought (OB) which means the index is bearish.

If M2 is lesser than–4000, the market condition may be considered oversold (OS) which means the index is bullish.

If it supports the signal, it generally indicates strength in the signal; however, if it is against the signal, it might suggest to hold off the proposed action generated by the signal.

If there is no signal, it is likely that the market will wipe out the OS or OB condition by moving sideways. **This indicator alone does not suggest any action whether to buy, to sell, or to close position.**

3. M3-Index (Cumulative sum Ics)

It measures the degree of participation of the overall market in relation to DJIA movement. For cumulative sum Ics, refer to Table 205A.

Note that cumulative sum Ics is relative to time because the cumulative sum is dependent on the point of time from when we begin to collect the data. Therefore, only after over a period of time, its highs and lows might have some significance in correlating market tops and bottoms. The comparison of the *general trend of the Ics line with that of the DJIA* over the same period of time could indicate the ongoing condition of the overall market.

The general trend (i.e., disregarding short ups and downs) of the Ics line could be up, down, sideways, zig-zag, or forming a crest or a valley. It reveals weakness or strength in the overall market based on the general trend of the cumulative sum (Ics) line relative to the market (i.e., DJIA based on weekly closing prices) over the last few weeks as follows:

- If the Ics line is advancing and the market (DJIA) is declining or moving sideways, it denotes internal strength which is then termed as bullish divergence.
- If the Ics line is declining and the market (DJIA) is advancing or is moving sideways, it denotes internal weakness which is then termed as bearish divergence.
- If the Ics line and the market (DJIA) are moving in the same direction, it denotes normal market behavior.

Because by nature the market is volatile and unpredictable, sometimes it becomes very difficult to decide on the direction and to interpret whether or not the Ics line is consistent or inconsistent with the Dow Jones Industrial averages based on weekly closing prices. In some instances, use of (I+N)/2% line in Table 205B has been found more meaningful than the Ics line.

The moving average line of (I+N)/2% is not relative to time like the cumulative sum (Ics) discussed above because the shape and size of the moving average line remains unchanged regardless of the point of time from when we begin to collect the data. Therefore, its highs and lows have some significance in correlating market tops or bottoms when evaluating the strength or weakness in the overall market in context with the buy or sell signals. As a general rule, higher highs or higher lows indicate strength and lower lows or lower highs indicate weakness.

For example, during April-July of 1998, while the DJIA was making new highs after a new high and forming a top, cumulative sum Ics (Table 205A) and the moving average lines (I+N)/2 and (I+N)/2% were generally on a declining trend and remained below their recent highs. This bearish divergence triggered the market fall began in July of 1998 soon after the DJIA made a 52-week new high of 9337.97 on July 17, 1998.

4. M4-Index (DJIA vs. MA)

For the week under consideration, check if DJIA has crossed downward or upward one or more of its moving average lines, namely 10-, 20-, 30-, and 40-wk moving averages (refer to Table 204A). Crossing upward means the index is bullish; crossing downward means the index is bearish.

It should be checked on a daily basis if and when appropriate.

5. M5-Index (DJIA MA Trend)

A change in the trend of DJIA moving averages (refer to Table 204A) is indicative of the market's present weakness or strength. For examples,

- If D10 > D20 > D30 > D40 and if all are moving up, it means that bullish behavior is on-going.
- If D10 < D20 < D30 < D40 and if all are moving down, it means that bearish behavior is on-going.

What is important to know is whether or not any change in the trend is in progress within the on-going bullish or bearish behavior. There are seven components, viz.: four components are the direction (up or down) of the four moving average lines, and the other three components are the comparison of their values among each other whether they are > or < as illustrated in the above examples.

Change in any one of the seven components from previous week to week under consideration could mean that change in the behavior of the market may be in progress. If the week under consideration resulted into a cumulative (i.e., including the changes occurred previously) change of three or more components, it could mean change in the behavior of the market from bullish to bearish or from bearish to bullish may be in progress.

6. M6-Index (Pt/Fg Trend Reversal)

Check if the Pt/Fg trend (refer to Table 206) has reversed for the week under consideration. If it has reversed from "O" to "X" would mean the index is bullish and "X" to "O" would mean the index is bearish.

Similar interpretation may be in order if a column on PT/Fg chart changes from "O" to "X" or from "X" to "O" (refer to Section 203). It should be reviewed daily if and when warranted.

7. M7-Index (New highs or New lows)

Check if DJIA, DJTA, SPX, VLG or OEX made a 52-week new high or new low. New high means the index is bullish; new low means the index is bearish. Refer to Tables 200 or 211 for 52-week new highs or new lows.

It should be reviewed daily if and when appropriate.

8. M8-Index (Market Condition Indicator Change)

If market condition (MC) indicator rises, it should be considered as a bullish index; if it falls, consider it as a bearish index. The index is neutral if it neither rises nor falls. Refer to Table 206 for Market Condition (MC) Indicator.

9. M9-Index (Market Momentum Trend-Table 204A)

If the general trend of the momentum (see "Mtm = D/D30" in Table 204A) during the last five or so weeks is up, it could indicate bullish market condition regardless of the direction of the market. If the general trend of the momentum is sideways or stagnant, it could mean indecisiveness in the market's behavior. If the rate of momentum (i.e., the ratio of this week's Mtm to previous week's Mtm) is 1.05 or greater, it indicates strength in the market, and it indicates weakness if it is less than 0.95.

(C) Summary

The following Table briefly summarizes market mood indicators for ready reference; they can be monitored, on a daily or weekly basis. They can provide valuable information about the market condition when trading index options (refer to Section 304 in Chapter 3).

Index Brief Description M1 Based on changes in Vu%, Ia%, Nh%, WIa% & WNh% from wk-to-wk M2 OB/OS Condition based on 20-day moving sum of Ia-d M3 Cumulative sum of Ia-d (Ics) vs. DJIA on a weekly basis M4 Has DJIA crossed its moving average lines? M5 Change in the trend among Moving Averages of DJIA M6 Pt/Fg Trend Reversal M7 New highs or New lows durimg the week of signal M8 Change in Market Condition (MC) Indicator M9 Market Momentum (Mtm) Trend

Index	Brief Description
M1	Based on changes in Vu%, Ia%, Nh%, WIa% & WNh% from wk-to-wk
M2	OB/OS Condition based on 20-day moving sum of Ia-d
M3	Cumulative sum of Ia-d (Ics) vs. DJIA on a weekly basis
M4	Has DJIA crossed its moving average lines?
M5	Change in the trend among Moving Averages of DJIA
M6	Pt/Fg Trend Reversal
M7	New highs or New lows durimg the week of signal
M8	Change in Market Condition (MC) Indicator
M9	Market Momentum (Mtm) Trend

SECTION 105
SAFETY GUARDS

(A) General

It should be understood that signals, buy or sell, will not be perfect all of the time; sometimes they will be wrong for many possible reasons. Therefore, to prevent getting into an unprofitable trade or to identify potential unprofitable trades quickly, two types of safety guards are devised. They are:

Exceptions: Conditions described under each exception category determine whether the signal is valid or invalid.

Warnings: If a trade is in place because of a valid buy signal, but if it is not likely going to be profitable, system may generate a warning signal within a week or so, alerting investors to close the position.

In most cases, the warning signal acts like a safety switch—saves from losses. Sometimes the warning signal may be false. However, it is always a good practice to watch for their occurrence after the trade is in place.

Although these safety guards are not fallible, strictly following them will help to minimize losses. Missing profitable trades occasionally should be considered acceptable. The key is to avoid losses most of the times.

Application of exceptions and warnings to buy and sell signals is summarized in *Table 105(A)1 on page 1-47* for ready reference.

(B) Exceptions

1. Exception EA

EA1: S1 buy and sell signals are not valid if the distance between IO-index and VI-index (confirmed), or VI-index (confirmed) and IO-index is more than 41 trading days.

EA2: a. S1 and S2 sell signals are not valid during the first 10 weeks in zone A and also only in the first occurrence of **zone A** in a series like **A**, A+, A, A+, A, etc.

b. S1 and S2 sell signals are not valid during the first 10 weeks in zone A+. They are also not valid in the first or the second occurrence of **zone A+** in a series like A, **A+**, A, **A+**, A, A+, A, etc.

EA3: S3 sell signals are not valid during the first 10 weeks in zone A+, and in the first or the second occurrence of **zone A+** in a series like A, **A+**, A, **A+**, A, A+, A, etc.

2. Exception EB

Unusual sharp declines in the market create panic behavior among investors. When sharp declines in the market occur, there is no way to predict the future course of the market. Therefore, it is advisable to take time off and refrain from trading, specially options, for at least few weeks.

However, under special conditions during the sharp decline weeks, this exception can generate a buying opportunity rather than a selling consideration. If such conditions develop, the decline in the market should be classified as a major correction in an ongoing bull market.

A decline in the market is considered as "sharp-decline" when all of the following conditions exist during the last ten (10) trading days:

(a) Single day drop in DJIA (or SPX) must be greater than 1.75%, **or**

Two-consecutive-day drop is greater than 3.00% with a single day drop no less than 1.50%.

(b) Change in DJIA (or SPX) daily closing prices between the highest and the lowest during the last five (5) trading days must be greater than 2.50%.

(c) Change in DJIA (or SPX) daily closing prices between the highest and the lowest during the last ten (10) trading days must be greater than 3.25%.

A log of sharp-decline (EB) weeks is shown in the Table below.

Log of Sharp—Decline Weeks

Yr.	WkEd	Zone	MC	Yr.	WkEd	Zone	MC	Yr.	WkEd	Zone	MC
86	4/4	A+	2/3	90	1/26	D1	0/5	97	4/11	A+	0/5
86	9/12	C1	0/5		8/3	B	0/5		8/15	A+	1/4
87	10/9	C1	4/1		8/10	B	0/5		10/24	C1	0/5
87	10/16	C1	0/5		8/17	B	0/5	97	10/31	C1	0/5
87	12/4	B	0/5		8/24	B	0/5	98	1/9	D2	1/4
88	1/1	B	4/1	90	10/12	B	2/3		6/19	E3	0/5
	1/22	B	3/2	91	11/15	C1	1/4		7/24	E3	0/5
	3/25	B	3/2	94	4/1	C1	0/5		8/7	E3	0/5
	4/15	B	3/2	94	11/25	D3	0/5		8/28	E3	0/5
88	8/12	D3	0/5	96	7/12	D1	0/5	98	9/4	E1	0/5
89	10/13	A+	1/4	96	7/19	D1	0/5	99	5/28	A+	1/4
90	1/12	C1	2/3	97	4/4	A+	0/5		7/30	A+	0/5

This exception will serve as a guide when sharp declines in the market occur.

EB1:

This exception is applicable to sell signals as indicated below.

a. Sell signals, either short-term or long-term, are valid signals and must be considered seriously if they occur during the week of sharp decline in the market.
   All call option positions must be closed immediately; sell signals are not suitable for trading put options.

b. Short-term sell signals (which occur after a sharp-decline week) are only valid if they occur after a technical rally in the market.

c. Long-term sell signals (which occur after a sharp-decline week) are valid sell signals.

EB2:

This exception is applicable to buy signals as indicated below.

a. Short-term buy (**except S3 buy**) and long-term buy signals should be ignored if they occur during the week of sharp decline.
b. Short-term buy signals (**except S3 and S5 buy signals**) which occur after the sharp decline week (EB-wk) are only valid or will become valid if and when one of the following conditions exist:
   i. A valley (second) higher than the valley (first) at or near the EB-wk is formed, and the DJIA on a closing basis exceeds those closed after the EB-wk. (Examples of this condition: 2/12/88-Table 102A; 3/2/90-Tables 102A & F; 12/23/94-Table 102G).
   ii. A third valley higher than the second valley is formed and the DJIA on a closing basis exceeds those closed between the second and the third valleys. Note that the third valley may be lower than the first valley formed at or near the EB-wk. (Examples of this condition: 9/9/88-Tables 102B & J; 12/20/91-Table 102D; 12/27/91-Table 102G.)
   iii. A third valley higher than the first valley is formed. Note that the second valley may be higher or lower than the third valley. (Examples of this condition: 11/10/89-Table 102I; 11/10/89-Table 102G; 11/17/89-Table 102J; 11/9/90-Tables 102E & F; 12/20/91-Table 102D.)
   iv. DJIA closes above those during the week just before the sharp-decline week (EB-wk) in the market **first began**. When there are side by side sharp decline weeks, consider the closing prices of DJIA during the week prior to the first sharp decline week. (Examples of this condition: 5/2/97-Table 102A.)

Definition of a Valley: Daily bar chart of DJIA published in *The Wall Street Journal of* indicates whether or not the market has formed a valley. (*Tip: A minimum of five days of daily bars should be considered in order to determine if a valley has formed.*

c. Long-term buy signals are generally valid if they occur after the sharp decline week.

3. Exception EC

EC1: All short-term sell signals should be considered invalid if (I+N)/2% < 40.00%

4. Exception ED

Frequent occurrence of IO and VI indicators is an indication of market's normal action-reaction behavior and they could generate false buy and sell signals. Therefore, the following check should be made:

ED1: S1 sell signals should be considered as valid sell signals when one of the following conditions exists:
   a. MC = 5/0, 4/1 or 3/2
   b. MC = 0/5, 1/4 or 2/3 and Zone is B or B–

ED2: S1 buy signals should be considered as valid buy signals when one of the following conditions exists:
   a. MC = 0/5, 1/4 or 2/3

b. MC = 5/0, 4/1 or 3/2 and the average rate of movement [i.e., (R30+R40)/2] is less than 1.013
c. MC = 5/0, 4/1 or 3/2 and SSR is 35.00 or less

5. Exception EE

EE1: S1 or S2 sell signal which occurs with any long-term (L1, L2 or L3) buy signal, or within, say *4 weeks,* from the week of such long-term buy signal, should be considered invalid.

EE2: S1 or S2 buy signal which occurs with any long-term (L1, L2 or L3) sell signal, or within, say *4 weeks,* from the week of such long-term sell signal, should be considered invalid.

6. Exception EF

EF1: All short-term sell signals are invalid if SSR < or = 35.00 regardless of the market level, high or low.

EF2: All short-term buy signals are invalid if SSR > or = 55.00 regardless of the market level, high or low.

7. Exception EG

EG1: All short-term sell signals, except S3, S4 and S8 sell signals, are invalid if they occur during the week in which DJIA, S&P 500 (SPX), Value Line Geometric (VLG) or S&P 100 (OEX) Index set a 52-week new high, or if any of these indexes had set a 52-week new high during the week previous to week of such signals.

EG2: All short-term buy signals, except S3, S4, S5 and S8 buy signals, are invalid if they occur during the week in which DJIA, S&P 500 (SPX), Value Line Geometric (VLG) or S&P 100 (OEX) Index set a 52-week new low, or if any of these indexes had set a 52-week new low during the week previous to week of such signals.

Notes: (1) All short-term buy signals occurring with the new highs are generally OK provided that the other indicators are also confirming the market action.
(2) When DJIA makes a new high, it is likely that the other indexes will soon follow the trend.

8. Exception EH

EH1: If a short-term buy or a long-term (L1, L2 or L3) buy signal occurs with S3 or S9 sell signal during the same week, S3 or S9 sell signal governs over the short-term and long-term buy signals first, and then the short-term buy or the long-term buy signal.

EH2: If a short-term sell or a long-term (L1, L2 or L3) sell signal occurs with S3 or S9 buy signal during the same week, S3 or S9 buy signal governs over the short-term and long-term sell signals first, and then the short-term sell or the long-term signal.

Note: All other situations should be considered as conflicting signals. Refer to Section 107 for details.

(C) Warnings

1. Warning WA

A change in the direction of the overall market from the week of signal to the next week must confirm the buy (direction should be up) or sell (direction should be down) position. If not, the position should be closed.

Direction of the overall market is determined by the direction set by a majority of the indexes, viz.: DJIA, DJTA, S&P 500, VLG and OEX from week-to-week (i.e., from the previous Friday's to this Friday's) closing prices.

This warning WA is applicable to S1, S2, S5, S7 and SZ signals. It may not apply if it coincides with low SSR values. For example, refer to case study (CS) #94/D in Chapter 7.

2. Warning WB

After S1/BY/3 or S1/SL/4 signal has occurred, if opposite change in the direction of (I+N)/2 (refer to Table 205A) meeting the requirements stated in sub-sections 102(A)3(b)4 or 102(A)3(c)4 occurs, it can void the previously confirmed B or S-index which generated the S1/BY/3 or S1/SL/4 signal. Such condition then voids (nullifies) the S1/BY/3 or S1/SL/4 signal. Simply reconfirmation of the VI-index (B or S-index) later is not sufficient for reconsideration; a new VI-index is required to generate a new buy or sell signal.

This warning WB is also applicable to S2 signals discussed in Section 102(B).

This warning WB if applicable, it means closing of the buy or sell position and, when not applicable, it does not necessarily mean continuing with the buy or sell position generated by the S1 or S2 signal.

Exception:

This warning WB is generally not applicable to S1 and S2 buy signals during the bull phase of the market and to sell signals during the bear phase of the market. Refer to Section 603 in Chapter 6 for market phases.

Section 106
How to Record Signals?

As soon as IO-Index (Table 201B), VI-Index (Table 205B), short-term signals (Section 102) or long-term signals (Section 103) occur, they should be recorded in appropriate tables with exceptions if applicable; appropriate comments may be added if clarification is warranted. Tables 103S and 602 should then be completed before making a buy, sell or hold decision.

For examples:

- If IN or OT index occurs, it should be recorded in Table 102A.
- If S5 Sell signal is indicated in Table 102E, it should be transferred to Table 602.
- If L2 Buy signal is indicated in Table 103C, it should be transferred to Table 103S.

The next step involved is to refer to Chapter 5 for further evaluation of current market conditions and the signals before making a final decision. Also refer to Section 213 in Chapter 2 for additional comments or remarks, if any.

SECTION 107
WHAT-TO-DO IF SIGNALS CONFLICT?

The following are general guidelines:

(a) If conflicting indexes occur during the week, they should be ignored.

(b) If index conflicts with the signal, ignore the index.

(c) If conflicting signals (S1 buy and S3 sell signals, S1 sell & S8 buy signals, S4 buy & S7 sell signals, etc.) occur during the same week, refer to Section 105(B) for applicable exceptions. For examples:

- S1 Buy & L1 Sell ..... Refer to Exception EE1
- S1 Sell & L3 Buy ..... Refer to Exception EE2
- S1 Buy & S3 Sell ..... Refer to Exception EH1
- L2 Sell & S3 Buy ..... Refer to Exception EH2
- S1 Sell & S8 Buy ..... Ignore both Signals, do nothing
- S1 Sell & S8 Buy(CNM)..... Use S1 sell signal

SECTION 108
CONFLICTING MARKET MOOD INDICATORS

When conflicting market mood indicators occur, it is suggested to go with what the majority indicates.

Strength of the signal depends on the market mood indicators and whether or not the market is showing signs of tired bull or tired bear phase. Use judgment and be cautious when trading options. Refer to Section 304 in Chapter 3 for details.

SECTION 109
SIGNS OF TIRED BULL PHASE

During the market's up-trend, at some point in time, market will stall and begin to move sideways (laterally) or in a zig-zag fashion (creating a narrow band of series of crests and valleys) without moving appreciably up or down, one of the following conditions can occur:

(a) Market could absorb the selling pressure and break out upward from the pattern, but might or might not be able to sustain the upward trend, or

(b) Market while trying to absorb the selling pressure, could run out of steam and break out downward from the pattern setting the stage for a bear market.

During the period when the market is in the state of transition, short-term losing trades frequently occur. Then, how to interpret the buy and sell signals? Consider the following:

- Long-term buy and sell signals should be considered with caution.

- Short-term buy signals should be ignored if they occur in bearish zone (B, C3, D2, D3 or E1), or if zone is changing to bearish or is more bearish than the previous zone. Refer to Section 101 for details.
- Short-term sell signals should be ignored if they occur in bullish zone (A, C1, E3, F2 or F3), or if zone is changing to bullish or is more bullish than the previous. Refer to Section 101 for details.

For examples, refer to S9 buy signals of 3/20/92 and 4/10/92 in Table 102I.

Section 110
Signs Of Tired Bear Phase

During the market's down-trend, at some point in time, market will stall and begin to move sideways (laterally) or in a zig-zag fashion (creating a narrow band of series of crests and valleys) without moving appreciably up or down, one of the following conditions can occur:

(a) Market while trying to consolidate could run out of steam and move further down.

(b) Market could complete the consolidation and break out upward from the pattern. and may set a stage for a bull market.

During the period when the market is in the state of transition, short-term losing trades frequently occur. Then, how to interpret the buy and sell signals? Consider the following:

- Long-term buy and sell signals should be considered with caution.
- Short-term buy signals should be ignored if they occur in bearish zone (B, C3, D2, D3 or E1), or if zone is changing to bearish or is more bearish than the previous zone. Refer to Section 101 for details.
- Short-term sell signals should be ignored if they occur in bullish zone (A, C1, E3, F2 or F3), or if zone is changing to bullish or is more bullish than the previous. Refer to Section 101 for details.

Form 103A—CONDITIONS FOR L1 SIGNALS—Work Sheet

Form 103A Page:

	Must	Required Any Two			Must	Conditions		Remarks	
	DJIA	DJTA	VLG	OEX	SPX	(a) & (b)	Met?	(Exception)	Signal
Week Ending						(a): vs.			
WkEd Close						(b): MA-Status			
WkAv						D5-			
30-wk MA						D10-			
						D40-			
WkEd vs. 30-wk									
WkAv vs. 30-wk									
Week Ending						(a): vs.			
WkEd Close						(b): MA-Status			
WkAv						D5-			
30-wk MA						D10-			
						D40-			
WkEd vs. 30-wk									
WkAv vs. 30-wk									
Week Ending						(a): vs.			
WkEd Close						(b): MA-Status			
WkAv						D5-			
30-wk MA						D10-			
						D40-			
WkEd vs. 30-wk									
WkAv vs. 30-wk									
Week Ending						(a): vs.			
WkEd Close						(b): MA-Status			
WkAv						D5-			
30-wk MA						D10-			
						D40-			
WkEd vs. 30-wk									
WkAv vs. 30-wk									
Week Ending						(a): vs.			
WkEd Close						(b): MA-Status			
WkAv						D5-			
30-wk MA						D10-			
						D40-			
WkEd vs. 30-wk									
WkAv vs. 30-wk									

Legend: WkAv = Average of daily closing prices for the week

Table 103(F)3/4—Examples of IS2 and IS3 Signals
For details, refer to Section 103(F)3 and 4

R		IS2 Buy Signals					IS3 Sell Signals					Result
o	A	C	D	E	F	G	I	J	K	L	M	N
w #	96-97 WkEd	13-Wk T-bill	3-wk smaC	Special mmaD	Ratio D/E	IS2 Buy Signal	3-Yr T-Note	3-wk smaI	Special mmaJ	Ratio K	IS3Sell Signal	Buy/Sell Signals
46	8/2/96	5.34	5.317	5.281	1.007	> 1.000	6.44	6.457	6.419	1.081		
47	8/9	5.22	5.280	5.281	1.000	> 1.000	6.34	6.393	6.412	1.065		
48	8/16	5.18	5.247	5.272	0.995	**< 1.000**	6.12	6.300	6.380	1.048		
49	8/23	5.20	5.200	5.254	0.990	**< 1.000**	6.13	6.197	6.327	1.031		
50	8/30	5.21	5.197	5.240	0.992	**Buy**	6.18	6.143	6.275	1.017		**Buy**
51	9/6	5.33	5.247	5.242	1.001	> 1.000	6.41	6.240	6.265	1.008		
52	9/13	5.31	5.283	5.252	1.006	> 1.000	6.55	6.380	6.298	1.003		
53	9/20	5.21	5.283	5.260	1.004	> 1.000	6.45	6.470	6.347	1.001		
54	9/27	5.32	5.280	5.265	1.003	> 1.000	6.40	6.467	6.381	1.002		
55	10/4	5.14	5.223	5.255	0.994	**< 1.000**	6.29	6.380	6.381	1.001		
56	10/11	5.09	5.183	5.237	0.990	**< 1.000**	6.16	6.283	6.353	0.995		
57	10/18	5.14	5.123	5.208	0.984	**Buy**	6.10	6.183	6.304	0.984		Rpt-Buy
58	10/25	5.14	5.123	5.187	0.988		6.08	6.113	6.250	0.974		
59	11/1	5.18	5.153	5.179	0.995		6.09	6.090	6.204	0.968		
60	11/8	5.18	5.167	5.176	0.998		5.97	6.047	6.159	0.965		
61	11/15	5.16	5.173	5.175	1.000		5.89	5.983	6.109	0.965		
62	11/22	5.16	5.167	5.173	0.999		5.81	5.890	6.046	0.964		
63	11/29	5.16	5.160	5.170	0.998		5.79	5.830	5.984	0.955		
64	12/6	5.11	5.143	5.163	0.996		5.75	5.783	5.927	0.941		
65	12/13	4.96	5.077	5.142	0.987		5.77	5.770	5.882	0.927		
66	12/20	4.88	4.983	5.102	0.977		5.89	5.803	5.860	0.918		
67	12/27	5.05	4.963	5.067	0.979		5.98	5.880	5.865	0.919		
68	1/3/97	5.22	5.050	5.063	0.997		5.97	5.947	5.889	0.927		
69	1/10	5.16	5.143	5.083	1.012	> 1.000	6.06	6.003	5.921	0.939		
70	1/17	5.18	5.187	5.109	1.015	> 1.000	6.15	6.060	5.961	0.954		
71	1/24	5.16	5.167	5.123	1.008	> 1.000	6.15	6.120	6.007	0.968	< 1.000	
72	1/31	5.20	5.180	5.138	1.008	> 1.000	6.17	6.157	6.049	0.982	< 1.000	
73	2/7	5.13	5.163	5.144	1.004		6.17	6.163	6.082	0.996	< 1.000	
74	2/14	5.16	5.163	5.149	1.003		6.03	6.123	6.094	1.008	**> 1.000**	
75	2/21	5.11	5.133	5.145	0.998	< 1.000	5.99	6.063	6.085	1.017	**> 1.000**	
76	2/28	5.14	5.137	5.143	0.999	< 1.000	5.96	5.993	6.059	1.022	**> 1.000**	
77	3/7	5.24	5.163	5.148	1.003		6.15	6.033	6.052	1.029	**Sell**	**Sell**
78	3/14	5.20	5.193	5.159	1.007		6.27	6.127	6.073	1.036		
79	3/21	5.27	5.237	5.179	1.011		6.30	6.240	6.121	1.044		
80	3/28	5.41	5.293	5.207	1.017		6.41	6.327	6.180	1.049		
81	4/4	5.32	5.333	5.239	1.018	> 1.000	6.36	6.357	6.230	1.052		
82	4/11	5.58	5.437	5.288	1.028	> 1.000	6.58	6.450	6.293	1.056		
83	4/18	5.29	5.397	5.315	1.015	> 1.000	6.62	6.520	6.358	1.059		
84	4/25	5.35	5.407	5.338	1.013	> 1.000	6.63	6.610	6.430	1.063		
85	5/2	5.35	5.330	5.336	0.999	**< 1.000**	6.64	6.630	6.487	1.067		
86	5/9	5.28	5.327	5.334	0.999	**< 1.000**	6.48	6.583	6.515	1.069		
87	5/16	5.22	5.283	5.321	0.993	**Buy**	6.44	6.520	6.516	1.071		**Buy**
88	5/23	5.31	5.270	5.308	0.993		6.40	6.440	6.494	1.072		
89	5/30	5.16	5.230	5.289	0.989		6.41	6.417	6.472	1.070		

Table 105(A)1—Application Of Exceptions & Warning Signals
(For details, refer to Section 105)

	Short-Term Signals									
Exceptions	S1	S2	S3	S4	S5	S6	S7	S8	S9	SZ
EA1	**B** S									
EA2	S	S								
EA3			S							
EB1 (*)	S	S	S	S	S	S	S	S	S	S
EB2 (*)	**B**	**B**		**B**	**B**	**B**	**B**	**B**	**B**	**B**
EC1	S	S	S	S	S	S	S	S	S	S
ED1	S									
ED2	**B**									
EE1	S	S								
EE2	**B**	**B**								
EF1	S	S	S	S	S	S	S	S	S	S
EF2	**B**	**B**	**B**	**B**	**B**	**B**	**B**	**B**	**B**	**B**
EG1	S	S			S	S	S		S	S
EG2	**B**	**B**				**B**	**B**		**B**	**B**
EH1			S						S	
EH2			**B**						**B**	
Warnings										
WA (?)	**B** S	**B** S			**B** S		**B** S			**B** S
WB (#)	**B** S	**B** S								

Legend: **B** indicates exceptions or warning signals are applicable to buy signals.
S indicates exceptions or warning signals are applicable to sell signals.
(*) means Exception EB1 and EB2 are applicable to long-term (L) signals also.
(?) Warning WA is generally not applicable if it coincides with low SSR values. For example, refer to case study (CS) #94/D in Chapter 7.
(#) WB warning signal if applicable, it means closing of the buy or sell position and, when not applicable it does not necessarily mean continuing with the buy or sell position generated by S1 or S2 signal.
WB warning signal is generally not applicable to buy signals during the bull phase of the market and to sell signals during the bear phase of the market. Refer to Section 603 in Chapter 6 for market phases.

❖ *Don't get buried under the overwhelming information.*
Be selective & work smart, Don't work hard ❖

Chapter 2

COLLECTION & ANALYSIS OF MARKET DATA

OBJECTIVE

To learn and understand what necessary market data are to be collected to develop market signals and how to tabulate and analyze them in order to develop technical indicators for use in Chapter 1 to generate market signals.

SECTION 200
INTRODUCTION TO MARKET DATA

(A) General

Market data required for analysis are shown on *Form 200 (see page 2-13)*. Refer to Table 200 in Appendix B for a sample of data elements. Data should be collected on a weekly basis, tabulated and analyzed as illustrated in Tables 201 to 211 included in Appendix B.

Market data shown on Form 200 may be obtained from:

- Barron's-The Dow Jones Business & Financial Weekly Publication
- The Wall Street Journal-Published every business day of the week

(B) What-To-Do With The Data?

Data elements, which are collected using Form 200 and shown in Table 200 in Appendix B, should be transferred to applicable Tables for analysis as indicated in the Table below.

DATA ELEMENTS FROM TABLE 200:	TRANSFER TO:
DJIA (daily closing figures)	Table 201A, Column B
IssAdv – IssDec (daily closing figures)	Table 201A, Column D
TICK (daily closing figures)	Table 201A, Column I
DJIA, DJTA, SPX, VLG & OEX (daily closing figures)	Use for plotting Pt/Fg Charts, Refer to Section 203
DJIA (end of the week closing figure)	Table 204A
DJTA & SPX (end of the week closing figures)	Table 204B
VLG & OEX (end of the week closing figures)	Table 204C
Vu-d, Ia-d and Nh-l	Table 205A
Vu%, Ia% and Nh%	Table 205B
Ia%	Table 207A
C/P	Table 207A
SSR	Tables 207A & 211
WIa%	Tables 207A & 211
WNh%	Table 211
Ratio = (Lesser of WNh or WNl)/WIt If & when the Ratio > 6.50%	Table 211

Section 201
IO (In/Out) Indicators & Indexes

Table 201A should be completed first. Information from Table 201A is used in conjunction with Table 201B for determining IO indicator (indexes) described in Section 102(A). Table 201A also includes 10-day moving sum (ms) of NYSE daily closing TICKs (refer to Section 202).

Table 201B facilitates determination of IO indexes using the information from Table 201A and is self-explanatory.

The following is an explanation of each column in Table 201A:

Column A	Enter date or week ending
Column B	Enter daily DJIA closing prices
Column C	Calculate 5-day moving sum (ms) of DJIA in Column A (*)
Column D	Enter daily Ia-d from Table 200
Column E	Calculate 10-day moving sum (ms) of Ia-d in Column D (*)
Column F	Calculate 5-day moving sum (ms) of values in Column E (*)
Column G	Determine LP or HP per Section 102(A)2 if warranted
Column H	Determine IO-Index per Section 102(A)2 if warranted
Column I	Enter daily closing TICK from Table 200
Column J	Calculate 10-day moving sum (ms) of values in Column I (*)

(*) Refer to Appendix A for calculation of moving sums.

Section 202
NYSE Closing Tick Index

A ten day moving sum of NYSE daily closing TICKs is found to be useful in developing a S9 buy and sell signals. For details refer to Section 102(I). Table 201A is used for calculating the various moving sums including the 10-day moving sum (ms) of NYSE daily closing TICKs.

Refer to Appendix A for calculation of moving sums.

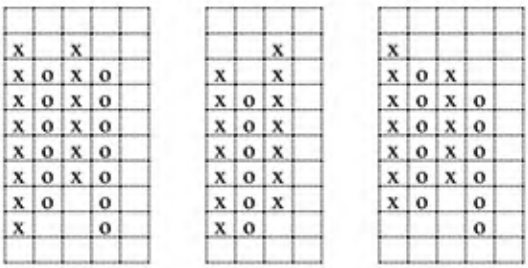
NYSE daily closing TICK figures—reported daily in *The Wall Street Journal* and weekly in *Barron's*. It is a number that is equal to the number of stocks whose last change in price was up, less the number of stocks whose last change in price was down. Where as the number of advancing and declining issues are determined based on the closing prices as of the previous trading day.

Section 203
Point & Figure (Pt/Fg) Charts

A point & figure chart is used exclusively in the stock market by many technicians and investors to predict trends. The application of point & figure charts used here is somewhat different from that which is customarily used.

A point & figure chart is easier to construct and maintain than any other type of chart. It is also easier to read and interpret than other charts. The construction of Pt/Fg (Point & Figure) charts of market indexes is described in Appendix A.

Table 203 shows the status of point and figure charts of the market indexes; "X" indicates the chart has a bullish pattern; "O" indicates the chart has a bearish pattern. Examples below illustrate some of the bullish and bearish patterns. For more details, refer to Appendix A.



Bearish (Assign "O") | Bullish (Assign "X") | Bearish (Assign "O")

The units of charting to be used for market indexes DJIA, DJTA, SPX, VLG and OEX are:

For values:	100 to 1250	Each block represents 2 points
	Over 1250	Each block represents 5 points
	Over 2500	Each block represents 10 points
	Over 5000	Each block represents 20 points
	Over 10000	Each block represents 50 points

In constructing Pt/Fg charts, only daily closing prices are to be used.

Section 204
Market Indexes

The market indexes considered here are DJIA, DJTA, SPX, VLG and OEX.

Table 204A shows 10-, 20-, 30-, 40-and 5-week moving averages (MA) of DJIA based on Friday's (end of the week) closing prices.

Table 204B shows 10-and 30-week moving averages (MA) of DJTA and SPX based on Friday's (end of the week) closing prices.

Table 204C shows 10-and 30-week moving averages (MA) of VLG and OEX based on Friday's (end of the week) closing prices.

Refer to Appendix A for calculation of moving averages.

Section 205
NYSE Composite Breadth Indexes

Tables 205A and 205B are self-explanatory. Note that 10-wk moving sum (MS) and cumulative sum of Vu-d in Table 205A are for information only and they need not be recorded.

Refer to Appendix A for calculation of moving sums, cumulative sums, and moving averages.

Section 206
Market Condition (MC) Indicator

A market condition (MC) indicator is a composite index determined based on changes in the following five technical indicators:

- **Composite summary of Pt/Fg Charts**

  In Table 203 for the week under consideration, if the number of X's exceeds the number of O's, the composite index is X and it is recorded as "X" in Table 206, and if the number of O's exceeds the number of X's, the composite index is O and it is recorded as "O" in Table 206.

- **DJIA Momentum (Mtm)**

  Momentum is determined by dividing Friday's (end of the week) closing price of the Dow Jones Industrial Average (D) to its 30-week moving average (D30).

  Refer to Table 204A for DJIA momentum (Mtm = D/D30).

  If the rise in momentum is 0.030 or more from its most recent low, it is recorded as "X" in Table 206, and if the fall in momentum is 0.030 or more from its most recent high, it is recorded as "O" in Table 206.

- **V%**

  If the rise in V% is more than 0.50 from its most recent low, it is recorded as "X" in Table 206, and if the fall in V% is more than 0.50 from its most recent high, it is recorded as "O" in Table 206.

  For V%, refer to Table 205B.

- **I%**

  If the rise in I% is more than 0.50 from its most recent low, it is recorded as "X" in Table 206, and if the fall in I% is more than 0.50 from its most recent high, it is recorded as "O" in Table 206.

  For I%, refer to Table 205B.

- **N%**

  If the rise in N% is 3.00 or more from its most recent low, it is recorded as "X" in Table 206, and if the fall in N% is 3.00 or more from its most recent high, it is recorded as "O" in Table 206.

  For N%, refer to Table 205B.

SECTION 207
OTHER INDEXES

(A) Call-Put Ratio

Refer to Table 200 for Call-Put ratio (C/P).

Call-Put ratios (C/P) are used for developing S3 buy and sell signals. For details, refer to Section 102(C) in Chapter 1.

Table 207A lists C/P ratio and (A–B) data on a weekly basis so that it would be easy to use in developing S3 buy and sell signals described in Section 102(C). Table 207A would serve as a reference if it should be necessary later for verification and review of S3 signal condition rules.

If and when the values of (C/P) and (A–B) fall within the range specified for S3 signals in Section 102(C), they should be recorded in Table 211.

(B) Ratio of New Highs or New Lows To Total Issues

Refer to Table 200 for new highs (WNh), new lows (WNl) and total issues (WIt).

The ratio of the lesser of week-to-week new highs (WNh) or new lows (WNl) to the total number of issues traded (WIt) is used for developing S4 buy and sell signals. For details, refer to Section 102(D) in Chapter 1.

Ratios greater than 6.50% only are indicative of market strength or weakness. Therefore, only such ratios, when they occur, should be recorded in Table 211 for further evaluation in accordance with Section 102(D).

SECTION 208
MARKET RATE OF MOVEMENT

(A) DJIA 30-Week Rate

Refer to Table 208A which is self explanatory. The DJIA 30-Week Rate (R30) is used in determining market movement zones described in Section 101.

Three weeks average of DJIA is needed for Table 208A. It is calculated by adding each set of three weeks of DJIA data recorded in Table 204A and dividing the sum by three.

(B) DJIA 40-Week Rate

Refer to Table 208B which is self explanatory. The DJIA 40-Week Rate (R40) is used in determining market movement zones described in Section 101.

Four weeks average of DJIA is needed for Table 208B. It is calculated by adding each set of four weeks of DJIA data recorded in Table 204A and dividing the sum by four.

SECTION 209
MARKET MOVEMENT ZONES

Using the information from Tables 204A, 208A and 208B, market zones are determined in accordance with the following Table and are recorded in Table 209 for ready reference:

R30	UP				DN				DN				UP			
R40	UP				UP				DN				DN			
D30	DN	UP	DN	UP	UP	DN	UP	DN	UP	DN	UP	DN	DN	UP	DN	UP
D40	DN	DN	UP	UP	UP	UP	DN	DN	UP	UP	DN	DN	DN	DN	UP	UP
ZONE	F1	F2	F3	**A**	C1	C2	C2	C3	D1	D2	D3	**B**	E1	E2	E2	E3

Explanatory Notes about Market Zones:

(1) Zone A becomes A+ (A plus) zone when three of the four moving averages, namely D10, D20, D30 and D40 rise more than 20 (40 for DJIA over 5,000; 100 for DJIA over 10,000) points in three weeks, and a plus (+) zone ends when this condition is broken. Plus means extra strength in the market.

(2) Zone B becomes B– (B minus) zone when three of the four moving averages, namely D10, D20, D30 and D40 fall more than 20 (40 for DJIA over 5,000; 100 for DJIA over 10,000) points in three weeks, and a minus (–) zone ends when this condition is broken. Minus means extra weakness in the market.

(3) When a change in zone occurs due to change in the direction of R30, such zones have three weeks of transition period and they may lag as much as by two weeks(*) because R30 is calculated in intervals of three weeks (i.e., in three-week steps).

Similarly, when a zone changes due to change in the direction of R40, such zones have four weeks of transition period and they may lag as much as by three weeks(*) because R40 is calculated in intervals of four weeks (i.e., in four-week steps).

(*) Zone may be considered effective one or two weeks prior to week of zone change revealed by the change in direction of R30 and two to three weeks prior to week of zone change revealed by the change in direction of R40. Refer to Table 209 for details.

However, in critical situations if it is necessary to validate a buy or a sell signal which depends on zone condition requirements, R30 and R40 may be determined for that week by including that week's (end of the week) closing price of the DJIA in calculating the 3-and 4-week averages needed for column B in Tables 208A and 208B. For example, refer to S1/BY/1 of 4/18/96 in Table 102A in Appendix B.

Section 210
MarketT Chart Of Key Indexes

The following key indexes are selected for the chart, which should be constructed on a simple graph paper, consisting of 10 blocks to an inch. The horizontal axis represents time in weeks (1 block = 1 week) and the vertical axis represents the variables listed below.

- A vertical bar on the chart for each week represents high & low based on DJIA daily closing prices during the week and Friday's close from Table 200
- DJIA 10-week, 20-week, 30-week and 40-week averages from Table 204A
- Cumulative sum of Ia-d (Ics) from Table 205A
- MC Indicator from Table 206

The purpose of the chart is to see how each indicator behaves relative to the DJIA movement, whether or not, any disparity exists among them. Therefore, it is important that they all should be included in one chart using suitable scales on the vertical axis. A chart is worth a thousand words; it can display things that are not otherwise readily apparent.

SECTION 211
WEEKLY SUMMARY LOG

The following information will be helpful in completing Table 211. The first column shown below is the same as in Table 211; the second column provides information from where to obtain the data required for the first column:

First Column in Table 211	For information, refer to:
Year	
Week Ending	
Zone	Table 209
DJIA	Table 200
DJTA	Table 200
S&P 500	Table 200
ValueLine (G)	Table 200
S&P 100	Table 200
WIa%	Table 200
WNh%	Table 200
WNh, WNl/WIt	Table 200 {Refer to Section 102(D) & 207(B) for details}
SSR	Table 200
(I + N)/2	Table 205A
N%	Table 205B
(I+N)/2%	Table 205B
MC: Market Cond.	Table 206
C/P	Table 207A or Table 200
(A-B) = WIa%-Ia%	Table 207A or Table 200
IO-Index	Table 201A or 201B {Refer to Section 102(A) for details}
VI-Index	Table 205B {Refer to Section 102(A) for details}
M1-Index	Table 200 {Refer to Section 104(B) for details}
M2-Index = OB/OS	Table 201A {Refer to Section 104(B) for details}
M3: Ics vs. DJIA	Sections 210 and 104(B)
M4: Has DJIA x'ed moving avgs?	Table 204A {Refer to Section 104(B) for details}
Long-Term Signals	Tables 103B through 103E
Short-Term Signals	Tables 102A through Table 102J
Exceptions	Section 105(B)
Warnings	Section 105(C)
Sug. Action	Buy, Sell, None, etc.
Remark #	Section 213 (If remark is noted)

SECTION 212
TALLYING THE WEEK-END INDICATORS

A review of the following table will be helpful to identify quickly if there is a possibility of a buy or a sell signal in the weeks ahead, and what-to-watch next so that any signal that is going to occur won't be missed.

Tallying the Week—End Indicators

If this Week Ending Indicators are	What to Check now and What to Watch next?	What signals to expect?	For Details Refer to Section #
IO-index and VI-index	Changes in (I+N)/2 and (I+N)/2%	S1 Buy or S1 Sell	102(A)
IO-index and VI-index	MC limits, Zone, Changes in (I+N)/2 and (I+N)/2%	S2 Buy or S2 Sell	102(B)
C/P < 1.20 and Zone = A or B	A–B = 0 to –6	S3 Buy	102(C)
C/P > 1.80 and Zone = A or B	A–B = 0 to +6	S3 Sell	102(C)
Ratio: WNh/WIt > 6.50	Refer to Section 102(D)	S4 Buy	102(D)
Ratio: WNl/WIt > 6.50	Refer to Section 102(D)	S4 Sell	102(D)
SSR < or = 35.00	Refer to Section 102(E)	S5 Buy	102(E)
SSR > or = 55.00	Refer to Section 102(E)	S5 Sell	102(E)
(I+N)/2% < 45.00%	IO-index, VI-index, MC and (I+N)/2	S6 Buy	102(F)
Nh% < 45 %	Nh% for the next two weeks	S7 Buy	102(G)
D/D5 < or = 0.97 (Refer to Table 204A)	Zone, MC = 0/5 or 1/4 and status of D5 line	S8 Buy	102(H)
D/D5 > or = 1.03 (Refer to Table 204A)	Zone, MC = 5/0 or 4/1 and status of D5 line	S8 Sell	102(H)
MC = 0/5 (or may be 1/4) (Refer to Table 206)	Direction of '10-day ms' of NYSE TICK and the market trend per DJIA bar chart	S9 Buy	102(I)
MC = 5/0 (or may be 4/1) (Refer to Table 206)	Direction of '10-day ms' of NYSE TICK and the market trend per DJIA bar chart	S9 Sell	102(I)
MC = 0/5 ↔ 1/4 for several weeks (Refer to Table 206)	Zone A or A+ and direction of DJIA (end of the week) closing prices for the next three weeks	SZ Buy	102(J)

SECTION 213
WEEK CONCLUDED

This Section should include:

- Detail explanation of remarks if and when noted in the last row of Table 211.
- Conclusion based on the guidelines given in Chapter 5.
- Other pertinent comments or questions if any.

The main purpose of this review is to make sure if the short-term signals are consistent with the ongoing market condition. For illustration purposes, Example 1: S7/BY of 12/23/94 {Remark #94/12 noted in Example 2 in Section 104(B)1} and Examples 2 & 3: S5/BY of 6/21/96 & S5/BY of 7/26/96 (Remarks #96/6 & #96/7 noted in Table 211 in Appendix B) are evaluated below.

Example 1: Analysis of Remark # 94/12, S7/BY signal week ending 12/23/94

Index	Brief Description of Index For details, refer to Section 104(B), Ch. 1	Status of Index	Direction of Market	The Index is:
M1	Change in Vu%, Ia%, Nh%, WIa% and WNh% from wk-to-wk vs. Market direction	= –1	Up overall fr. prev. wk	Bearish
M2	20-day MS of Ia-d = OB/OS	Neither	Not Appl.	--------
M3	Ics vs. DJIA direction over the last few weeks	Down overall	Up overall	Bearish
	OR (I+N)/2% vs. the DJIA	Down overall	Up overall	Inf. only
M4	DJIA X-ing upward or downward its MA lines	X-ing Upward	Not Appl.	Bullish
M5	Change in relation of DJIA MA lines	As is, no change	Not Appl.	--------
M6	Reversal of Pt/Fg trend	From 1/4 to 2/3	Not Appl.	Bullish
M7	New highs or new lows	Neither	Not Appl.	--------
M8	MC rose or fell?	From 2/3 to 1/4	Not Appl.	Bearish
M9	Mtm rising or falling over the last few weeks?	Rising overall	Not Appl.	Bullish

Overall consensus of the indicators is neutral. Therefore, the buy signal is neutral.

Example 2: Analysis of Remark # 96/6, S5/BY signal week ending 6/21/96

Index	Brief Description of Index For details, refer to Section 104(B), Ch. 1	Status of Index	Direction of Market	The Index is:
M1	Change in Vu%, Ia%, Nh%, WIa% and WNh% from wk-to-wk vs. Market direction	= –1	Up overall fr. prev. wk	Bearish
M2	20-day MS of Ia-d = OB/OS	Oversold	Not Appl.	Bullish
M3	Ics vs. DJIA direction over the last few weeks	Down overall	Zig-zag	Bearish
M4	DJIA X-ing upward or downward its MA lines	As is, no change	Not Appl.	--------
M5	Change in relation of DJIA MA lines	Neutral	Not Appl.	--------
M6	Reversal of Pt/Fg trend	As is, no change	Not Appl.	--------
M7	New highs or new lows	Neither	Not Appl.	--------
M8	MC rose or fell?	From 0/5 to 1/5	Not Appl.	Bullish
M9	Mtm rising or falling over the last few weeks?	Falling overall	Not Appl.	Bearish

Overall consensus of the indicators is bearish. Therefore, the buy signal is not consistent (nc).

Example 3: Analysis of Remark # 96/7, S5/BY signal week ending 7/26/96

Index	Brief Description of Index For details, refer to Section 104(B), Ch. 1	Status of Index	Direction of Market	The Index is:
M1	Change in Vu%, Ia%, Nh%, WIa% and WNh% from wk-to-wk vs. Market direction	= –1	Dn overall fr. prev. wk	Normal
M2	20-day MS of Ia-d = OB/OS	Oversold	Not Appl.	Bullish
M3	Ics vs. DJIA direction over the last few weeks	Down overall	Dn overall	Normal
M4	DJIA X-ing upward or downward its MA lines	As is, no change	Not Appl.	--------
M5	Change in relation of DJIA MA lines	Neutral	Not Appl.	--------
M6	Reversal of Pt/Fg trend	As is, no change	Not Appl.	--------
M7	New highs or new lows	Neither	Not Appl.	--------
M8	MC rose or fell?	From 0/5 to 0/5	Not Appl.	--------
M9	Mtm rising or falling over the last few weeks?	Begins to rise	Not Appl.	Bullish

Overall consensus of the indicators is bullish. Therefore, the buy signal is consistent.

Note:

For additional illustrations prepared using Form 304B/Page1 included in Chapter 3, refer to option trading case studies CO6, CO7, CO9 and PO5 in Appendix B, Chapter 7-Tables.

Form 200—DATA COLLECTION FORM

Form 200 WkEd: .....

.....Market Indexes..... .....NYSE Composite Daily Breadth.....

	DJIA	DJTA	SPX	VLG	OEX	VolUp	VolDn	IssAdv	IssDec	Nhigh	Nlow	TICK
M												
Tu												
W												
Th												
Fr												
Note below if 52-week new highs or new lows:												

S&P 100:- ..... / ..... = ... C = Call Vol. / Open Interest ..... / ..... = ... P = Put Vol. / Open Interest C/P = ...

Adv/Dec Tot. wkly comp.:- ..... Iss.Trad. WIt ..... IssAdv WIa ; ..... IssDec WId ..... Nhigh WNh ; ..... Nlow WNl ..... Specialists SSR / ..... = ... / Total Short Sales

---

$WIa\% = \frac{WIa}{WIa+WId}$ = ... %

$WNh\% = \frac{WNh}{WNh+WNl}$ = ... %

Ratio {Sect. 102(D)} = {Lesser of WNh or WNl} / WIt = ... / ..... = ... %

Market Indexes:

DJIA = Dow Jones 30 Industrial Average
DJTA = Dow Jones 20 Transportation Average
SPX = Standard & Poor's (S&P) 500 Index
VLG = Value Line Geometric (G) Index
OEX = Standard & Poor's (S&P) 100 Index
TICK = NYSE Daily Closing TICK

NYSE Composite Daily Breadth:

Listed under the heading Trading Diary in *Barron's*—Market Laboratory Stocks Section.

VolUp = Volume Up IssAdv = Issues Advanced Nhigh = New Highs
VolDn = Volume Down IssDcl = Issues Declined Nlow = New Lows

S&P 100 (OEX) Call/Put Figures:

Listed under the Stock Index Options: Weekly Summary in the Options Section.

Adv/Dec Tot. Wkly Comp.:

Market Advance/Decline Totals-Weekly Comparison figures are listed under the heading "Trading Diary" in *Barron's*—Market Laboratory Stocks Section.

Specialists' Short Sales to Total Short Sales:

Listed under the heading "NYSE Members Report" in *Barron's*.

Note: The Specialists' and Total Short Sales figures reported in *Barron's* lag by approximately two weeks. However, it is used here as if it had occurred the week under consideration.

❖ *Never ever consider buying anything without a buy signal. Key is to avoid buying at or near the top* ❖

Chapter 3

STOCKS, MUTUAL FUNDS & OPTIONS

OBJECTIVE

At the conclusion of this Chapter, you should be able to learn how & when to buy and sell stocks, mutual funds and index options intelligently and, how to keep a simple but effective records of all your investments.

OVERVIEW

This Chapter describes how to select stocks and mutual funds, when to buy and sell them, and a systematic approach for trading index options. It is divided into following Sections:

301 -Stocks Selection & Evaluation

302 -Stock Buy & Sell Index

303 -Mutual Funds

304 -Options-Special Situation

305 -Tracking The Investment

SECTION 301
STOCKS SELECTION & EVALUATION

(A) Selection

The primary purpose here is to give general background information and to show when to buy and sell a particular stock once it is considered as a good value for investment. It is not intended here to discuss "how to select the best stocks" from thousands of stocks listed on the major stock exchanges.

The Outlook-a weekly publication of Standard & Poor's, parts 1 and 2 of The Value Line Investment Survey, Barron's and various financial magazines, which time-to-time, feature companies that they believe have potential for growth, are useful references for preparing a initial list of few investment grade stocks. Many brokerage houses also periodically publish information on companies they analyze or they follow for their clients.

To select a few good stocks from the list for further consideration, investors need to spend some time to gather vital information about the companies. A local library will be very helpful for such studies. *The Value Line Investment Survey, the Standard & Poor's (S&P) Stock Reports* and *the S&P Stock Guide* are often available in most public libraries. They are good source of investment information.

Never ever consider those companies for which the necessary information for evaluation is not readily available. *Refer to Forms on pages 3-31 and 3-32* for necessary information.

While reviewing such material, investors should be careful of phrases which begin with "if, but, expect, in spite of, etc." In conducting a research, investors should consider several factors, such as the primary business of the company, company's competitive position relative to others in the same industry, whether its overall business depends on a single customer or a single product or general economic condition, company's involvement in new product development or new service area, and prospects for future earning and dividend growth.

If a stock does not appeal based on the products or services the company offers or promotes, potential for earning growth, company's financial condition, etc., it should not be considered. Prepare a list of such selected stocks with brief comments, as appropriate.

Use of *Form 301A on page 3-31* may ease the task of gathering vital information on stocks for review and selection, and later, monitoring the performance, as the case may be. The task involves finding under-valued and emerging growth stocks or stocks with potential for price appreciation and with strong balance sheet that have yet plenty of room left for upside move.

(B) Fine-Tuning The Selection

For a stock to remain on a selection list, a *Value Line Investment Survey* data sheet, or a *Standard and Poor's Stock Report*, or other equivalent information should be available about the company. In

other words, if the information on a company is not available or is hard to find, that stock should be eliminated from the list.

Ponder the information gathered and decide which stock(s) should not remain on the final list. Do not pay any attention to who, why and where the stock was featured. Do not jump into conclusion of buying a stock because it is recommended highly by an advisory service until you thoroughly investigate and understand the issue. Never think that you are going to miss the opportunity by doing so. Remember—haste is waste and hurrier you go, behinder you get. Refer to case studies in Section 702 in Chapter 7.

Keep in mind, value should be the primary consideration in the selection process. Certain ratios can be useful tools in analyzing and comparing companies. Financial ratios provide ways to quantify company's operating success and financial well being. Valuation ratios, such as price-to-earning and price-to-book value can be helpful to gauge the price of the share in relation to the market averages.

The following ratios generally indicate the financial condition of the company:

1. Current Ratio

   Total current asset to total current liability ratio of at least 1.50 is generally considered satisfactory for most companies. The ratio may be calculated using the information from the *Standard & Poor's Stock Report*, the *S&P Stock Guide,* the *Value Line Investment Survey* or the company's financial condition report.

   This ratio is especially critical for companies in financial trouble. Declining ratio from period to period could signal a forthcoming cash problems. On the other hand, too high of a ratio imply company's inability to turn assets into profitable business. Remember that the suggested ratio, however, may differ significantly among various industries, such as utility, banking and financial service industries.

2. Debt To Total Capital Ratio

   It is a ratio of long-term debt to total capital (long-term debt plus stockholders' common equity) expressed as percent. Figures for the long-term debt and the common equity may be found in the *Standard & Poor's Stock Report,* the *S&P Stock Guide* or the company's financial condition report. This ratio measures the company's financial strength.

   A high ratio generally indicates high risk and greater potential for default. Therefore, companies with ratios over 50% should not be considered.

Once, one or more interesting stocks are pinned down, the next task involved is to determine when to buy.

To invest in stocks, one should first decide which stocks to buy and then when to buy and sell. Which stock to buy or sell is important, but when to buy or sell is far more important and it is also the most difficult task.

For that, one should refer to the methodology discussed in Section 302.

(C) Buying Consideration

It is imprudent to buy a stock because of striking news or a special bulletin issued by a company. We do, however, get tempted to invest funds because of fear that we might miss the opportunity. Generally when we read the news, it is no longer a news—it is a history. In that you are following the crowd. The stock generally has already advanced to a point that the people who invested earlier would get tempted to cash in their profits. The methodology described in this chapter should be able to detect such news early enough for us to take position before the crowd. This does not mean that we should not keep in touch with the company's financial condition, recent developments, earning forecasts, etc.

We should not buy any stock until its technical strength shows improvement. We should always avoid buying a stock as long as it remains within the confines of formation. As long as it remains within such confinement, there is no way of predicting the length of the confinement, and when it will emerge (up or down) from it. The best time to buy a stock is when it emerges upward from its confinement (consolidation) or it is making a new high after undergoing a price consolidation.

In order to estimate when a particular stock has completed the consolidation and is ready to emerge up, it is necessary to construct 10-, 20-and 30-week moving average lines for those stocks on the list.

The methodology for buying and selling a stock is discussed in Section 302.

However, to ensure against errors in judgment (because no method is perfect), the stock portfolio should be diversified among stocks of different industries. Over-diversification, however, is equally bad unless the portfolio can be watched closely and carefully. It requires self-discipline and reasonable investment of time and effort. **A sound investment program requires continual attention.**

The last and the most important task is to evaluate the condition of the general market (refer to Chapters 1 and 2). If the general market climate is not favorable, none will do any good.

Occasionally, some investors may find winners in a bad market, but that should be considered as an exception. To find such exceptions in a bad market is like finding a needle in a stack of hay. It is not necessary to remain invested all of the time. If in doubt, do nothing.

To summarize the approach briefly, one should not consider buying any stock until a buy signal is generated by the methodology described in Section 302. It is wise to ignore all lucrative articles and recommendations published regarding the stock in question. Refer to case studies in Section 702 in Chapter 7 for details. Don't let someone tell you what you need to buy if that person happens to be promoting the issue.

It is not the price of the stock that is important for buying, but when to buy is critical in order to make money. Because the stock sells below its book value or has low price-to-earning ratio, that alone should not be the primary reason for buying a stock.

Stock prices primarily depend on the supply (sellers) and demand (buyers) created by the investors in the market place. The prices fall when there are more sellers (supply of number of shares) and fewer buyers (demand of number of shares) and the prices rise when there are fewer sellers and more buyers. In other words, price rises when demand exceeds the supply. The job of the marketmaker is to discourage some buyers by raising the prices when there are more buyers than the sellers.

To determine when to buy or sell a particular stock, one should have the last 30 to 40 weeks of Friday's closing prices for that stock. Saving of Sunday's local newspapers, which generally carry this information, is helpful for recording this information. Refer to Section 302 for details.

One should not buy a stock after a long decline because it appears cheap. One should always follow the buy and sell signals described in Section 302, **even if it mandates buying a stock at higher price than the price a few weeks or months earlier**.

(D) Time-To-Act

When a buy signal is generated by the system described in Section 302, the following should be considered before buying a stock in addition to those listed in (B) above:

1. Earning Per Share (EPS)

   Sum of earning per share for the last five years should be greater than zero, or the earning per share for the most recent quarter should be greater than that of the previous quarter a year ago.

   Comment: Either condition should be generally satisfactory when a buy signal is received per methodology in Section 302. It is presumed that stock is poised to post better earning when a buy signal is generated by the stock.

   Past and current earnings per share information are reported in *Barron's,* the *Standard & Poor's Stock Report,* and the *Value Line Investment Survey.*

2. Relative Price Strength (RS)

   Relative Price Strength is the measure of how well a specific stock performs in comparison with other stocks or the general market averages. Higher the number better the performance.

   Stocks with relative price strength rank (number) of at least 35 and showing improvement should be considered. For a relative price strength (RS) rank (number), refer to stock tables in *Investor's Business Daily.*

   During a bull phase of the market, majority of the stocks appreciates in value. However, stocks with high relative strength will appreciate to a much greater degree than the overall market.

3. Institution Holdings

   Some institutional interest in the stock is preferable. If a stock is not attractive to institutions, it may not be an investment grade stock. On the other hand, if the institution interest is too big, it may be risky for the individual investor. You will be affected if institutions decide to dump it for whatever reasons.

   Percent holding of common shares by the institutions may be found in the *Standard & Poor's Stock Report or* the *S&P Stock Guide.*

4. Price-to-Earning (PE) ratio

   Price-to-Earning (PE) ratio is determined by dividing the current share price by the latest 12-month earning per share. It is given in the business section of most local and financial newspapers and in *Barron's* weekly.

Low price-to-earning ratios do not necessarily mean value. It alone should not be used as the basis for buying a stock. Supply and demand can cause one stock to sell at, say 10 times its earning, another at, say 20 times and another at 50 times its earning.

Companies poised for growth or with potential for an accelerated earning growth, or companies poised for turn-around, or emerging companies with new products generally sell at much high PE ratios (several times the PE of S&P 500 Index). They should only be considered if the market conditions are right.

In general, stocks with PE ratios much greater than (say, over two and one-half times) that of S&P 500-Stocks index are risky and highly volatile to any bad news, any earning disappointments, or if the market suddenly takes a downturn. Such stocks should not be considered until detail study of the situation is conducted; they might not have much room for further price appreciation. However, stocks with high relative strength (say, 80 or greater) can sustain high PE ratios and may be purchased if a buy signal is generated by the methodology discussed in Section 302.

5. Price-to-Book Value ratio:

It is the ratio of price of the stock to its book value. Book value can be determined by dividing the common stockholders' equity by the number of common shares. Information required for determining the book value can be obtained from the *Standard & Poor's Stock Report* or the company's financial condition report.

Because the stock sells below or at its book value should not be the reason for buying. It may be that the stock has been selling below or at the book value for most of the time.

Note that profitable companies often show a high price-to-book value ratio compared to the market indexes. On the other hand, companies having low or irregular earnings may sell below or slightly above its book value. The book value of certain companies, such as transportation, utilities, banking, investments, and insurance may sometimes indicate its fair market value.

(E) Selling Consideration

This is the most difficult decision investors are faced with. Greed and attitude toward losses or missing further gains work against the investors. Greed and attitude are two wicked witches controlling the investors' ability to make appropriate decision and, when it is mixed with hope, investors become passive without taking any action which, in most cases, results in a bigger loss.

The tendency of many inexperienced investors is to sell stocks that do well (because it is easy to accept profit) and hold those showing losses, or those sitting and doing nothing. Sometimes it is OK to hold on to poor performers and selling those fully or over-valued investments (i.e., those appear to have the least room for the near-term appreciation).

Investors should learn or discipline themselves to overcome feelings about profits and losses, and to face the reality. One cannot create an opportunity in the stock market, one takes the advantage of one that exists.

Most investors don't want to act when their stocks are down even if they have profits. They prefer to wait for more gains with the hope that their stocks will soon rise to their previous levels. This may or may not happen.

The driving force behind stock prices is the amount of earning per share companies are expected to make; any earning disappointments or poor earning forecasts often lead to decline in stock prices. However, a variety of factors, such as changes in the economy, and within a company or industry, or changes in the investors' sentiment can influence the stock prices.

Relative downward action of stock prices in a good market is usually indicative of forthcoming bad news or lower earnings. However, if the earnings are doing well and the stock is going down because the general market is going down, that could be an opportunity to buy more shares.

The single most important parameter for selling a stock is the sell signal discussed in Section 302. It works well in a majority of the cases. Don't think that the stock you own is an exception to the rule. Occasionally there may be, but it is hard to detect. You can always buy it back if conditions warrant to do so.

Section 302
Stock Buy & Sell Index

(A) Introduction

The methodology for determining buy and sell indexes is based on the stock prices in relation to its various moving averages. When a buy or a sell index meets certain requirements listed under "Index Requirements" in sub-section (D) below, it is then considered as a buy or a sell signal.

In order to generate a buy or a sell index, it is necessary to construct a 10-week moving average line for a stock in question using its Friday's (end of the week) closing prices. *Form 302A on page 3-32* may be used for calculating 10-, 20-and 30-week moving averages.

Sample examples are prepared using Form 302A. They are included in Appendix B (see Tables 302A). The procedure for determining buy and sell indexes and then, buy and sell signals is illustrated in these examples.

The elements of a buy index are B, C, BC, B/C and BR, and the elements of a sell index are S, C, SC, S/C, SB, SF, SR and ST.

(B) Elements of Buy Index

B-Index:

B-index occurs when the 10-week moving average line of a stock in question rises above the established low point (LP) by more than 1.50% (i.e., at the B-Index, the value of the 10-week moving average should be greater than 1.015 times that average at the low point).

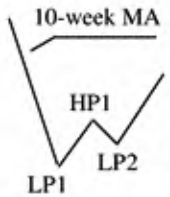
LP: It is a low point on a 10-week moving average line. A low point is considered established if the 10-week moving average line rises above 1.015 times that average at the low point (LP).

B-Index is only valid if the distance between the LP (low point) and the B-Index is 4 weeks or less. If the B-Index is invalid, no need to continue further.

Note: For stocks trading from $100 to $200, number of weeks indicated above for B-Index may be increased by one.

When two (or more) low points (LP1 and LP2) on a 10-week moving average line occur, refer to Figure 302(B) below to determine a low point (LP) to be used for a B-index.

Figure 302(B)



When HP1/LP1 < 1.015:

LP2 should be considered LP if LP2/LP1 < 1.005; otherwise LP1 is LP.

Note: LP1 < or = LP2

C-Index:

It is an index that confirms the B-Index. The B-Index is confirmed when

- 10-week moving average line rises above the 20-week moving average line, **or**
- 20-week moving average line is on a rising trend or has begun to rise at least for the last two weeks.

If one of the above conditions is present with the B-Index, the B-Index becomes a BC-Index, and when one of the above conditions occur after the B-Index, the B-Index becomes a B/C-Index.

BC-Index:

BC-Index is only valid if the distance between the LP (low point) and the BC-Index is from one week to four weeks (including).

Note: For stocks trading from $100 to $200, number of weeks indicated above for BC-Index may be increased by one.

B/C-Index:

B/C-Index is only valid if it meets one of the following conditions:

- The distance between the LP (low point) and the B-Index is from 1 week to 4 weeks (including), and the distance between the B-Index and the B/C-Index is 4 weeks or less.
- The distance between the LP (low point) and the B-Index is 0 (zero) weeks and the distance between the B-Index and the B/C-Index is 3 weeks or less.

Note: For stocks trading from $100 to $200, number of weeks indicated above for B/C-Index may be increased by one.

BR-Index:

BR is a buy-index if a ratio of this Friday's closing price to previous Friday's closing price is 1.15 or greater and is 1.40 or less. A sharp rise in stock prices is generally associated with rumors or speculation by the investors, or in anticipation of some good news.

(C) Elements of Sell Index

S-Index:

S-index occurs when the 10-week moving average line of a stock in question falls below the established high point (HP) by more than 1.50% (i.e., at the S-Index, the value of the 10-week moving average should be less than 0.985 times that average at the high point).

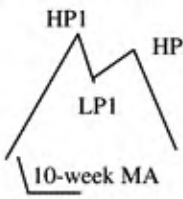
HP: It is a high point on a 10-week moving average line. A high point is considered established if the 10-week moving average line falls below 0.985 times that average at the high point (HP).

S-Index is only valid if the distance between the HP (high point) and the S-Index is 4 weeks or less. If the S-Index is invalid, no need to continue further.

Note: For stocks trading from $100 to $200, number of weeks indicated above for S-Index may be increased by one.

When two (or more) high points (HP1 and HP2) on a 10-week moving average line occur, refer to Figure 302(C) below to determine a high point (HP) to be used for a S-index.

Figure 302(C)



Note: HP1 > or = HP2

When LP1/HP1 > 0.985:

HP2 should be considered HP if HP2/HP1 > 0.995; otherwise HP1 is HP.

C-Index:

It is an index that confirms the S-Index. The S-Index is confirmed when

- 10-week moving average line falls below the 20-week MA line, **or**
- 20-week moving average line is on a falling trend or has begun to fall at least for the last two weeks.

If one of the above conditions is present with the S-Index, the S-Index becomes a SC-Index, and when one of the above conditions occur after the S-Index, the S-Index becomes a S/C-Index.

SC-Index:

SC-Index is only valid if the distance between the HP (high point) and the SC-Index is from one week to four weeks (including).

Note: For stocks trading from $100 to $200, number of weeks indicated above for SC-Index may be increased by one.

S/C-Index:

S/C-Index is only valid if it meets one of the following conditions:

- The distance between the HP (high point) and the S-Index is from 1 week to 4 weeks (including), and the distance between the S-Index and the S/C-Index is 4 weeks or less.
- The distance between the HP (high point) and the S-Index is 0 (zero) weeks and the distance between the S-Index and the S/C-Index is 3 weeks or less.

Note: For stocks trading from $100 to $200, number of weeks indicated above for S/C-Index may be increased by one.

SB-Index:

A stock can generate a SB sell-index as described in (a) or (b) below during its ongoing bull-behavior-broken (BlBB) condition.

(a) If and when the following both conditions are met:
- The ratio of Friday's Stock Price to its 30-week MA = 1.000 to 1.030
- The ratio of Friday's Stock Price to its 10-week MA < 0.900

(b) At the seventh *consecutive* occurrence of BlBB condition. *Note*: The ongoing BlBB condition should be considered *interrupted* by a single occurrence of bull-behavior (BlB) condition.

Definition of BlB and BlBB Conditions:

In order for the bull-behavior-broken (BlBB) condition to occur, a stock must first establish a bull-behavior (BlB) condition.

A bull-behavior (BlB) condition exists when

- Friday's Stock Price rises above its 10-week MA by at least 0.10 points, and if 10-week MA > 20-week MA > 30-week MA

A bull-behavior-broken (BlBB) condition exists when

- Friday's Stock Price falls below its 10-week MA by at least 0.10 points, and if:
  (1) 10-week MA > 20-week MA > 30-week MA and
  (2) Friday's Stock Price > Its 30-week MA

SF-Index:

SF is a sell-index if a ratio of this Friday's closing price to previous Friday's closing price is 0.85 or less. A sharp drop in stock prices is generally associated with some forthcoming bad news and/or unexpected damaging events.

SR-Index:

A sudden or sharp rise in the stock price may trigger a SR sell index. SR sell index governs over BC, B/C and BR buy indexes if they occur during the same week ending.

SR sell index occurs when all of the following conditions are met:

- The ratio of this Friday's Stock Price to Previous Friday's Stock Price > 1.15
- The ratio of this Friday's Stock Price to its 10-week MA > 1.55
- The ratio of this Friday's Stock Price to its 30-week MA > 1.50

Sometimes a BR buy index becomes a SR sell index if the above conditions exist.

ST-Index:

After a stock has established a bull-behavior condition (for definition, see SB-Index above), a stock may generate a ST sell index if:

(1) It closes on Friday (i.e., end of the week) below its 30-week moving average line, **and**
(2) The ratio of the closing price to its 10-week moving average is less than 0.95.

Other Selling Tips:

Besides the sell indexes discussed above, there are other reasons why a stock should be placed on a sell watch list.

In general, rise in the stock prices after a buy signal indicates strength. On the other hand, falling or erratic stock prices is an indication of weakness.

After a buy signal is generated, a stock should establish a bull behavior condition (explained above), or should show signs of doing it by prices progressively moving higher and then crossing its moving average lines upward within a reasonable time span (say 13 weeks).

If a stock makes a new high after a buy signal, it is an indication of strength. However, if a stock fails to make a new high after the last new high within a reasonable time span (say 13 weeks), it could mean weakness and possibly the end of its uptrend.

If a stock fails to demonstrate the strength or if it performs poorly as indicated above, it should be placed on a sell watch (SW) status for further evaluation. If the condition does not seem to improve, *stock must be sold.*

Sometimes take-over rumors or other street stories generate interest among investors causing sudden and sharp rise in stock prices. If this situation occurs, the stock should be placed on a sell watch (SW) status or should be sold. The methodology will not generate a sell signal in time, and waiting for such a signal could wipe out the gain generated by such rumors or stories. Refer to Example 4 on *page B-62* in Appendix B.

A mental stop loss (MSL) limit technique discussed in Section 404(C) titled "Manage Risk" in Chapter 4 should be used to preserve the gains or to cut losses.

(D) Index Requirements

The following Table lists several requirements that should be met by an index as indicated. When a buy-index or a sell-index meets the requirements indicated by "√" in the Table below, it is then considered a buy or a sell signal. If it does not meet the requirements, the signal should be considered invalid.

Require -ments	B	BC	B/C	BR	S	SC	S/C	SB	SF	SR	ST	MSL
A	√	√	√	√								
B						√	√	√			√	
C						√	√	√			√	
D		√	√	√								
E		√	√	√								

Requirement A

Index	Requirements
B	1. Friday's Closing Price > 10-week MA, and 2. 10-week MA line should be rising
BC or B/C	1. Friday's Closing Price > 10-week MA, and 2. 10-week MA line should be rising, and 3. Ratio of Friday's Closing Price to its 10-week MA < 1.35, and 4. Relative price strength (RS) is at least 35 & rising **or** is > 55, see footnote (a).
BR	1. Ratio of Friday's Closing Price to its 10-week MA < 1.35, and 2. Ratio of Friday's Closing Price to its 30-week MA > 0.80, and 3. Relative price strength (RS) is at least 35 & rising **or** is > 55, see footnote (a).

Footnotes:

(a) If this condition is not met, stock should be placed on a buy watch (BW) status. Buy watch status changes to buy if one of the following conditions occurs within a few (say 10 to 13) weeks:

1. The relative price strength (RS) begins to rise and is at least 35 provided that Friday's closing price is (or has been) above the 10-wk moving average line, **or**
2. A bull behavior condition is established by the stock consecutively for two weeks, **or**
3. The stock has recently made a 52-week new high or it appears to be ready to make one.

Requirement B

A sell index (SC, S/C, SB or ST) which occurs during any of the following market conditions should be placed on a sell watch (SW) status unless the stock is trading at PE greater than three or more times that of S&P 500 Index:

1. At or very next to a 52-week new high
2. With the existence or occurrence of a bull behavior condition
3. Just after a "LP" on the 10-week moving average line (which generally indicates the possibility of an impending buy signal)
4. When the relative price strength (RS) is greater than 85

Requirement C

During an advancing trend, stock generally establishes new highs after a new high. When a stock makes the first and the second 52-week new high, there is a temptation among investors to take profits. As a result, a sell index may be generated by the system. Therefore, a sell index (SC, S/C, SB or ST) should be considered valid if one of the following conditions is met:

1. Sell index occurs after the ninth week from the first new high, see Note (a).
2. Sell index occurs after the fifth week from the second new high, see Notes (b) and (c).

Notes:

(a) If new highs occur during consecutive weeks, then count the number of weeks from the first new high in such occurrences.
(b) In order to determine whether the new high is second, third, etc., there should be at least one week gap between the occurrences of new highs.
(c) If the second new high occurs within five weeks of the first new high, Condition 2 governs over condition 1. For example, refer to Table 302A, Example 7 in Appendix B.

Requirement D

During a declining trend, stock generally establishes new lows after a new low. Stock may generate a buy index during its technical rally. Therefore, buy index (BC, B/C or BR) should be considered valid if one of the following conditions is met:

1. Buy index occurs after the ninth week from the first new low, see Note (a).
2. Buy index occurs after the fifth week from the second new low, see Notes (b) and (c).

Notes:

(a) If new lows occur during consecutive weeks, then count the number of weeks from the first new low in such occurrences.
(b) In order to determine whether the new low is second, third, etc., there should be at least one week gap between the occurrences of new lows.
(c) If the second new low occurs within five weeks of the first new low, Condition 2 governs over condition 1.

Requirement E

Except as noted below, a buy index (BC or B/C) is generally not valid within twelve weeks and a BR index within six weeks of SC, S/C, SB, SF and ST sell signals including SC and S/C repeat sell signals. For the application of requirement E, sell watch (SW) status assigned to any of these sell signals (indexes) per Requirement B above should also be treated like a sell signal.

1. A buy index (BC, B/C or BR), which occurs within six weeks of any of the above mentioned sell signals, is valid if:
   - The stock has not made a 52-week new low during these five weeks, **and**
   - Friday's Closing Price > 20-week MA > 30-week MA, each by at least 0.10 points. (Note that Friday's closing price may be < or > 10-week MA.)
2. A buy index (BC or B/C), which occurs from seventh through twelfth week after any of the above mentioned sell signals, is valid (regardless of the 52-week new low) if:
   - Friday's Closing Price > 20-week MA > 30-week MA, each by at least 0.10 points. (Note that Friday's closing price may be < or > 10-week MA.)

Exception: Requirement E does not apply to stocks under $5.00.

(E) How Not-To-Miss Signals

Once a stock is selected for Form 302A and is followed to determine if a buy signal will be generated, or a sell signal will be generated, a question arises "how-not-to-miss" a buy or a sell signal.

Missing a buy or a sell signal could reduce your gain or increase your loss. For this reason, the following guidelines are developed:

For a buy signal—

- Watch 10-week moving average line on Form 302A for a formation of LP which could generate a B-index.
- Watch for an abrupt rise in the closing prices from Friday-to-Friday which could mean a BR-index.

For a sell signal—

- Institute a Mental Stop Loss (MSL) limit technique from day one and make a note of it in the remark column of Form 302A.
- Watch 10-week moving average line on Form 302A for a formation of HP which could generate a S-index.
- If a stock establishes a bull behavior, watch for a SB or ST index.
- Watch for an abrupt fall in the closing prices from Friday-to-Friday which could mean a SF-index.
- Watch for an abrupt rise in the closing prices from Friday-to-Friday which could mean a SR-index instead of a BR-index.

It would be a good idea to make a note of any of the above conditions if and when occur and review them at the end of each week in order not to miss a buy or a sell signal. It happened to me and it can happen to anyone. Proper recording of indexes and signals is therefore very important.

(F) Recording Indexes & Signals

Form 302A on page 3-32 may be used for calculating 10-, 20-and 30-week moving averages to determine a buy or a sell index, and then a buy or a sell signal if and when an index meets the applicable requirements listed in sub-section (D) above.

The following Table shows the method of recording them on Form 302A:

Index (a)	Index Conditions (a)	Require-ments (b)	Refer to Form 302A (Table 302A)		
			Index Column	Remarks Column (c)	Signal column
LP or HP	Met	----	LP or HP		
B or S	Met	Met	B or S		
BC or B/C	Met	Met	BC or B/C		Buy
SC or S/C	Met	Met	SC or S/C		Sell
BR	Met	Met	BR (d)		Buy
SF, SB or ST	Met	Met	SF, SB or ST (d)		Sell
B or S	Met	Not Met	B	RNM (e)	
BC or B/C	Met	Not Met	BC or B/C	RNM (e)	
SC or S/C	Met	Not Met	SC or S/C	RNM (e)	
BR	Met	Not Met	BR (d)	RNM (e)	
SF, SB or ST	Met	Not met	SF, SB or ST (d)	RNM (e)	
LP or HP	Not met	----	LP or HP	CNM (f)	
B or S	Not Met	----	B or S	CNM (f)	
BC or B/C	Not Met	----	BC or B/C	CNM (f)	
SC or S/C	Not Met	----	SC or S/C	CNM (f)	

Footnotes:

(a) Refer to sub-sections (B) and (C) above for Index Conditions.

(b) Refer to sub-section (D) for Index Requirements.

(c) Remarks or Observation column may be used for recording relative strength (RS) rank numbers from stock tables in *Investor's Business Daily* and other pertinent information mentioned in footnotes (e) and (f) below.

(d) Only the first occurrence of BR, SB, SF and ST should be considered & recorded.

(e) RNM = Index Requirements are Not Met. For example, A/RNM means requirement 'A' is not met.

(f) CNM = Index Conditions are Not Met.

(G) Commentary

The stock buy and sell methodology by definition cannot generate a buy signal at the bottom or a sell signal at the top. Buy signals are generated on the way up and sell signals are generated on the way down. Note that occasionally the methodology will create a loss situation. Refer to examples in Tables 302A in Appendix B.

We, as investors, prefer to buy at the bottom and sell at the top, not knowing where the bottom or the top is. When a buy signal is received, we tend to apply the common logic that if we didn't buy it when the price was low a few weeks or months ago, why should we buy now paying few bucks more for the same. Such logic is against the principles of investing because nobody knows where the bottom is until it becomes a history. We should be only concerned with the upside potential of the stock.

Case in point, examples are Rite Aid, Mylan Lab and many more others. I missed them in spite of following them on Form 302A. This is how we would generally react and miss the upside move:

Rite Aid Corporation

Buy signal was generated by week ending 1/14/94 at $18.62 after the low of $15.38 week ending 9/24/93. If we applied the logic discussed above and didn't buy it, we missed the big upside move which carried the stock to $60 by December 1997.

Mylan Lab

Buy signal was generated by week ending 7/4/97 at $15.06 after the low of $12 week ending 4/11/97. If we applied the logic discussed above and didn't buy it, we missed the upside move which carried the stock to $24.50 within a few months. The sell signal was received week ending 12/12/97 at $19.38 (a whopping gain of over 25% in eighth months). A mental stop loss limit technique would have required to sell the stock between $21 and $22.

After the sell signal of 12/12/97, the stock generated a buy signal week ending 3/20/98 at $22.38 and a sell signal week ending 9/4/98 at $27.44. A mental stop loss limit technique would have required to sell the stock around $30.00.

As mentioned earlier, the system also alerts investors from getting deeper into loss situations. For examples, refer to Tables 302A in Appendix B.

SECTON 303
MUTUAL FUNDS

(A) Introduction

The purpose of this book is not to dwell on mutual funds in detail. Ample information on mutual funds can be found elsewhere (for examples, mutual fund companies, stock brokers, financial magazines, local libraries and book stores) and it is easily obtainable. Only what is relevant to the objective of this book is discussed.

Simply a mutual fund is a portfolio consisting of various stocks, bonds or money market instruments managed by professionals. When you invest in mutual funds, you own a small share of the fund's entire portfolio managed by professionals.

(B) Why mutual funds

All investments involve varying degree of risks. Generally speaking, the higher the risk, the greater the potential reward; by the same token, the lower the risk, the lower the potential reward. One way to manage the risk is to diversify the investments across the different classes of investments. In other words, the risk is much greater if the available capital is invested in one or two stocks of the same or similar industry class.

Mutual funds provide the benefits of a diversified portfolio of stocks, bonds, etc. to individual investors, and they give investors affordable access to professional management. Therefore, indi-

vidual investors, with limited funds, who cannot diversify effectively among stocks of different industries, should seriously consider mutual funds. Selecting a mix of different category of funds can help to build a well-diversified portfolio. Since some investments rise in value while others may fall depending on the general economical conditions, a well-diversified portfolio will help smoothing out much of the volatility in the market and lead to more consistent and reliable outcomes. For more on managing risk, refer to Chapter 4.

In spite of mutual funds managed by professionals, growth and safety are not guaranteed; they do incur losses at times.

Mutual funds are categorized by investment objectives, such as Growth, Growth & Income, Equity Income, Balanced, Sector (Specialized) and Small and Mid Cap Stock funds.

(C) Selection Hints

1. Type of Economy

Selection of mutual funds (stock, bond, money market, etc.) depends on the type of economy that lies ahead.

One type of fund does better at one time; it may perform poorly at other time. Performance is a measure of how well or how poor a fund has performed over a certain period of time in terms of average annual return. Past performance is one of the methods used for comparing various mutual funds. Since the past performance reflects the type of economy that existed in the past, it does not guarantee the same or better results in the future.

Therefore, one should not concentrate only on the past long-term performance history, but should also consider the most recent short-term (e.g., 1, 3, 6 or 12-month) performance figures. Short-term performance figures generally reflect the ongoing market conditions and it is likely that such conditions could prevail in the months ahead.

2. Size of the Fund

Small and large are relative terms. The general thinking is that if the fund is too small, fund cannot afford to hire the best manager; on the other hand, if the fund is too large it may lose the flexibility to move money in and out of the fund if and when economic conditions warrant. Thus, it is likely that a large fund is subject to decline more if the market takes a sudden turn.

3. Choosing Mutual Funds

There are no good or bad mutual funds per se. They are good if they make you money; they are bad if you lose money. So as an investor, you should not have a personal liking or disliking for any particular fund or a fund family. For example, just because you like bio-medical field does not necessarily mean that you should purchase mutual funds that primarily invest in bio-medical stocks. Your job is to sort out and find funds that hopefully can make you money.

If you look at the financial section of the newspaper, you may find there are as many mutual funds as there are common stocks. The list of mutual funds is getting bigger and bigger day after day. Therefore, it is becoming extremely difficult for any individual investor to choose with reason-

able certainty the few best funds from thousands of mutual fund choices on the market. Many of us simply don't have the time, expertise, or tools to analyze them.

Many investment advisory services and brokerage houses provide performance data on mutual funds and offer recommendations based on extensive research and study of the behavior of many mutual funds during a variety of market conditions. Subscribing to an investment advisory service specialized in offering buy/sell/hold recommendations should greatly ease the monumental task of choosing funds.

In spite of this, it is hardly possible to achieve optimum return on any investment because no one can with certainty predict the future trends. No fund is alike in performance and no one selection method can consistently generate maximum returns.

The following tips may be helpful in choosing funds from thousands of mutual funds:

Begin your preliminary selection from those mutual funds which are no load or low load funds. If you are trading with discount brokerage houses, such as Fidelity Investments, Charles Schwab and Company, Jack White & Company, Kennedy Cabot & Company-just to name a few. Consider those funds which are offered by them without any transaction fees. Certain load funds may be considered if their performance deserves merits over the no load or low load funds,

Mutual funds performance guide or directory which contains quarterly performance figures for 1-wk, 3-mo, 6-mo, 1-yr, 3-yr, year-to-date, etc., and other information available from the above mentioned discount brokerage houses or similar performance figures available from the financial newspapers will be helpful.

It is important to remember that past performance is not always a predictor of the future performance and it is no guarantee of future results. On the other hand, it would be a poor choice to consider mutual funds that have not established an above average performance in the most recent months. It is wise to go with the winners than to bet on the losers. However, there may be some funds with exceptional values outside the winning circle, but they are hard to find. Therefore, for better or worse, funds with high medium to long-term returns coupled with high short-term returns should be the first choice in the selection process.

The performance figures that are easily available from the financial newspapers can be combined in many ways to produce various methods for prioritizing mutual funds. No one approach will yield optimum results all of the time because the market conditions ahead may not be a duplication of the past. What works at one time does not necessarily work at other times. No matter how complex and meticulously we can devise a method, predicting a fund's future performance with 100% accuracy is impossibile. The simpler the method, easier it is to implement and monitor. As long as the same method is used through out, it should, in general, produce consistent results and will help to weed out the poor performers.

It is important to note that the investment returns do vary depending on the entry and exit levels (prices), not what the market has done or the returns reported by the mutual fund companies. That's why the entry and exit levels (prices) are very important to achieve maximum possible returns on any investment. **To achieve this goal, long-term buy and sell signals generated by the methodology should be used for entry and exit levels.**

In general, total returns depend on many factors, such as:

- Amount invested in each fund. It is not possible to optimize the investment; some funds may rise faster than the others. No one can predict funds which are poised to appreciate faster than the others with 100% certainty.
- Method of Selection: No one method seems to work best all of the time and therefore, it is not feasible to achieve optimum results all of the time.
- Type of funds included in the selection process.
- Market conditions and the public's choice of industry and market sector for investment.

All of the above should not mean that we should make investment decisions randomly. A need for a set of rules and a systematic approach in selecting funds, and later, monitoring and managing the mutual fund portfolio, cannot be over-emphasized.

The following step-by-step approach is one of the many approaches that may be used in selecting mutual funds using the 1-Wk, YTD (Year-To-Date) and 3-Yr % Returns (performance data) published in *Barron's*:

Step 1. Upon receiving a long-term buy signal, prepare a list of funds with the high 3-Yr returns and preferably with 3-Yr performance rank A or B. (Note: 3-Yr performance ranks may be found in the Mutual Fund Section of *Investor's Business Daily.*)

Tip: Selection may be made from no or low-load fund families that you are familiar with and have some knowledge about them. Just to name a few fund families, such as American Century, Dreyfus, Fidelity, Founders, Invesco, Janus, PBHG, Scudder, Stein Roe, Strong, T. Rowe Price, Vanguard that may be included in your list of selection. If sufficient number of mutual fund candidates is not found to meet your investment objectives (Growth, Growth & Income, Equity Income, Balanced, Sector, etc.), other fund families may be included in your selection process.

Step 2. List should be limited to no more than 24 funds.

Step 3. Record 1-Wk (= W), YTD (= YD) and 3-Yr (= TY) % return figures for each fund on the list. Compute the sum of M times W, YD and TY (i.e., Sum = M×W + YD + TY) and arrange the funds in the descending order of the sum. M equals the "month number" divided by 3. For example, if the month is June, then M = 6/3 = 2.

Step 4. Select the top six to twelve funds depending on the amount of money available for investment.

Tip: Before making a final decision, it is advisable to obtain a prospectus for more complete information on any fund that you are considering for investment. Toll free numbers for funds are given in the mutual fund section of Investor's Business Daily.

Step 5. Invest equal amount of dollars in each fund.

Step 6. Repeat the same procedure and adjust the mutual fund portfolio every six to twelve months. Also every twelve months, adjust the dollar amount so that each fund will have approximately the same market value.

(D) Investment Portfolio

Your mutual fund investment portfolio should include a mix of different category of funds to create a broadly diversified portfolio taking into consideration your investment goals, time frame (based on present and future anticipated financial circumstances), and tolerance for risk (an investor's personal ability and willingness to endure occasional moderate to sharp declines in the market value of his or her investment portfolio). A broadly diversified portfolio of mutual funds minimizes and spreads risk over a variety of market sectors. This approach will help to smooth out the volatility in the market sectors and lead to more consistent and reliable outcome.

The side effect of diversification is that it also spreads opportunity. You may not get rich quickly, but you may get rich slowly and sleep a whole lot better. However, be careful of over-diversification; the portfolio should be manageable.

It is very important to re-evaluate the portfolio mix periodically as you approach retirement age or if and when circumstances change, and to make sure that you are not over-diversifying the portfolio so that it would become difficult and time-consuming for you to monitor it on a regular basis. The main purpose of this exercise is to weed out the poor performers before they become losers.

(E) Buying Strategy

In general, you should not buy shares of a mutual fund just before the dividend (distribution) record date. Because under the current tax rules, the income tax will be due on those dividends which is the same money you just sent them to buy shares of a fund. This is called "buying a dividend." In other words, you have acquired a year's worth of taxable gains without actually taking part in them. Therefore, it may be wise to wait until after the dividend record date before buying shares of a mutual fund. Dividend distribution dates can be obtained by calling the mutual fund company.

On the other hand, when you sell shares of a mutual fund, you should be careful not to pay income tax twice on the same dividends if they are reinvested to buy shares of the same fund since the dividends are taxed the year they are received. Reinvested dividends should be added to the cost basis of the fund for income tax purposes. For details, refer to Section 305.

No one knows with certainty the perfect time for buying mutual funds. However, as a general rule, the best time to buy mutual funds is when the system has generated a long-term buy signal.

(F) Selling Strategy

Now you have invested your hard-earned money in mutual funds. Do not sit back and relax. Investments should be watched from day one.

The price (the principal value plus the investment return) of mutual funds do fluctuate with market conditions and mutual fund shares when redeemed, may be worth more or less than their original cost. Therefore, investment portfolio should be evaluated at regular intervals (for example, every three months, or every month if market conditions warrant) for making necessary adjustments to

meet your changing needs, to eliminate poor performers, and to add new funds that are expected to produce better returns in the coming months.

As a general rule, it is preferable to sell selectively or the entire portfolio as soon as a long-term sell signal is generated by the system. A sell action should be implemented as immediately as possible without any due regard to loss or profit. Never allow your emotions and feelings convince you otherwise from implementing the action generated by the system; most investors fail to do so.

SECTION 304
OPTIONS-SPECIAL SITUATION

(A) Introduction

It is assumed here that the readers have the basic understanding of the stock and index options and the risk associated with trading options. A booklet titled "Characteristics and Risks of Standardized Options" available from Chicago Board of Options Exchange or your broker will be helpful. Readers may also contact their brokers and/or financial advisors for more information.

Only simple call and put option trading strategies will be discussed here. It is more popular among many investors. More sophisticated use of option strategies is discussed elsewhere and is beyond the scope of this book.

Options are contracts that entitle, but do not oblige the holder to buy (i. e., referred to as call option) or to sell (i.e., referred to as put option) a specified stock, stock index, etc. at a specified price (striking price) within a specified period of time (i.e., before the expiration date of the option.)

For example, an XYZ (stock's symbol) December (expiration month) 40 (striking price) Call gives the buyer the right to purchase 100 shares of XYZ stock at a price of $40 per share, or a total price of $4000 before the option expiration date in December.

Options are highly speculative and are not suitable for all investors because of the inherent risk involved in trading options. Investors can lose money as fast as they can make while investing in options. Making money depends on how right the investor is in predicting the price of the underlying stock or index within the selected time frame.

Options lose value fast with the passage of time and/or when the price of underlying stock or index is going against the anticipated trend. When investing in options, becoming quick rich feeling must be avoided. Although, it is very hard to do; every one likes to make money fast. You can make money quickly in trading options if you are right in predicting the trend and the time frame within which the trend should occur.

Therefore, it is resolved here from the author's past experience that a mechanical option trading plan is needed, and that **it must be adhered to all of the time without due regard to emotion, hope, greediness, or other human involvement.**

Like any other investments, the use of disciplined approach for trading options cannot be overemphasized; it is your best friend. If the plan calls for closing the trade, even at a loss; it must be done without hesitation before a small loss becomes a larger loss. **Preservation of the capital as**

much as possible should be your prime objective; the second objective being not to become greedy when you have a profit.

When investor buys a call option, he or she expects the underlying stock or index to rise within the time frame selected by him or her. When investor buys a put option, he or she expects the underlying stock or index to fall within the time frame selected by him or her.

The price of an option consists of (a) Option's intrinsic value and (b) Option's time value. Option's intrinsic value is the amount, if any, by which an option is in the money (actual cash difference between the strike price and the current price of the underlying stock or index), where as time value of an option is the amount in addition to its intrinsic value, referred to as the time premium, or simply premium. The greater the market's volatility, the larger an option's (time) premium is.

Options that have intrinsic value are commonly referred to as "in the money," while options without intrinsic value are called as "out of the money."

Examples of "in the money" options are:

(1) If the OEX December 380 Call is offered at $9.00 when the OEX is trading at 385.00 then the intrinsic value of the OEX Call is 385.00–380.00 = $5 00 (in the money) and the time value (premium) of the Call is $9.00–$5 00= $4.00.

(2) If the OEX December 380 Put is offered at $9.00 when the OEX is trading at 375.00 then the intrinsic value of the OEX Put is 380.00–375.00 = $5 00 (in the money) and the time value (premium) of the Put is $9.00–$5 00= $4.00.

Examples of "out of the money" options are:

(1) If the OEX December 380 Call is offered at $3.50 when the OEX is trading at 375.00 then the intrinsic value of the OEX Call is nil (because 375 < 380, i.e., out of the money) and the time value (premium) of the Call is $3.50.

(2) If the OEX December 380 Put is offered at $3.50 when the OEX is trading at 385.00 then the intrinsic value of the OEX Put is nil (because 380 < 385, i.e., out of the money) and the time value (premium) of the Put is $3.50.

The premium of an option decreases as the number of days to expiration decreases, although not proportionately. The premium could be erratic because it is dependent upon the forces of supply and demand in the option market, and the volatility of the underlying interest and the market in general.

(B) Option-Trading Plan

Option trading plan consists of three parts:

1. Buy/Sell Signals

Details given in Chapter 5 will serve as nucleus for making all investment decisions when a short-term buy or sell signal (refer to Chapter 1) is received.

2. Option Trading Monitor

The purpose here is to keep constant surveillance of the market indicators to determine whether or not changes in the direction of the indicators are taking place which may ultimately influence the

price of an option, even though investor may be right regarding the general trend of the market, but could be wrong about the time frame selected for the option.

Once the option position is taken, start monitoring the market mood indicators described in Section 104, Chapter 1 using *Form 304B/Page1, titled "Market Mood Indicators-Trend Change Watch" on page 3-33*, and consider closing the position as soon as the indicators and/or signals dictate to do so.

Never think of accumulating options as the price declines with a hope of coming out even or making profit in the end unless the indicators and/or signals dictate to do so. This temptation must be avoided absolutely. Believe it or not, such strategy does not work. Be guided by the trading plan described here, you would be glad you did it. Refer to Case Studies included in Section 704 (Tables 704A & 704B in Appendix B) prepared using Form 304B.

The third most important aspect of the plan is the **option sell condition monitor** to help investors to determine when to sell the option regardless of loss or profit. The objective of the plan is to minimize losses, not to maximize profit. It is hardly possible to sell any stock or option for the top dollar.

3. Option Sell Condition Monitor

It is generally more difficult to close a trade than to open one. It's a fact of life; we must accept it.

Therefore, rules are developed to make the decision making process as simple and painless as possible. The rules are shown in a tabular form, for ease of reference, covering most conditions encountered in trading options.

Various conditions generating sell (close position) signals are listed in *Table 304(B)3 titled "Option Sell Conditions" on page 3-26.*

Use of *Form 304B/Page2, titled "Option Sell Condition Monitor" on page 3-34* to record daily closing data for determining when to sell (close position) option is recommended.

Case studies presented in Section 704 prepared using Form 304B show that the plan has greater chance for success if followed mechanically. As investors become familiar with the plan, they can add their own case studies for future reference.

(C) Option-Trading Tips

1. General

(a) Be cautious when investing in call or put options during:

- Tired bull or bear phase (see Sections 109 & 110 in Chapter 1) of the market.
- Third week of March, June, September and December (generally referred to as "triple witching weeks"). Fridays of these weeks, stock futures and index options expire causing unprecedented volatility in the market.
- Week before the long weekend.
- Week of major market holidays.

(b) Never set a target sell price on paper or in your mind. Be guided by the option sell condition rules. Some options will not perform the way you expect, while others may far exceed your expectations.
(c) When option is acting favorably, do not rush to take profit. Wait until the close of the day; review potential for additional gain before making a final decision.
(d) If sell condition for call option coincides with the market making new high, institute a mental stop loss limit technique. It is likely that the market could move higher.
(e) If sell condition for put option coincides with the market making new low, mental stop loss limit technique may be used if it is reasonably expected that the down-trend will continue.

2. Trading with S3 or S9 signals

(a) Call or put option position must be closed on or before Friday of the week whether or not option sell condition occurs.
(b) All sell (close position) signals should be considered as MC (must close) unless option sell condition 3 occurs.

3. Trading with all Other Signals

(a) During the bull market phase (see Section 603, Chapter 6):

Follow option-sell condition rules for call and put options. Mental stop loss limit technique may be used for call options.

Mental stop loss limit technique may be used for put options only in rare cases if the trend of indicators listed on Form 304B/Page1 (see page *3-33*) has changed or is changing to more and more bearish.

(b) During the bear market phase (see Section 603, Chapter 6):

Follow option-sell condition rules for call and put options. Mental stop loss limit technique preferably should not be used for put options.

Mental stop loss limit technique may be used for call options if the trend of indicators listed on Form 304B/Page1 has changed or is changing to more and more bullish.

4. Mental Stop Loss (MSL) Limit Technique

The question is—how not to miss future gains by closing the positions prematurely based on a signal generated by the Option Sell Conditions listed in Table 304(B)3?

People are generally bullish and are hesitant to sell, but are eager to buy more on any good news or any technical strength. Therefore, it is likely that a better chance exists to make money with call options than put options.

When the market conditions are favorable (for example, DJIA made a new high) or are becoming favorable (for example refer to condition 3 in Table 304(B)3, or if market seems to be advancing without hesitation), the following technique may be useful in order to maximize gains in call options:

- Consider closing 50% of the option contracts upon sell signal generated by the Option Sell Condition Monitor.

- Institute a mental-stop-loss (MSL) limit and **monitor the option prices on an hourly basis.** *(Note: Check prices every one-half hour if market begins to fall rapidly or a sudden fall is suspected.)* If the price falls below the mental stop loss limit during anytime of the day, the option **should be sold** without any delay and deliberation.
- Set the Mental Stop Loss (MSL) limit at 0.90 times OC.
- The mental stop loss limit, once set, should be upgraded with the prices advancing based on a daily closing values, but never be lowered with the declining prices. For examples, refer to option case studies CO6, CO7, CO12 and CO13 in Tables 700 in Appendix B.

5. Finally...

Before investing in options, make sure you have a written plan of action ready based on the rules described above, and that you are determined:

- to follow the plan strictly
- to follow the signal(s) generated by the Option Sell Condition Monitor regardless of loss or profit
- not to be influenced by any internal or external forces
- not to become greedy regardless of loss or profit
- not to seek opinion from others
- not to ignore option case studies illustrated in Tables 700 in Appendix B

Tips:

- *Before investing your hard-earned money which you have put aside for risky investment, such as trading in options, and in order to get a feel and understanding of trading index options based on the methodology discussed herein, it is suggested to do a few simulated trades on paper using paper money. Reminder: Option trading is very risky by nature.*
- *It is generally a good practice to avoid buying or selling options during the first and the last one-half hour of trading.*

To illustrate a typical human behavior involved in trading options, refer to case study CO9 in Section 704. Case study CO9 which demonstrates what could happen if you trade options based on logical assumptions. Briefly, it goes this way. Your option gained about 10% in value within the first day; system did not flash a sell signal. Next day your option lost most of the gain, and the third day it went into a loss territory. System had not yet flashed a sell signal. Within a few days, the loss amounted 50% or more and the system flashed a sell signal. You started wondering because of the gain you had on the first day and you hesitated to follow the signal. You drowned in the hope of recovery and kept waiting. Option kept losing its value day after day, and finally, you decided to sell at a loss of around 90%.

Table 304(B)3—OPTION SELL CONDITIONS

See Footnotes (FtNts.) & Nomenclatures below

Cond. No.	See FtNts.	Sell (Close Position) Conditions for Call and Put Options {See FtNts.: (a) & (b)}	Option Sell (Close Position) Signals — Option Time Spans							
			A	B	C	D	E	F	G	H
1	(c)	For any two days, but not necessarily in a row: If IC < (SP–X1orX2) for Calls; If IC > (SP+X1orX2) for Puts.	WC (c)	WC (c)	CC (c)	CP (c)	CP (c)	MC	MC	MC
2a		Indicators are unfavorable	WC	CC	CC	CP	CP	MC	MC	MC
2b		Signal(s) is unfavorable	CP	CP	CP	CP	MC	MC	MC	MC
3a		Indicators are favorable	HP	HP	WC	WC	CC	CP	MC	MC
3b		Signal(s) is favorable	HP	HP	HP	WC	WC	CC	CP	MC
4a		OC/OP > 1.34 & < 1.50 (for Call Option)	CC	WC	WC	CC	CC	CP	CP	MC
4b		OC/OP > 1.24 & < 1.50 (for Put Option)	CC	CC	CC	CP	CP	CP	MC	MC
4c		OC/OP > 1.49 & < 1.75	CP	CC	CC	CP	CP	MC	MC	MC
4d		OC/OP > 1.74 & < 2.50	CP	CP	CP	CP	MC	MC	MC	MC
4e		OC/OP > 2.49	MC	MC	MC	MC	MC	MC	MC	MC
5a		OC/OP < 0.41	CC	CC	CP	CP	MC	MC	MC	MC
5b		OC/OP > 0.40 & < 0.56	HP	WC	CC	CP	CP	MC	MC	MC
6	(d)	OC, TC or TP < EC or EP	CP	CP	CP	CP	MC	MC	MC	MC
7	(e)	OC = Any Value	HP	HP	WC	WC	CC	CP	MC	MC

FtNts.:

(a) If multiple sell conditions occur simultaneously, they should be considered in the order of MC, CP, CC and WC. For example, if CC and CP sell conditions occur, consider CP and ignore CC condition.

(b) If DJIA or OEX set a new high, sell condition CC becomes WC.

(c) If this condition occurs, it may lead to loss; consider signals seriously. If for any single day IC < (SP – X2) for calls and IC > (SP + X2) for puts, the signal becomes MC.

(d) For estimating values of call (EC) and put (EP) options, see equations 1 and 2 below. Option price can fall below estimated value during the day. This intra-day value should not be used for Sell Condition No. 6.

Eq. 1. Estimating Value of Call (EC) Options

$$EC = \frac{(NC - NP)IC}{IP(NC + K1)} \times K2$$

Eq. 2. Estimating Value of Put (EP) Options

$$EP = \frac{NC - NP}{IC} \left\{ \frac{IP \times OP \times K2}{NC + K1} \right\}$$

(e) Governs if none of the above conditions occurs.

Nomenclatures:

A to H = NC/8 = Option Time Span

CC = Consider Closing the position now. Review market mood indicators, exceptions and past case studies. Make decision to sell or hold. If in doubt, close position. Mental Stop Loss (MSL) limit technique may be used. Refer to Option-Trading Tips in Section 304(C).

CP = Close Position. Mental Stop Loss (MSL) limit technique may be used. Refer to Option-Trading Tips in Section 304(C).

EC = Estimated value of Call Option (see equation 1 in Footnote (d) above)

EP = Estimated value of Put Option (see equation 2 in Footnote (d) above)

HP = Hold Position

IC = Closing price of the underlying Index on a day under consideration

IP = Price of the underlying Index at the time when the option was Purchased

K1 = 0.25NC but not to exceed 10

K2 = 2NC/100 but not to exceed 1.00

MC = Must Close position regardless of loss or profit

MSL = Mental Stop Loss limit

NC = Number of Calendar days between buy date and option expiration date
= Option Time Length

NP = Number of calendar days from buy date to date (day) under consideration including

OC = Closing price of the Option on a day under consideration

OP = Purchase price of the Option

SP = Striking price of the Option

TC = Time value of Call options (applicable when IC > SP) = SP – IC + OC

TP = Time value of Put options (applicable when IC < SP) = IC – SP + OC

WC = Warning/Caution. Review market mood indicators, exceptions, and past case studies. Make decision to sell or hold. If in doubt, close position. Mental Stop Loss (MSL) limit technique may be used. Refer to Option-Trading Tips in Section 304(C).

X1 = 1.5 times the difference between IP and SP but not less than 10.

X2 = 2.0 times the difference between IP and SP but not less than 13.

SECTION 305
TRACKING THE INVESTMENT

(A) General

It is like anything else—when we buy a car, we maintain it as specified in the car manual; when we buy appliances, we follow manufacturers' recommendations, etc. However, for stocks, bonds, mutual funds, etc. investments, we don't receive a manual. So what happens:

- We invest and put it on shelf.
- We don't know what our investments are.
- We have no idea how our investment is performing relative to the market.

We normally assume or expect that the investments we own would perform well and rise in value day after day, month after month. Later, most investors, to their surprise, find out that the investment they thought was doing well, went sour.

Therefore, to resolve this dilemma, investors should develop a technique or a procedure to monitor the performance of each investment in the portfolio. Investors should cultivate this habit. It is preferable to do this on a regular basis, may be quarterly, monthly or daily if conditions warrant.

The purpose of such a procedure is

- To identify the weak and strong performers and to make necessary adjustments to the investment portfolio.
- To periodically reassess the risk inherent in owning stocks, mutual funds, etc. and to evaluate each investment from its potential for future gain or loss.

Don't rely on others to do it for you. It is your money. Remember a sound investment program requires a dedicated attention. It requires time, effort, and self-discipline. Therefore, one should not over-diversify the investment portfolio to a point that it becomes unmanageable.

(B) Investment Performance & Record Keeper

Here is a simple way of keeping a record of investment and, simultaneously monitoring the performance of various types of investments, such as stocks, mutual funds, etc. All it is necessary to evaluate performance relative to each other over the same time periods (for examples, at the end of 3 months, 6 months, etc.) by computing the percent changes in the values of each investment from the previous period which would help to identify the poor performers. This way, it eliminates the influence of the price paid for the stocks, bonds, or mutual funds. Average annual returns depend on the prices paid for the stocks, bonds or mutual funds, but performance relative to each other does not.

The most common measurement of performance of any investment is a simple or compounded average annual return expressed as a percent of capital investment. For relative comparison between various types of investments, it does not matter whether a simple or compounded average return method is used.

Record keeping is an important part of any investment process. Keeping a detailed record of all transactions can save the investor time and money. The cost of having someone or yourself to sort out the details at income tax time or when the investment is sold could be astronomical. If you are not willing to do this, don't invest.

The method should be simple and easy to use. *Form 305B on page 3-35* is designed to do both things, to keep record of investments and to evaluate relative performance of investments. Such records will also be helpful in preparing income tax returns when the investment is sold.

1. Terms & Notations:

C = Cost of Buying: It represents cost of initial investment including brokerage charges, if any, for buying stocks, mutual funds, etc.

O = Other Costs: It includes any taxable distributions (dividends, capital gains, etc.) **if reinvested**.

(Note: Distributions by the fund are subjected to income taxes, regardless of whether, the distribution is made in cash or reinvested in additional shares of the fund. If any portion of the taxable distribution is reinvested that amount is then included in the other costs which increases the cost basis of the investment for determining profits or losses for income tax purposes to avoid paying income taxes twice on the same distribution because the distribution is taxed the year it is received. Non-taxable distribution, referred to as return of capital, is not taxed the year it is received. It is used to reduce the cost basis, thus it is taxed when the investment is sold. On the other hand, if it is reinvested, it is not added to the other costs and thus, it neither reduces nor increases the cost basis. For more information, refer to appropriate IRS publications or contact your tax advisor.)

V = Market value of investment = No. of shares times the current price of the share, or the net amount received if the investment is sold.

Change in V (Ratio) = Change in V from the previous period "V" to current period "V" expressed as the ratio of current period "V" to the previous period "V".

D = Total distributions received since the date of trade that is **not reinvested**.

N = Number of months since the date of trade

2. Average Annual Percent Return:

It is the average annual percentage change of an investment over a specified period. It can be determined based on a simple percent return or a compounded percent return as illustrated below.

(a) Based on simple average method:

$$\text{Average Annual Simple Return (ASR) \%} = \frac{1200(V + D - C)}{C \times N}$$

(b) Based on compounded every six months:

Average Annual Compounded Return (ACR) %

$$= 200\left[\left\{\frac{V+D}{C}\right\}^{6/N} - 1\right]$$

(c) Based on compounded every twelve months:

Average Annual Compounded Return (ACR) %

$$= 100\left[\left\{\frac{V+D}{C}\right\}^{12/N} - 1\right]$$

3. How-to-calculate the average annual percent return from the total return T:

T = Total % return over a specified period, say 1, 3 or 5 years, used by a fund in reporting the total return which is generally equal to

$$100\left[\left\{\frac{V+D}{C}\right\} - 1\right]$$

In the following formulas, N represents the period in months (1 yr. = 12 mos., 3 yr. = 36 mos. and so on):

(a) Based on simple average method:

$ASR\ \% = 1200(T/N)$

(b) Based on compounded every six months:

$ACR\ \% = 200\{(1 + T)^{6/N} - 1\}$

(c) Based on compounded every twelve months:

$ACR\ \% = 100\{(1 + T)^{12/N} - 1\}$

Example: If T = 45.00 % (= 0.45) & N = 36 months, that is to say—an investment of $1 grew to $1.45 in 36 months (a gain of $0.45, i.e., 45% return on investment of $1 in 36 months), then the average annual percent return based on compounded every twelve months using formula (c) above is equal to:

$ACR = 100\{(1 + 0.45)^{12/36} - 1\} = 13.18\ \%$

and the average annual simple return using formula (a) is equal to:

$ASR = 1200(T/N) = 15.00\%$

Note: Keep in mind that a fund's average annual return is a compounded average return calculated at the end of each year. In the example above, average annual return is 13.18 % over a period of 3 years.

Stocks Review/Selection—Work Sheet

Form 301A Page:

From Barron's dated

Ref #	Company Name	Tick Sym	Exch	52-week High	52-week Low	Div. Yld	PE	Last Price	Earnings Interim or FY	Earnings Year ago
A										
B										
C										
D										
E										

From S&P Stock Guide for the month of

Ref #	No. Inst	Shs (000) Hold	Cash	Curr. Asset	Curr. Liab.	LT Debt	Common Shs (000)	FY Earning Curr.	FY Earning Last	% Hold by Inst	Curr. Ratio
A											
B											
C											
D											
E											

	Standard & Poor's Stock Report					
Ref #	Page Dated	Sum of 5-Yr EPS	EPS Qt vs. Qt	Curr. Ratio	% LT Debt of Capital	Comments
A						
B						
C						
D						
E						

Ref #	Page # Dated	Value Line Investment Survey Overall Opinion	RS (a)	Remarks
A				
B				
C				
D				
E				

Legend: D=Deficit; L=Non-recurring loss or charge included; E = Estimated; P = Preliminary; N/A = Not Available. (a) RS from *Investor's Business Daily*.

Remarks:

Stock: ....

Form 302A Exchange: .... Page: ....

19...	Row	Stock	10-wk	20-wk	30-wk	52-week New		S&P... VL... (available)	Stock		Sig-
WkEd	#	Closed	MA	MA	MA	High	Low	Observation	Index	Remarks	nal
	1										
	2										
	3										
	4										
	5										
	6										
	7										
	8										
	9										
	10										
	1										
	2										
	3										
	4										
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	4										
	5										
	6										
	7										
	8										
	9										
	10										

Legend: BIB = Bull Behavior condition; BIBB = Bull Behavior Broken condition; RS = Relative Price Strength

FtNts.:

Form 304B/Page1—MARKET MOOD INDICATORS
Table 704
OEX Option Trading
Week End.: ..... **Signal:** ..... Comments: .....

CASE STUDY# .....
Call/Put: ..... **Page:** .....

Instructions:

If and when appropriate, this form should be used to monitor market mood indicators when trading options; **change in trend** of indicators may detect, in advance, any forthcoming change in market direction which might influence the option values adversely.

Form 304B/Page1 MARKET MOOD INDICATORS—**Trend Change Watch**

Indicators (Refer to: Section 104)	WkEd (Date)	WkEd (Date)	WkEd (Date)	WkEd (Date)	WkEd (Date)	WkEd (Date)
M1: Wk to Wk change vs. Market						
M2: OB/OS Conditions						
M3: Cum-Sum (Ics) trend vs. Market						
M4: Has DJIA X'ed up/dn its MA lines?						
M5: Change in DJIA MA Trend						
M6: Change in Pt/Fg trend						
M7: DTSVO new high or new low						
M8: MC, Rose or Fell						
M9: Momentum Trend status						
SSR FtNt. (a)						
Buy/Sell Signals						
Exceptions						
Warnings						
Overall short-term market condition &/or Action						

FtNts.: (a) Low SSR does not always mean bullish, refer to Section 102(E).

Form 304B/Page2—OPTION SELL CONDITION MONITOR
Table 704
OEX Option Trading

CASE STUDY# .....
Call/Put: ..... **Page:** .....

Market Phase/Section 603: .....
Week End.:..... **Signal:**..... *Comment*: .....
Zone:.... MC:..... DJIA:..... OEX:..... .....

Sug.Action:..... Exp.Mo:..... **SP(*)**:..... Exp. Date:.....
Buy Date:..... Time: ..... OEX(**IP**):..... Opt.Price(**OP**):.....

(*) Difference between **SP** & **IP** preferably should not be more than 10.
NC = No. of calendar days (40 min.) between buy date and date option expires =..... K1 = ...
Time Span = A thru H are 8 time-spans, each approximately equals NC/8 = ... K2 = ...
NP = No. of calendar days from buy date to date under consideration (including).

Form 304B/Page2 **OPTION SELL Conditions MONITOR**—Ref. Section 304(B)

19... Date	NP	NC – NP	Time Span A→H	Index closed IC	Option close OC	TC or TP	EC or EP (Eq:....)	Ratio OC / OP	Sell Cond.	FtNt. #	Action	Remarks
	---	---	---			---	---	---	---		---	
	0										Bot	
	1											
	2											
	3											
	4											
	7											
	8											
	9											
	10											
	11											
	14											
	15											
	16											
	17											
	18											
	21											
	22											
	23											
	24											
	25											

FtNts.:

Form 305B—INVESTMENT PERFORMANCE & RECORD KEEPER

(Refer to Section 305 for details)

Account-Name(s)/Type: Account with: Tel. #: Page:

Bot or Sold	Account with and Description of Stocks, Mutual Funds, etc.	Trade Date or (As of)	Cost of Buying = C FtNt. (a)	Distribution [Reinvested? FtNt. (b)] Ordinary Div.	Cap. Gain	Non-taxable	Other Costs? = O	No. of shares	Share price	Market Value = V	Annual Simple Return (ASR)	Change in V = Ratio	Remarks

FtNts.: (a) Cost of buying "C" includes all brokerage charges, if any for buying.

(b) Asterisk* after the figures means distribution is not reinvested.

❖ *To stick with the methodology is the key and it is the toughest part of investing. Follow all the rules all of the time* ❖

Chapter 4

STRATEGIC TRADING DISCIPLINE

OBJECTIVE

At the conclusion of this chapter, you will be able to understand the importance of self discipline. One has to practice to implement the principles listed herein to become a successful investor. Reading this chapter more often will help to break the old habits.

OVERVIEW

This chapter covers many useful disciplines, but not all expected of the investors to generally succeed in the market. It is divided into following Sections:

401 -Think Like A Wise Man
402 -Be Like A Traffic Engineer
403 -Act Like A Pro
404 -Trading Wisdom
405 -Investment Strategies
406 -Be An Observer

Section 401
Think Like A Wise Man

- The forces of supply and demand generated by the public (investors) create market trends. To question the trends or to find logical reason to convince one's own belief otherwise is merely a stupidity and waste or time.
- Gaining understanding about the market trends is far important to winning the market game than attempting to predict future prices of the market indexes or the individual stocks.
- Trying to predict individual stock prices without forecasting the market averages is like putting the cart before the horse.
- To buy or sell in anticipation of a reversal in the market trend is foolish. Never, ever try to get ahead of the market. To do so, is a fatal mistake.
- If you don't see your way clear, do nothing. In the stock market, you can't create an opportunity, but you can take advantage of one that exists.
- Never invest in something that you don't understand; that promises you get rich quickly; that requires you to invest on-the-spot; it is like stepping into an uncharted water.

Section 402
Be Like A Traffic Engineer

- Job of a traffic engineer is to design traffic signals tailored to meet the traffic and road conditions for a smooth flow of the traffic. Properly installed traffic signals helps to prevent accidents and traffic jams. Similarly, the job of an investor is to device a plan or a chart by which the investment would be protected from market downturns. The charts are like traffic signals for the stock market investors. They can indicate the condition of the market ahead and alert the investors like the traffic signals.
- Without a plan or a chart, it is easy to get lost in the wilderness of information highway. We could easily become victims of excitement, tips, gossip, fears and wishful thinking.
- Charts will clearly indicate whether the forces of supply or demand are in control, and they function like the traffic signals on the roads, warning the travelers about the danger zones ahead.
- Charts, in general, will clearly indicate the inception and ending of the market trends like the traffic signals which indicate the beginning and ending of the work zones. Charts will give all the news in advance and they reveal the facts without comment or explanation.
- Once the plan is formulated, we must develop courage and conviction to stick with it. We must divorce ourselves from all habits and thinking that fail to advance the principles involved.
- Therefore, we should not invest until a buy signal is generated and should not sell until a sell signal is generated by the methodology discussed in this book.

SECTION 403
ACT LIKE A PRO

- Knowledge and experience by themselves are never of any value to anyone unless they are put into action.
- The mere possession of good tools (knowledge of market averages) does not make a good mechanic (investor), but its skillful application that makes us successful investors. Its skillful application should be based on a well thought out plan of action.
- Trade with the trend; don't try to swim against the current. Market trends are never wrong; opinions often are.
- Buy that which is showing strength and sell that which is showing weakness.
- Don't expect all of the decisions to be perfect. Therefore, learn to cut losses quickly when your selection or timing was not right (i.e., learn to accept the fact that buy and sell signals will be wrong sometimes.)
- Be patient. If a trade is missed, look elsewhere for an opportunity.
- Be patient. Once a trade is in place, allow it time to develop, but remain alert. When an investment posts gain, review the potential for further gain before deciding to sell.
- Go over the list periodically. Retain investments that perform well and consider selling those that have performed poorly. The tendency of many inexperienced investors is to sell investments that do well and hold those showing losses.
- Be impatient. When investment performs poorly, don't hang on too long if there is a potential for further loss. Be willing to cut loss before it grows into a bigger one. Small losses and quick losses are the best losses. Ban all wishful thinking. Don't be greedy and emotional.
- Emotions & Feelings. Don't let human emotions or feelings about your favorite stock or the market in general govern your actions. But remember, emotions and feelings do have tremendous inherent power to empower you in making right decisions. Therefore, be aware of them and remain alert.
- Never, ever under any circumstances add to a losing trade. To do so is throwing good money after bad money.
- Obey all the rules all of the time. Let the methodology be your guiding light.

SECTION 404
TRADING WISDOM

(A) Investigate Before Investing

Most of us have tendency to believe and act upon based on what we hear without investigating and separating facts from fictions. Because collecting facts require time and effort. It requires asking right questions to gather facts. Believe it or not it is well worth doing so before putting your sav-

ings to stake and the whims of the market. If the situation is not properly thought out and analyzed based on facts, **we will generally end up spending more time and effort later when the investment goes sour**.

To say you don't have time to investigate or to do your homework before investing should not be an excuse. Not only it will cost you time, but it will drive you nuts with guilt feelings, stress, anxiety, fear, etc. which will disable you from making appropriate decisions.

However, it is equally important not to waste time and effort in collecting and analyzing data or information irrelevant to the situation. All that does is clutter your mind and create confusion when you try to separate facts from fictions. Don't get buried under the over whelming information, be selective.

(B) Don't Be Opinionated

Don't try to find reasons or to formulate opinion about the market, and what it should do when it moves against your belief or imagination. It's merely a waste of time and effort. Let the market trends (buy and sell signals discussed in Chapters 1 and 3) govern the course of your action.

(C) Manage Risk

Risk is an inevitable part of investing whether the investment is in stocks, mutual funds, bonds, real estate or commodities. The key is to understand the potential risks and learn to manage them in order to preserve the capital and capital appreciation.

Before we begin to learn "how to manage risk," we should be aware of certain personal friendly enemies that must be conquered. They are pride (means we like to enjoy owning investment and falling in love with it), ignorance (we forget why we are investing) and greed (means like to become rich quickly by hanging in there to squeeze more); in short it is "PIG". If we get attached with them, they will surely wreck our plan of managing the risk by preventing us from taking actions if and when warranted by the methodology.

Risk does not begin after fund is invested; it should be strategically evaluated prior to committing funds. Before investing, we must understand the ways we lose money and the ways we can make money. Therefore, the process of managing risk should begin before we consider investing our hard-earned money.

If we make bad investment decision, we automatically inherit built-in risk and managing the inherited risk becomes an acute problem. **It is therefore utmost important to investigate before investing to avoid investments which may have built in risk.**

The question is how do we do to not getting into making bad investment decisions when it relates to investing in stocks and mutual funds. The main thrust here is to avoid risky or shaky investments and to select the investment that is in line with the ongoing trend. Even if how carefully the investment is selected, the time for committing funds may not be right. **We should by all means avoid buying it just before it is setting for a declining trend.**

Sometimes we are influenced by media, friends, tips, information that we read in articles and advertisements which present lucrative performance figures about a specific stock or a mutual fund. The temptation to invest in such investments having very impressive past returns is hard to hold of because we like to get rich quickly. It is generally too late when we hear or read about it. **The question to ask is how much room has left in it for further price appreciation or has it reached its maximum price appreciation**.

Investors are generally guided by the past performance. Past performance of any specific investment, however, does not guarantee the same or better returns in the future. Past performance, however, do help to judge an investment about what it can deliver if the same performance does continue in the months ahead. **Since we are sandwiched between the past and the future, we should learn to live in the present utilizing the past performance as a guide and looking ahead with caution in the future to manage the risk better**.

Answers to the following questions which can be derived by tracking the issue in question on Form 302A (see Chapter 3) will shed some light on the above concerns:

- When and how was the buy signal generated?
- Is it near generating a sell signal?
- How many weeks has it been from the last 52-week new high?
- Is the bull behavior broken? Is it swaying between the bull and the bear behaviors?
- Is it trading below its 30-week moving average?

If we follow and learn to utilize the methodology discussed in this book, we may be able to avoid buying a stock or a mutual fund that is just about to top out. It's well worth the effort to spend couple of hours in collecting the data needed for Form 302A before committing fund, no matter how small amount it may be, in order not to be sorry later.

We invest because we want to make money. However, we fail to manage the process by which we intend to achieve this goal. If we disciplined ourselves to learn and implement the various strategies discussed in this book, the goal can be attainable.

When our investment goes sour, we continue to sit on it and take the easy path of procrastination. Do you stay in your house if your house is on fire? Definitely not. You get out of the house immediately, and then, you take immediate action to extinguish the fire as quickly as possible. Same approach we should take when our investment goes sour. We can always buy back the issue we sold if the conditions later dictate to do so.

The basic mistakes we make when managing the risk are:

1. We fail to cut loss until it gets bigger.
2. We fail to guard profit and allow it to grow.
3. We allow our profit turn into loss.

Comment: We generally tend to accumulate losses due to our greedy attitude and fail to cut losses or protect whatever gain is left. We could learn something from the following hypothetical case study:

(a) Our stock on January 2, 1997 was closed at $12.00 (i.e., annual percent return of 20%.). We bought the stock at $10.00 on January 2, 1996.

(b) On July 2, 1997, stock closed at $14.00 (i.e., annual percent return of 33.33% in the last six months.)

We felt very good seeing the return going up and believed that the past performance would continue in the future. Although we knew that the past performance was not always a predictor of the future, but we relied on it anyway. We did not have a well-defined plan of action and we did not implement the techniques for managing the risk discussed in herein.

(c) On January 2, 1998, stock closed at $9.00 and we incurred paper loss. Stock, thereafter, kept declining and finally, it was sold for $5.00.

Question: *Why we don't sell when we should. Because to sell or not to sell is the toughest decision. But why? Because we fear of missing out on the further gain, we become greedy and emotional. And therefore, we procrastinate until it becomes unbearable. We then sell at loss.*

4. We fail to diversify our investment adequately to guard against the volatility in any sector of the market and any unexpected unforeseen events.
5. We tend to invest all of our funds at one time.

The technique used by many investors to cut losses and guard profits is to set a trailing mental stop loss (MSL) limit of 10-15% below the daily closing price and updating it to a new mental stop loss limit as the price advances. When the investment hits the mental stop loss limit on a daily closing basis, investment should be sold the next trading day without hesitation even though the market in general is still rising. We must learn to overcome the greed. This is easier said than done.

However, it can be achieved if we don't get drowned in our hopes, expectations, emotions, feelings and greediness, and if we learn to discipline ourselves to use our experience and knowledge in our favor.

When a mental stop loss limit strategy is deployed, it must be followed religiously. Since the trailing mental stop loss limits are determined based on the closing prices, intra-day price fluctuations should be ignored in making sell decision. This is one reason why it is not proper to place a stop (loss) order with the broker. **Patience and a disciplined approach are the keys to master this technique.**

If a stock has made a new high, it may be used in determining a mental stop loss limit. This may be sometimes advantageous for highly volatile stocks to guard profit against sudden fall in prices.

However, it is not uncommon for a stock to turn-around and rise after it has been sold at or below the MSL limit. **The MSL limit technique serves as a safety switch in the event the stock continues to decline.**

Tips:

- Institute a trailing mental stop loss limit from day one. Remain alert if the price falls to 10% and should sell if the price continues to deteriorate.

  For examples, stocks with high PE ratios (say, PE ratios three or more times that of the S&P 500 Index) *should be sold without any hesitation* if the price (on a daily closing basis) falls to below 10% and, from 12.50% to 15.00% for other stocks depending on the market conditions.

  MSL limit should not be used for stocks whose dividend yield exceeds the 13-wk T-bill and 3-yr Treasury Note rates.

Never ever lower the trailing mental stop loss limit with the falling prices, but update the trailing mental stop loss limit upward with the prices advancing. Monitor the stock using the buy and sell methodology discussed in Chapter 3.

- Remember that small losses are better than large losses. However, too many small losses are as bad as large losses. Therefore, one must stick with the methodology of buying and selling stocks discussed in Chapter 3. *One of the many examples was Green Tree Financial, a fast growing company with accelerated record of earnings year after year, generated a sell signal by week ending 11/14/97 at $33 based on the methodology. (Note: With the mental-stop-loss limit technique, stock would have been sold around $42 on 10/27/97 based on MSL limit of 43.97 (MSL = From 0.875x50.25 = 43.97 to 0.85x50.25 = 42.71) determined using the new high of 50.25 set during the week ending 10/17/97 or MSL limit of 43.48 based on the closing price of 49.69 on 10/10/97).* At the time, Standard & Poor's report as well as the Value Line Survey report both looked very positive and appealing; the PE was very low compared to the general market averages. Result –The stock was trading around $20 by end of January 1998.
- How do we guard against share prices falling sharply on a single day? We can't. Even the methodology of buying and selling stocks discussed in Chapter 3 would not warn us ahead of the time by generating a sell signal. Therefore, it is suggested that when you own a high PE ratio stocks you should not wait for the system to generate a sell signal. Because it wiould be too late. Such stocks should be sold when you believe that it has reached its potential, or price has fallen below the MSL limit.

For examples:

(1) Cendant's share fell nearly 50% on April 16, 1998 (Stock closed @ $19.06 on April 16, 1998) because of the news that the reported earning would be cut by $100 to $115 millions, or 11 to 13 cents per share, owing to apparently deceptive bookkeeping. The PE ratio of the stock during the previous week was around 85 and the PE ratio of S&P 500 index was around 28 (PE ratio: Stock to S&P 500 Index = 85/28 = 3.04). The stock made a new high of 41.75 a few weeks ago and the mental stop loss limit was set at 10% (i.e., MSL = 0.90 x 41.75 = 37.57 or MSL set at 37.25 based on the closing price of 41.38 on 4/6/98). On April 9, 1998, the stock closed @ $37 below the set MSL limit requiring it be sold on the next trading day (i.e., on April 10, 1998). The stock began falling and by September of 1998, it was trading around $10-15.

(2) Criimi Mae's share closed at $1.31 week ending 10/9/98 since the company announced its intention to file bankruptcy. The stock traded around $13.00 to as high as $18.00 between 1/10/97 and 8/21/98. The dividend yield was around 9.00% which was greater than the 13-wk T-bill and 3-yr Treasury Note rates. The methodology discussed in Section 302 in Chapter 3 generated the first sell signal at $15.94 week ending 10/10/97, the second sell signal at $15.00 week ending 11/21/97 and the third sell at $6.94 week ending 10/2/98. If we had own the stock, we would have sold the stock at $16.00 following the first sell signal generated by the methodology. No buy signal was generated since the first sell signal of 10/10/97. *(Tip: Regardless of how high the current dividend yield is, acting per the*

signal generated by the methodology should be the prudent choice. Sell signal could indicate the possibility of cutting dividend by the company or some other troubles ahead.)

The important thing to remember is that there is no easy way to eliminate the risk entirely. Under one economic scenario, investing in stock funds may be the best, whereas in another market cycle, bonds or money market funds may perform well. However, the risk can be minimized by spreading the investment across different classes of investment that is generally referred to as diversification. I relate diversification with foods we eat. We cannot get the nutrients we need to support our life by eating just one kind of food daily. We need to eat varieties of good foods (not junk foods) to maintain good health. Similarly, in order to build a risk resistant investment portfolio, we should invest in different classes of investment instruments.

Mutual funds offer built-in diversification because they invest across the range of securities and industries. Thus investing in mutual funds of good qualities will spread the risk in a way that would be difficult for individual investors to achieve on their own. By owning a mix of varieties of good quality mutual funds, one automatically reduces the vulnerability to a downturn in any one market segment.

A diversified investment portfolio spreads the risk over a variety of market sectors, thus lowering the overall effect of risk on investment. Since no one knows for sure which class of investment (stocks, bonds, money market funds, etc.) will perform better in the months or years ahead, it makes sense to spread funds among different classes of investments.

Therefore, investing in a selected few different classes of investments should be considered in order to reduce the inherent risk of being wrong. A well-diversified investment portfolio containing good quality of mutual funds will have a high degree of survival rate from any one negative economic development and will protect from the full brunt of a market decline. It should include a variety of investment products, such as stocks, bonds, mutual funds, money market accounts and certificates of deposit. It can provide a balance between income and growth, maintain liquidity and help to reduce risk.

The side effect of deploying this strategy is that it also spreads opportunity. One may not get rich quickly, but one may get rich slowly and sleeps a whole lot better.

Sometimes when a particular investment appears to be very attractive, it is very hard to resist temptation of putting all the eggs in one basket. If so, stop and think, evaluate risks versus rewards, and ask questions "what if" before investing.

To reduce the risk further, a strategy called "dollar-cost averaging" may be used. That is, to invest a fixed amount of dollars at regular intervals for the longhaul. This strategy eliminates the guesswork of trying to figure out the best time to invest. For more details, refer to Section 405(C). **The tip is don't tie up all of your moneys in one single venture at one time only.**

The methodology described in this book will tell us when to step aside or when to remain invested. The plan is like an insurance, for which we have paid the premium, by investing our time and effort in developing buy and sell signals and putting them to work. **We should not procrastinate.**

A well-designed plan of action will help us to make appropriate decisions in managing the investment portfolio in order to minimize the overall risk.

(D) Failure To Accept Loss

Human tendency is to cash in the best performers and hold on to weak performers. Because we are generally hesitant to accept loss and prefer to take the rear seat and hoping that a weak performer would soon gain in value. Does this really happen? Please remember it rarely happens.

On the other hand, holding on to our best performers too long to squeeze out a little more profit can also drown us. **Remember that greed is a wild animal without a steering wheel and one must stay away from it.**

The best approach is to strictly follow the sell signals generated by the methodology discussed in this book. We should learn to stick with them to harness our emotions.

(E) How To Lose

Some of the ways to get trapped into losing propositions based on my experience are:

- Advertising: Telling your friends and relatives about your investment activities.
- Attitude: Unwilling to admit the mistake and take appropriate actions to rectify.
- Borrowing: Risking borrowed money based on tomorrow's promise.
- Cheap & Bargain: Buying something because it is cheap and seems a real bargain, or because it has fallen in price and is now cheaper than it was a few months earlier when you were considering for adding it to your investment portfolio.
- Greediness: Not selling if and when indicated by the plan because you are afraid to take loss or you want to squeeze a little more profit or have desire for huge profits to get rich quickly.
- Insistence: To remain fully invested all of the time.
- Over-trading Addiction: To trade more frequently with the hope of getting rich quickly.
- Placing a Limit Order: Missing or losing a profitable trade by one-eighth of a point.
- Temptation: Rushing to buy because of fear of missing a big chance. Remember haste is waste and hurrier you go, behinder you get.
- Tips & Rumors: Acting on tips, rumors, street stories, inside information, or recommendations from friends, brokers, advisory services, etc. (These are generally stale like left over foods, or have different objectives—see case studies in Section 702.)
- Under Pressure: Buying or selling under pressure from your broker or friends.
- Investing without Investigating: It is like stepping into unknown water.

Time-to-time, financial newsletters, magazines or newspapers carry advertisements and articles (in many instances, primarily written for promotion) which feature attractive and convincing information about stocks (or other investments) that seem to promise a spectacular rate of returns. Many investors fall into such traps and invest heavily in order to get rich quickly. In general, investors who buy such stocks, later find out themselves in a deep loss. Therefore, sometimes it's hard to tell who is on our side. In such advertisements, only the most attractive features are likely to be highlighted by the promoter of the issue. That's why it's very important that we find time to follow up with our own research before investing. It can make the difference between striking it rich or striking out. **If the information about a stock is not available from reliable sources, it should not be considered for investment.** Examples are Case Studies #ST4 and #ST5 in Section 702, Chapter 7.

In addition to above, we must avoid all "get-rich-quick" schemes no matter how good they sound whether they involve small or large amount of money. It is easy to get trapped into such or similar schemes or deals that are too good to pass up. Because such schemes or deals generally involve small amount of money with the promise of a big return from investing in shares of a company that hadn't been heard of or that couldn't be investigated because of unavailability of information from sources other than the company itself or its promoter. Hey what! If I lose, I would only lose small amount for the promise of a big return—such attitude toward any investment should be avoided.

We must not get involved in those or other similar schemes if it requires a quick decision or decision on the spot. We must not believe unrealistic promises offered by mail or by telephone from high-pressured promoters or salespersons including sweepstake offers. We should not assume that an offer is legitimate because it is publicized on television, or magazines, newspapers, etc. Remember anyone can buy advertizing or time on television.

We mustn't invest in a product we don't fully understand and for which little or no information is available from reliable sources. Such actions will generally lead to disaster.

We must systematically work toward elimination of such beliefs and practices in order to become a successful investor.

Whether my readers believe it or not, it is the wish of God that makes us rich and prestigious. My all experiences lead to believe me firmly in this hypothesis; God's plans are different for every person.

Section 405
Investment Strategies

(A) Buy-and-Hold Strategy

A buy-and-hold wisdom of long-term investing does not work very well. Most investors probably lose money or get mediocre return because of selling desperately (i.e., at the wrong time) or ride the market up and down without pocketing the profits. This conventional thinking does not always hold good in a changing economy.

Nothing is static in the market. Different types of investments usually respond differently to changing economic conditions. Therefore, investment strategies should be tailored to suit the changing economic conditions. What is good today may not be necessarily good tomorrow.

Stocks and bonds are good investments, but not necessarily at the same time. As a general rule, bond prices move inversely with interest rates. When interest rates go up, bond prices go down; and when rates go down, bond prices go up. It should be noted that the longer-term bonds fluctuate more than the shorter-term bonds as interest rates change.

Investors should be flexible to adjust their investment portfolio to suit the changing economy and market conditions. Buying and selling strategies discussed in Chapter 5 should, in general, produce consistent gains and avoid huge losses that come with the bear market conditions.

It is not intended here to condemn the long-term, buy-and-hold investment strategy that is used by most long-term investors. It is generally easy to implement and may be more effective than frequent selling and buying based on timing the market. Timing the market consistently is virtually impossible. Past dictates that the overall long-term of the market is generally up. However, long-term investment plan is not suitable for all. It is appropriate for those investors who can bear through up and down market periods, can hang in with the market and are not forced to sell at the wrong time.

(B) Stocks vs. Mutual Funds

If you don't have time to become an astute stock or bond picker, consider mutual funds.

Buying into one or two stocks will be risky due to lack of adequate diversification. Investing in mutual funds as an alternative to stocks should be a viable approach. For example, if the future prospects of a particular industry look bright, but difficult to pick a winner(s) within that industry, mutual funds which primarily invest in that industry should be considered.

Mutual funds offer built-in diversification because they invest across the range of various securities and industries, and spread the risk in a way that would be difficult for most individual investors to achieve on their own. By owning a mix of variety of mutual funds, one automatically reduces the vulnerability to a downturn in any one market segment.

(C) Dollar Cost Averaging

Investing a large sum of money at a single point in time will lead to the risk of having possibly invested at a market peak rather than at a market bottom. Investing at a market peak will have a negative effect on yield. Perfect market timing is virtually impossible. One may be right sometimes but cannot be right consistently. Therefore, if a large sum of capital is available at a single point in time, the funds should be invested gradually.

If you cannot or don't have time and expertise to time the market consistently, dollar cost averaging strategy may be an answer for you.

Dollar cost averaging strategy is the practice of investing equal dollar amounts at regular and continuing intervals (monthly, quarterly, etc.) in stocks or mutual funds regardless of the price. With this technique, one buys more shares when the price is low, but fewer shares when the price is high. As a result, the average cost per share, over a period of time, is generally lower than the average market value of your investment. Because the history suggests that the overall long-term trend of the market is generally up. The longer the holding period, the less likely an investor is to incur loss from common stocks or mutual funds. For the strategy to be effective, **one should continue to invest in both up and down markets at set intervals**. Therefore, one should not consider this strategy unless one is financially able to continue investing through various market conditions. Finding a way to invest a set amount automatically at fixed intervals should be beneficial for financially able investors.

This strategy assumes long term commitment of funds and therefore, the investment type selected may rise or fall with changes in the economic cycle. The investor has to bear the pain of anxiety and maintain patience through the declining market periods.

Similarly, if you need the money or decide to liquidate the shares, selling shares gradually through a regular series of transactions should be a viable approach depending on the market conditions and your financial circumstances.

In deploying "Dollar Cost Averaging" strategy, we do sacrifice returns on our investment for the exchange of reduced risk. If we knew the market was on its way up, we would be wise to invest as much money as we can. Conversely, if we knew the market was going to fall, we would be wise to pull our money out of the market and invest somewhere else where it is expected to grow.

The advantage of "Dollar Cost Averaging" strategy is great during the fluctuating market conditions or when the direction of the market is not certain.

Tips:

When a long-term buy signal (action) is generated by the methodology, market conditions sometimes may not appear to be convincing for committing funds to stocks or mutual funds and deciding to wait until the market trend becomes clear, would sometimes result in missing opportunities. Therefore, an investment strategy which integrates the dollar-cost averaging strategy with the long-term buy signal should be a viable approach and would reduce exposure to unexpected events before the market sets its upward direction.

Therefore, why not begin "dollar cost averaging" strategy upon receiving the long-term buy signal. And later, get fully invested as soon as the market direction is clear. The approach should be reversed when a long-term sell signal (action) is received. In other words, selling shares gradually through a regular series of transactions should be a viable approach depending on the market conditions and it is advisable to be out of the market completely as soon as the market appears to be establishing a bearish trend.

(D) Options: A Special Situation

It is a great way to make money quickly if you are right on the trend; it is also a great way to lose money quickly if you are wrong on the trend. Option trading is inherently risky and should only be undertaken by individuals with adequate risk capital.

If you like to trade options, start with a small amount of fund that you can afford to lose, but strictly follow the option trading guidelines given in Section 304 in Chapter 3 without any exception. Before investing in options, become familiar with the case studies listed in Section 704 in Chapter 7.

(E) Investing In The Golden Years

For most people, savings, investments, pension and social security are primary source of income producing assets during retirement. Retirees should learn to live on income available from those sources. Investing should not stop when you retire; it should be handled with care keeping income

and safety in mind. A low risk investment approach should be used to supplement the retirement income.

Investing in stocks and other money instruments, which greatly fluctuate in values due to changes in the economical environment, may not offer a needed rate of return, and is therefore, not suitable for all individuals. Investing in fixed-income instruments, such as certificates of deposit, treasury bills and notes, or mutual funds which primarily invest a large portion of funds in fixed income instruments and a lesser portion in blue chip stocks and investment grade bonds should be a viable approach. Speculative investment approach should be avoided. However, individual's financial, health and personal circumstances have great bearing in dictating the type of investment during the golden years. Though your retirement investment strategies may focus on maximum income with safety, growth of income should not be ignored. The effects of inflation can cause substantial erosion of purchasing power over time on a fixed-income investment portfolio.

A fixed-income annuity is a best way to provide for a lifetime income protection. If conditions dictate, it may be considered for a steady income either for a certain period or for the rest of the life. Before purchasing an annuity, understand the different types of annuities, available investment and withdrawal options, and the risks, rewards and charges associated with each type of annuity.

The main concerns for retirees are income, inflation and expenses which are not always predictable, and the risk of outliving the income generating assets due to longevity. However, by developing and implementing a plan that addresses these concerns, and with proper budgeting the available income and curtailing the unessential expenses should help to ease those concerns. **Remember that financial freedom comes as a result of careful planning and wise spending decisions.**

(F) Investing In The Early Years

Everyone is interested in making more money. More money is needed for future needs, such as to raise a family, to save for college education of children, to buy a home, to improve living standards, to avail funds for the rainy days, and finally to prepare for a comfortable retirement.

After graduating from school or college, you begin your life in the real world facing the competitive job market. Once you start your working career and receive your first pay check, you begin to dream about many things, some of which are mentioned above. You become interested in investing your money to make money. You want to employ "money-makes-money" strategy, but wander how. But remember, before one can invest, one must save.

Understandably, young people generally turn to stock market for investment as a viable approach, but without understanding thoroughly the risks associated with market fluctuations. They also dream for both maximum growth and maximum safety of their money. These objectives are simultaneously not achievable in the real world of investment because they tend to move inverse of each other. The practical approach is to find the middle road between maximum growth and maximum safety.

When you decide to invest in the stock market first-time, you generally turn to your friends and brokers for advice, and expect to see your investment rise in value. Suppose it doesn't, then what?—

You probably would blame your friends and brokers. You lose sleep, become impatient, emotional and angry, and begin to worry. As a result, you tend to make decisions based on the outside influences. The side effects would be depression and impulsion to get more deeper into the stock market without collecting the facts and analyzing them thoroughly. It happened to me and I don't want it to happen to you. Therefore, I wrote this book.

When you have saved some money that you can stash away for sometime, don't rush to the stock market for investment without thoroughly understanding how it works and the associated risks. If you invest in the stock market first-time and lose money, you also lose confidence and you might shy away from such investments in the future. As a first-time investor, you should play "what if" game before considering such investments, and be prepared beforehand, and have a written plan of action ready in the event your investment begins to decline in value. The methodology discussed in this book will help you to formulate the plan.

It is suggested that you take conservative and cautious approach when it comes to investing for the first-time until you gain experience and confidence. This book tells you how and when to invest in stocks and mutual funds. It is wise to invest some of the money in certificates of deposit and money market funds. Certificates of deposit are insured by FDIC; money market funds, however, are considered just as safe. Money market fund is liquid asset and therefore, it is available on demand for investment when the market condition becomes suitable.

The table below illustrates the compounding effect of money and it compares the result with hypothetical returns from investing in the stock market. Three scenarios are illustrated. Each scenario begins with initial $10,000 investment. Scenario A represents investment in certificates of deposit at 6% compounded annually. Scenario B invests in stocks, bonds and mutual funds accepting risk of market fluctuations and the investor stays in during market's upturns and downturns. Scenario C is similar to scenario B but the investor pulls the money out of the market during the bear (downturn) market periods and invests the proceeds in money market funds paying 5% annually.

	Scenario A	Scenario B		Scenario C	
Year	Value of Cert. of Deposit at the end of year	Annualized return from investment	Market value at the end of year	Annualized return from investment	Market value at the end of year
1	10,600	12%	11,200	12%	11,200
2	11,236	12%	12,544	12%	12,544
3	11,910	-8%	11,540	5%	13,171
4	12,625	12%	12,925	12%	14,751
5	13,382	15%	14,864	15%	16,964
6	14,185	12%	16,648	12%	19,000
7	15,036	-12%	14,650	5%	19,950
8	15,938	12%	16,408	12%	22,344
9	16,894	13%	18,541	13%	25,249
10	**17,908**	-6%	**17.429**	5%	**26,511**

In the table above, a period of 10 year was considered during which downturn in the market occurred three times. Scenario B did not realize these downturn periods until it was all over and therefore, stayed in the market. This generally happens to most of us—**We do not realize that we are in the bear market phase until the bulk of the bear market damage has occurred or it's all over**.

The above illustration is hypothetical and it demonstrates the importance of staying out during the bear market periods (Scenario C) and rolling over the proceeds to money market accounts or short-term certificates of deposit. This book tells us when to stay in and when to stay out of the market.

Scenario B, in fact, demonstrates "Buy-and-Hold" strategy. The question to be asked to yourself when the result is compared with Scenario A—Is it worth the trouble of taking market risks when you don't have time and expertise to detect downturns and upturns in the market?

Financial freedom comes as a result of careful planning and wise spending decisions (i.e., understanding the difference between your 'wants' and 'needs'). If you live beyond your means now, you are stealing from your retirement. A sound financial plan can make your retirement years truly golden. The need to start early and save as much as possible now for retirement cannot be over emphasized.

Getting started with investing as early as possible can make a big difference in how much wealth you can accumulate over a period of time. It is never too late to start for a financially independent retirement, sooner the better. The benefits of begin savings and investing early in life are greatly enhanced by the effect of compounding. The following examples illustrate the importance of begin investing early in the life and the power of compounding.

- If you invest $1000 a year for the first ten years of a 30-year period with annual compounded rate at 6%, you will have accumulated $33,370 on a total $10,000 investment, compared to someone who invests $1000 a year for 20 years beginning from year eleventh through thirtieth year (i.e., a total of $20,000 investment over a period of 20 years) would accumulate approximately the same (i.e., $33,065) on a twice the investment of yours.
- However, if you can find an investment that returns 10% annually over a period of 30 years, the accumulations would be $107,220 for you and $57,275 for the other person who started investing 10 years after you did—a remarkable difference with one-half the investment of the other person.

Tips:

To help save and grow money for a comfortable retirement, you should

- Learn to begin saving on a regular basis from the first month of your first job even if it is only $10, $20 or $30 monthly and invest your savings wisely.
- Take advantage of the tax-deferred investment opportunities available to you. These will include traditional Individual Retirement Accounts (IRAs), 401(k)s, company pensions plan, etc.

In addition to, you might also like to consider a variable annuity which allows your **other savings** to grow tax-deferred to supplement income from IRAs, 401(k)s, etc. during retirement years. The annuity can generally produce more after-tax income than other taxable investments yielding mediocre returns. Detail information on variable and other types of annuities may be available from your insurance agent, broker, or your financial advisor.

(G) Fool's Strategy

I was one of the fool investors, per se best of all. That's why I wrote this book. Fool investors make many assumptions to suit their ideas and beliefs about the market and they usually don't have well defined and thought out plan when it comes to making investment decisions.

Fool investors, in general, do buying and selling without any basis and they are inclined to follow the crowd. This may be right for some of the time, but such actions are blind-folded and could have disastrous impact on the returns of their investments. Market might not treat them right all of the time. Fool investors have no idea why they are doing it and do not know if the time is right; they mostly act based on guess-work, rumors, or stories and they don't care to document reasons for their actions.

Fool investors, in general, don't have a well-defined action plan and if they do, either they don't follow it with great discipline or it is based on fiction rather than facts. They make decision based on guesswork. Fools don't have the knowledge of the technical market indicators in general, and they don't care about it because they are busy in predicting the value of their investment and how much profit they should be able to fetch from the stock market. They set their target prices and are not willing to compromise. Such investors will inevitably make decisions that lead to very poor investment returns.

A fool always looks at the glass as one-half empty; he or she forgets that the glass is one-half full. So they hang-in with their investment and hesitate to take whatever gain is left there. Instead they wait for the price to reach their initial goal. They don't believe that to get rich is to get rich slowly—drop by drop you can fill the bucket. If you pour the water fast into the bucket, most of the water will spill out and bucket will mostly remain empty.

If we want to acquire wealth with lasting effect, we should not expect to become rich too quickly or too easy. If it comes too quickly, it will not last. It is like hay-fire that makes a great blaze, but neither last nor gives heat like a log fire.

Fools, in general, don't enter the market until the bull market is in its final phase and he or she does not move to the sidelines until the bulk of the bear market's damage has been realized.

Fool's Investment Wisdom:

- Why buy now when I did not buy it when it was cheaper a few weeks or months ago. So a fool waits and waits, lose patience and jumps into the market near the top or when the market is about ready to plunge.
- Why sell a stock now when I did not sell it when it was few dollars higher a few weeks or months ago. He or she looks at the empty portion of the glass and not at the filled portion of the glass. So a fool waits for the stock to go up to his or her set target price. While waiting, he or she watches his or her loss getting bigger. He loses patience and sell the stock at the bottom or just before the stock is ready to make an up move.
- **Fools never bother to investigate to find out why their stock is steadily falling or has declined abruptly. Their normal excuse is "no time."**
- Greater Fool Theory—The more money the fool makes, the more addicted the fool becomes; the more money the fool loses, the deeper the fool gets into it until the fool is in verge of losing all.

Therefore, don't follow the fool's strategy and never assume (ass-u-me) anything while investing; act on facts, not on fiction or assumptions or guess-work; market has no feeling and it does not care what you think or believe in. When it comes to making a sell decision, keep your eyes on the lower filled portion of the glass, not on the upper empty part of the glass.

I got trapped into similar situations and I don't want it to happen to you. Therefore, I developed the methodology of mechanical (disciplined) investment strategy presented in this book. **In any case, one should not get addicted and should learn when to quit.**

Buying and selling based on rumors, stories, guess-work, or belief should not be employed. Selling because we believe the market is about to decline could cause us to miss out on potential returns. Conversely, postponing buying because we believe that the market is very high and the correction in the market is imminent could result in missing completely the market continued advance (see Case Study #MF2 in Chapter 7).

When the methodology generates a buy signal, act accordingly (see Chapter 5) without paying any attention to the prices, high or low, and without comparing current prices with the prices a few weeks or months ago. The following examples which are few of many, illustrate a typical (fool) investor's sentiment:

- Rite Aid stock generated a buy signal week ending 6/16/95 at $26.25 based on the methodology described in this book, where as the price of the stock was in the $18-20 range a year ago (April-May 1994) about $6.00 cheaper.
- Mylan Lab stock generated a buy signal week ending 7/4/97 at $15.06 based on the methodology described in this book, where as the price of the stock was in the $12-13 range a few moths ago (April 1997) about $3.00 cheaper.

Both stocks rose sharply after the buy signal. Not buying them as per the buy signal generated by the methodology resulted in missing the great opportunity.

SECTION 406
BE AN OBSERVER

- It is a generally accepted belief that the market, in general, has a tendency to rise on the last trading day and during the first few trading days of most months. The market also tends to rise before the market holidays (such as New Year's Day, Memorial Day, Independence Day, Labor Day, Thanksgiving Day and Christmas Day) most of the times.

  Buying call options solely based on this strategy is highly speculative.

- Last Hour Change in DJIA: If the DJIA has moved up in the final hour of trading that strength is generally carried over into the following day. Conversely, if the DJIA has been moving down in the final hour of trading, that weakness is generally carried over into the following day.
- NYSE Closing TICK: High positive NYSE (New York Stock Exchange) closing TICK figure does not necessarily indicate that the market will open higher on the next day; it generally depends on the overall trend of the TICK near the close of the trading day and the trading activities conducted by the marketmakers or the exchanges around the world between closing and opening of the market.

- DJIA trend during the beginning of the week or the day, or during the later part of the week or the day, does not necessarily indicate weakness or strength in the market.
- Bear (down) market periods are generally short. Bull (up) market periods are generally long. It is a general belief that a bear market is considered over if the DJIA declines the most (say more than 15%) in a relatively short period of time, or the DJIA declines 15% or more slowly over an extended period of time. If market declines to a lesser extent, it is considered as a correction. (Comment: However, there is no certainty that the market would or would not continue its decline further and longer.)

It is generally not possible to predict in advance with certainty whether the market is undergoing a major correction or establishing a bear phase. It takes awhile (and always too late) to know if we are really in a bear market or in a correction phase. Experience shows that one should, therefore, stick with the plan described in this book, and be self-disciplined to adhere to it. Market can be volatile, but your trading strategy should not be.

- It is not uncommon for a system to generate a long-term buy signal shortly after a long-term sell signal. The period from sell to buy signal then may be considered as a major correction within the confines of an ongoing bull market. Refer to Table 601 for information.
- In an election year, the beginning of a bear market is not a certainty, even though the system flashes a long-term sell signal. The market usually rises in an election year. Conversely, a market decline historically follows a presidential election year and this, of course, would not materialize unless a system flashes a sell signal.
- When the market advances after heavy volume on the downside during the previous few trading days, it may be because the specialists want to unload their inventory (if accumulated) before taking the market further down or may be up.
- If the DJIA is trading far above or below its 30-week moving average line, don't expect the market to reverse its trend for it to come closer to its 30-week moving average line; it may continue its advance or decline even further.

❖ *Profits and losses are two sides of the same coin; one doesn't exist without the other* ❖

Chapter 5

PLAYING THE MARKET GAME

(A Systematic Approach To Winning)

OBJECTIVE

To learn and understand the investment techniques for playing the market game once a buy or a sell signal is generated by the methodology.

OVERVIEW

One must remember that signals are guides and are intended to reveal changes in the market trends, but are not always obligated to do so. That is to say, if signal does not occur, it does not mean that the market has to wait for a signal to occur. However, it is imprudent to act without a signal.

Therefore, emphasis is placed on checking and rechecking the validity of the buy and sell signals in conjunction with other indicators described in this book. Guidelines are given for necessary homework before investing funds, and then monitoring the investment for a profitable trade or to minimize losses.

Thus, the key elements for playing the market game for successful investing are: (1) Have a disciplined investment strategy in place based on the time-tested methodology and (2) Implement the strategy, and monitor and manage the investment to reduce the risk.

Some investors may prefer to prepare a flow chart showing the step-by-step plan of action to be used as a guide. Flow chart acts like a ladder, step-by-step, to help achieve investment goals. A sys-

tematic plan or a flow chart will help in making appropriate decisions for the management of investments.

One should not invest funds without completing the homework described in this Chapter. This is very important, particularly when trading options. One should make a habit to obey all the rules all of the time without any feeling regarding profits or losses.

After all, you have invested time and effort in determining buy and sell signals; you, as an investor, should believe in them and willing to try them. Knowing they can go wrong sometimes, you should pay serious attention to any warning signals (Section 105, Chapter 1) that may develop later. You must remain alert to recognize any unexpected changes in the political picture, at home and abroad, which often can influence the behavior of the market.

Upon satisfactory completion of the homework described in Section 501 below, and if a conclusion for investing funds is reached, the only thing to do is to build-up courage, get prepared, and go for it. **Do not wait for the perfect market conditions. Because there are none. If you wait for it, you are going to find yourself getting in at or near the top or getting out at or near the bottom.**

Don't sit back and relax. Begin guarding your investments using the rules described in this book. It is hard for anyone to invest hard-earned dollars in the stock market due to fear of losing. It is even much harder to pull the money out of the stock market because of the urge to be greedy.

Once an investment is liquidated, it is suggested to monitor the investment sold for sometime to see if the sell decision was wrong or right. If it is determined that the decision was wrong, describe reasons for buying and selling, and if any lesson could be learned. Develop a case study for future reference. Case studies are very important for trading stocks and options. Refer to Chapter 7 for examples of case studies.

We generally have tendency to forget our own experiences, and the thoughts (hopes, feelings, expectations, etc.) that flash through our minds while sitting back and not acting according to the plan during the period the investment has been going sour. Therefore, we should believe in putting down our experiences and thoughts on paper for future reference.

It is necessary to keep detail records of all buy and sell investment decisions. If we remember only our wins, we tend to underestimate the prospect for defeat. We could learn valuable lessons from our own mistakes only if we had kept a detail record of our investment experiences.

This Chapter is divided into following Sections:

Section 501
Understanding The Signals

Long-term signals should be used for investing in mutual funds. Short-term signals are like waves, ups and downs, occurring during the bull and bear phases of the market. They are suitable for short term trading, or adding funds to existing long term positions if the market conditions are favorable.

The following Table shows general interpretation of the market signals:

Market Action	Signal	What-To-Do
Down-Wave	Sell	Act soon
Down-Wave	Buy	Waiting until market approaches to its most recent bottom could be very beneficial
Up-Wave	Sell	Waiting until market approaches to its most recent top could be very beneficial
Up-Wave	Buy	Act soon

Either buy or sell signals can occur during the market's uptrend or downtrend cycles, or at market tops or bottoms. Most buy signals occur when the market is on the way up, not when the market is at the bottom and most sell signals occur when the market is on the way down, not when the market is at the top.

It is generally not likely to have a buy signal to occur at the bottom and a sell signal to occur at the top. However, it can happen sometimes. When a buy signal occurs at the bottom of the market, and a sell signal occurs at the top of the market, acting accordingly, can be very rewarding.

It is not uncommon for a system to generate a long-term buy signal at higher prices than those were at the previous long-term sell signal. Refer to Table 601 for details.

It should be noted that a buy or a sell signal does not necessarily mean that the stock market is going to turn-around immediately. It is likely that the market could continue its advance after a sell signal and decline after a buy signal.

Regardless of the above, experience shows that one should follow the plan described in this book and adhere to it all of the time in order to become a skillful investor. By following the plan, investors generally will be in the market for a major portion of the market advance and out of the market for a major portion of the market decline.

However, during a period of high volatility when the market swings up and down sharply, buy signals generated by the methodology discussed in Chapters 1 and 3 should, however, not be ignored, but should be considered with prudent judgment and caution. Such buy signals may be speculative and suitable for short-term trading the market. That is to say, take profit (loss) when it seems appropriate or protect gain (cut loss) by initiating mental loss limit limit technique (see Chapter 4) rather than waiting for a sell signal to occur. A strategy which takes into account the fundamentals, value investing and evaluation of the general market condition based on the market mood indicators (see Chapter 1) is suggested.

Section 502
You Have A Signal, Now What?

(A) Verification

Before committing funds, it is absolutely necessary to conduct a thorough review of all technical indicators using the procedure described below. The purpose of such a review is to make sure we didn't miss to consider any data that might have influenced the outcome of the signal.

1. Technical Indicators

Revisit the Technical Indicators

Review and list those indicators that have generated a buy or a sell signal (Section 102, Chapter 1) and, those if any, contradicting the signal for future use. Recheck if the signal has met all of the specified conditions and determine whether or not the signal is valid.

Review and list the status of Market Mood Indicators (Section 104, Chapter 1) that could or would influence the validity of the signal in question.

Also make sure that personal feeling about the market has not influenced the interpretation of the indicators that generated the signal.

Revisit the Exceptions (Section 105, Chapter 1)

Review all exceptions and determine if they are applicable to the signal in question. Make sure if the signal is still valid.

2. Questions?

Answers to the following questions should aid the decision making process:

- Is change in the market movement zone in progress or anticipated?
- Is the general market condition improving or deteriorating based on the trend of the market movement zones (Section 101, Chapter 1)?
- Is the general market condition improving or deteriorating based on the status and the trend of the Market Mood Indicators (Section 104, Chapter 1)?
- Are there any conflicting signals?
- Has the signal occurred with the market making a new high or a new low?
- Is DJIA at the top or bottom or has it established a top (crest) or a bottom (valley)?
- Has the signal occurred at the top (crest) or at the bottom (valley) of the market?
- Has the signal occurred during a rising or a falling market?
- Has the signal occurred during a tired bull or bear phase of the market (Sections 109 and 110, Chapter 1)?
- Would there be any warning signals (Section 105, Chapter 1) anticipated?
- Is there any possibility of a rally or correction in the market from the current level?

3. Rules That Negate Mistakes

- Review Chapter 4.
- Review applicable case studies if available. Refer to Chapter 7.

4. What's Expected Of The Market?

- Describe briefly what is expected of the market based on the signals and the strength or weakness of the technical indicators.

(B) Investment Strategies (Suggested Actions)

The following are some guidelines on *how and when to invest* once the signal is verified and a decision is made for investing funds:

Short-term Buy & Sell Signals (Section 102, Chapter 1)

Use buy signals for adding funds to existing long term positions such as mutual funds (Section 303, Chapter 3) if market conditions are favorable.

Use these signals for trading OEX (S&P 100) Index options with money you can afford to lose. Use the option trading strategy discussed in Section 304 in Chapter 3. **Option trading case study #CO9 listed in Section 704, Chapter 7 may be of special interest to option traders**; it must be reviewed along with the other case studies in Section 704 to gain insight to the mechanism involved for a more successful trade.

Long-term Buy & Sell Signals (Section 103, Chapter 1)

Use these signals to buy and sell mutual funds (Section 303, Chapter 3).

The plan of action here is to get fully invested and remain fully invested until a long-term sell signal is received. Once the sell signal is received, one should reduce the holdings considerably, but selectively. At that point preservation of capital must be the primary and the critical issue.

Stock Buy & Sell Signals (Section 302, Chapter 3)

Use these signals to buy and sell stocks.

It is suggested that the investment portfolio includes portion of each of the following for a well diversified investment portfolio:

(1) Money market funds, certificates of deposit, and/or treasury notes and bills
(2) Short term and long term investment grade bond funds
(3) Stock mutual funds, such as growth, growth and income, and some sector and international funds if appropriate to your investment sentiment
(4) Index funds—This ensures that a portion of your investment portfolio performs like the general market.

How much should an investor allocate to each of the above investment categories? Answer to this question depends on the individual's financial circumstances and the general market conditions. During a bull phase of the market, a greater portion of the total investment should be allocated to stock and index mutual funds and individual stocks, and during a bear phase of the market most of the funds should be in the money market and may be some funs in bond funds.

(C) Comments

List any comments or remarks pertinent to the action taken that should be reviewed later if the investment does not perform as expected.

If no action was taken, list pertinent reasons for not doing so for future reference.

When a buying opportunity is missed, it is not uncommon for investors to get frustrated when they see the market keeps going up, up, up. At that point it is prudent not to jump into the market with full force in order to make up for what was missed, and not to blame yourself or anyone else for that matter. Do not mourn over the missing opportunity, but concentrate on "how-not-to" miss the next opportunity, or how to make the best use of the present situation.

Section 503
You Have Invested, What's Next?

Once a fund is committed, do not sit back and relax. Investments should be watched from day one. Let the following step-by-step procedure guide you:

(A) Attention

A sell action generated by the methodology should be implemented as immediately as possible without any due regard to loss or profit. Never allow your emotions and feelings convince you otherwise. Learn to manage risk in accordance with Section 404(c) in Chapter 4.

Investing would be vastly more profitable if we could learn and discipline ourselves

- to stick with the methodology all of the time, and
- to harness our emotions and feelings.

(B) Disciplines That Negate Mistakes

- Review Chapter 4.
- Review applicable case studies if available. Refer to Chapter 7.
- Keep track of performance of all investments in accordance with Section 305 in Chapter 3.

(C) If Invested In Index Options

- Follow all the rules all of the time. Refer to Section 304, Chapter 3.
- Establish a plan or a strategy that can alert you when to sell or close the position. Form 304B in Chapter 3 are designed for this purpose. They should be used to monitor the market conditions and the price movement of the option. Refer to case studies listed in Section 704, Chapter 7 for details.
- Monitor the price of an option on a daily basis, and on an hourly basis if conditions warrant.

- Close option position as soon as a sell condition is generated. Refer to Table 304(B)3 in Chapter 3.

Tip:

When trading options, ban all wishful thinking, guesswork and emotional feeling regarding profit or loss. Let the option trading plan described in Section 304 govern the course of your action. For details, refer to Section 704 for Index Options Trading Case Studies.

❖ *No one is immune from losses all of the time; everyone incurs losses at times* ❖

Chapter 6

MARKET SIGNALS LOG

OBJECTIVE

To verify the methodology for detecting market trends presented in this book by tallying the changes in the DJIA and OEX (S&P 100) indexes with each market signal.

OVERVIEW

All market signals, long-term and short-term, are chronologically listed in Tables 601 and 602 in Appendix B and a brief explanation is presented in this Chapter. Comments or remarks where appropriate are noted in Tables 601 and 602 and signals are identified for case studies where necessary.

This chapter is divided into following Sections:

600 -Introduction
601 -Summary of Long-Term Signals
602 -Summary of All Signals
603 -Bull & Bear Phase Periods

SECTION 600
INTRODUCTION

The following information will be helpful in understanding Tables 601 and 602 included in Appendix B:

Table 601 lists whichever long-term signal of the three long-term signals discussed in Section 103 occurred first. It is not uncommon for a system to generate a long-term buy signal at higher prices than those were at the previous long-term sell signal.

Long-term signals should be used for long-term investments, such as mutual funds. Short-term signals may be suitable for short-term trading. For example, trading OEX Index options in accordance with Section 304 in Chapter 3. If conditions warrant, short-term buy signals may be used to add funds to existing long-term positions. For details, refer to Chapter 5.

Short-term trading scenario column in Table 602 indicates what could happen if OEX Index call or put options are traded based on the short-term buy and sell signals.

When sharp declines in the market occur (refer to Exception EB in Section 105(B), Chapter 1), there is no way to predict the future course of the market. Therefore, it is suggested to close all option positions. Sharp decline weeks, if and when appropriate, are included in Table 602 for reference only.

Certain technical data, such as Market Condition (MC) Index shown in the Tables, are as of the previous week ending when dates ( ) are identified.

When conflicting indexes, such as IN-index and OT-index, or conflicting signals, such as S1/Sell and S8/Buy signals occur, refer to Section 107 in Chapter 1 for details.

Nomenclatures used in Table 602 are:

SL	=	Sell (i.e., consider taking put option position)
BY	=	Buy (i.e., consider taking call option position)
LT/SL	=	Long-Term Sell Signal
LT/BY	=	Long-Term Buy Signal
CSP	=	Close Sell (put) Position
HSP	=	Hold Sell (put) Position
CBP	=	Close Buy (call) Position
HBP	=	Hold Buy (call) Position

Note that in Table 602, S3 and S9 signals are recorded right justified for ease in identification of these speculative, very short-term (approximately one-week) signals.

SECTION 601
SUMMARY OF LONG-TERM SIGNALS

Detail summary of long-term signals from year 1984 through 1999 is shown in Table 601 in chronological order. They are compiled from Table 103S. The last column in Table 601 shows % changes in the DJIA, SPX (S&P 500), VLG and OEX (S&P 100) indexes from buy date to sell date.

In the following Table, a brief summary of Table 601 showing changes in the values of those indexes between buy signal and sale signal dates expressed as the ratio of index values at sell signal date to buy signal date is presented.

Buy Signal Dates	Sell Signal Dates	Changes in			
		DJIA	SPX	VLG	OEX
12/21/84	09/19/86	1.47	1.41	1.25	1.35
10/31/86	10/09/87	1.32	1.27	1.18	1.32
02/12/88	10/13/89	1.30	1.30	1.22	1.26
05/11/90	08/03/90	1.00	0.98	0.95	0.99
12/07/90	11/22/91	1.12	1.15	1.19	1.14
12/27/91	04/21/92	1.08	1.01	1.04	1.02
10/30/92	03/29/94	1.12	1.06	1.17	1.08
01/06/95	06/28/96	1.46	1.46	1.27	1.51
08/16/96	03/12/97	1.24	1.21	1.13	1.21
05/02/97	10/31/97	1.05	1.13	1.16	1.10
01/30/98	05/15/98	1.15	1.13	1.11	1.15
10/16/98	02/05/99	1.11	1.17	1.11	1.19
04/16/99	07/23/99	1.04	1.03	1.06	1.05

Section 602
Summary Of All Signals

Table 602 lists all short-term and long-term signals in chronological order from year 1986 through 1999 that are compiled from Tables 102A through 102J and Table 103S. Signals requiring explanations are identified and details are presented in Section 701 in Chapter 7.

Section 603
Bull & Bear Phase Periods

The bull and bear phase periods of the market are to be determined using the buy and sell signals from Table in Section 601 above. A bull phase is the period of time from a buy signal (for example, 12/21/84) to a sell signal (for example, 9/19/86) and a bear phase is the period of time from a sell signal (for example, 9/19/86) to a buy signal (for example, 10/31/86).

◆ Reminder ◆

It should not be assumed that the use of the methodology in the future will equal past performance.

❖ *Don't be greedy and emotional.*
Follow all the rules all of the time ❖

Chapter 7

CASE STUDIES

OBJECTIVE

The purpose of this Chapter is to discuss selected case studies (special situations) for future reference. It will serve as a guide in making all future decisions if and when similar conditions arise. Lessons learned from these case studies will help prepare investors for a more successful trading.

OVERVIEW

This Chapter includes case studies involving market signals, stocks trading, mutual funds investing and index options trading. It is divided into four Sections. They are:

701 -Market Signals Case Studies
702 -Stocks Trading Case Studies
703 -Mutual Funds Investing Case Studies
704 -Index Options Trading Case Studies

Section 701
Market Signals Case Studies

Detail explanation of signals identified as case studies in Table 602 (Appendix B) is presented in this Section. The following case studies will serve as references in making future decisions.

CS#90/A: 3/2/90 S1/BY, S6B/BY & S7/BY

How occurred:	During up-market after two bottoms on 1/26/90 (DJIA = 2559.23) and 2/23/90 (DJIA = 2564.19)
What's expected:	Market might continue its up-trend

What happened:

WkEd or (Date)	DJIA	OEX	Remarks
3/2/90	2660.62	315.66	S1/BY, S6B/BY & S7/BY Signals
3/9	2683.33	318.13	
3/16	2741.22	322.94	To be on the safe side, close call position per WB warning applicable to S1/BY and **ignore the S6B/BY & S7/BY Signals.**
3/23	2704.28	318.55	
3/30	2707.21	320.03	
4/6	2717.12	320.89	
4/13	2751.89	325.09	

CS#91/A: 3/8/91 S9/SL

How occurred:	S9/SL Signal occurred at market peak, very near to 52-week new high that occurred during the week ending 7/20/90.
What's expected:	Because of a S9 sell signal and it being a one-week signal, market might decline by end of the next week

What happened:

WkEd or (Date)	DJIA	OEX	Remarks
3/8/91	2955.20	355.12	S9/SL Signal
(3/11)	2939.36	353.95	
(3/12)	2922.52	351.37	
(3/13)	2955.20	356.25	
(3/14)	2952.23	355.31	OT-index suggests to hold S9 sell position.
3/15	2948.27	355.88	Repeat S9/SL Signal—hold sell position for the next week
(3/18)	2929.95	354.09	
(3/19)	2867.82	347.40	
(3/20)	2872.03	348.28	
(3/21)	2855.45	346.80	Consider closing the position. Note that S9 signal is good for one week only.
3/22	2858.91	347.84	Must close sell position per S9 signal rules
(3/25)	2865.84	350.59	
(3/26)	2914.85	357.74	
(3/27)	2917.57	356.00	

CS#92/A: 7/24/92 L1/SL and S3/BY (Exception EH2)

How Occurred	Both signals occurred during market decline (sideways movement) and at or near the most recent bottom of DJIA = 3274.12 on 6/18/92.
What's expected	Technical rebound would be expected per S3/BY Signal. L1/SL Signal would become a delayed signal per Exception EH2. Previous peaks were at DJIA=3413 (week ending 6/5/92) and OEX=391 (week ending 5/8/92)

What happened:

WkEd or (Date)	DJIA	OEX	Remarks
7/24/92	3285.71	384.29	S3/BY Signal governs over L1/SL Signal per Exception EH2
7/31	3393.78	395.81 New High	S3/BY Signal ends and Long-Term Sell Signal becomes effective per Exception EH2.
8/7	3332.18	389.77	
8/14	3328.94	394.79	S1/BY Signal—invalid per Exception EE2
8/21	3254.10	384.23	
8/28	3267.61	385.76	

CS#92/B: 12/25/92 S2/SL with Exception EE1

How occurred:	S2/SL Signal occurred within two weeks of L1/BY Signal
What's expected:	Since S2 sell signal occurred within two weeks of long-term buy signal, it should be considered invalid per Exception EE1.

What happened:

WkEd or (Date)	DJIA	OEX	Remarks
12/18	3313.27	403.39	
12/25	3324.11	401.42	S2/SL Signal—invalid per Exception EE1. Refer to Option Case Study PO2 also.
1/1/93	3301.11	396.64	Although results are favorable, consider it as an exception and a special situation.
1/8/93	3251.67	389.93	S1/SL Signal and Exception EE1 (refer to CS#93/A below).
1/15/93	3271.12	397.17	Warnings WA and WB to S1/SL Signal of 1/8/93
1/22/93	3256.81	396.75	
1/29/93	3310.03	401.57	

CS#93/A: 1/8/93 S1/SL with Exception EE1

How occurred:	During market decline (sideways movement) where DJIA lost 73 points and OEX lost 11 points from their most recent peaks on 12/28/92 (Monday). It was also at or near the previous bottom on 12/18/92(Friday). Exception EE1 is applicable.
What's expected:	Note that DJIA was at or near the previous bottom and the 10- & 30-week moving average lines have turned up, resistance to downtrend is expected. Ignore S1/SL Signal per Exception EE1, and also, because of change in the status of DJIA moving averages.

What happened:

WkEd or (Date)	DJIA	OEX	Remarks
1/1/93	3301.11	396.69	
1/8/93	3251.61	389.97	S1/SL Signal—invalid per Exception EE1.
1/15/93	3271.12	397.17	Warnings WA & WB to S1/SL of 1/8/93
1/22/93	3256.81	396.75	
1/29/93	3310.03	401.57	

CS#94/A: 3/4/94 S3/BY

Remarks:	S3/BY Signal is a buy on Monday & sell on or before Friday type signal. However, IN1-index of 3/9/94 can be considered supporting the S3/BY Signal. Therefore, it is preferable not to close the buy position on Friday as required by S3 signal rules. Therefore, hold buy position for the next week.

What Happened:

WkEd or (Date)	DJIA	OEX	Remarks
3/4/94	3832.30	431.68	S3/BY Signal
(3/7)	3856.22	432.92	
(3/9)	3853.41	433.63	IN1 index suggests to Hold Buy Position until next week
(3/10)	3830.62	430.82	
3/11	3862.70	432.74	Hold Buy Position until next week
(3/16)	3848.15	435.18	
3/18	3895.65	436.31	Close Buy Position per S3 signal rules

CS#94/B: 6/17/94 S9/SL

How occurred:	Almost at or near the top of the market
What's expected:	Market might decline. Note that S9/SL Signal is good for one week (Buy on Monday 6/20, sell on or before Friday 6/24).

What Happened:

WkEd or (Date)	DJIA	OEX	Remarks
6/17/94	3776.78	424.07	S9/SL Signal
(6/20)	3741.90	421.58	
(6/21)	3707.97	417.68	
6/24	3636.94	409.93	Close Sell Position per S9 signal rules.
7/1	3646.65	412.39	Market began rising. Also S6B/BY Signal occurred this week ending 7/1/94.

CS#94/C: 9/2/94 S9/SL with Exception EF1

Remarks	S9/SL Signal generated no action because of Exception EF1. Signal is considered invalid per Exception EF1. Note Labor Day weekend.

What Happened:

WkEd or (Date)	DJIA	OEX	SSR	Remarks
9/2/94	3885.58	434.82	33.69	S9/SL Signal with Exception EF1.
(9/8)	3908.46	437.18		Highest for the week
9/9	3874.81	433.13	34.12	
(9/12)	3860.34	432.24		Lowest for the week
9/16	3933.35	438.21	35.96	S1/SL Signal
9/23	3831.75	426.55	29.62	**Close sell position** (SSR = 29.62)
9/30	3843.19	428.17	33.21	
10/7	3797.43	421.56	34.01	

CS#94/D: 10/14/94 S5/BY

How occurred:	Almost at or near the previous market top
What's expected:	Market might rise based on low SSR of 33.12

What happened:

WkEd or (Date)	DJIA	OEX	SSR	Remarks
10/14/94	3910.47	434.76	33.12	S5/BY Signal
10/21	3891.30	430.92	30.74	Close Buy Position per Warning WA and incur loss or **take a chance and hold position because of SSR = 30.74.** For information, refer to Section 105(C)1.
(10/24)	3855.30	426.57		
10/28	3930.66	439.21	37.10	
11/4	3807.52	429.26	34.10	
11/11	3801.47	430.47	33.81	
11/18/94	3815.26	430.76	34.18	

CS#95/A: 7/28/95 S9/SL? (DJIA set new high previous week—Exception EG1)

How occurred :	Near the previous top formed week ending 7/14/95. DJIA bar chart shown in *The Wall Street Journal* indicated that the crest might be forming week ending 7/28/95.
What's expected:	Very hard to guess because of Exception EG1.

What happened:

WkEd or (Date)	DJIA	OEX	Remarks
7/21/95	4641.55	529.52	DJIA closed on Friday 13 points above the low of 4628.87 on 7/19/95 for the week and 94 points below the new high of 4736.29 on 7/17/95.
7/28	4715.51	535.63	S9/SL Signal may be OK as a **special case, but it is speculative and risky.** See Option Case Study #PO4 in Section 704.
8/4	4683.46	529.60	
8/11	4618.30	525.95	

CS#95/B: 10/16/95 (Monday) S1/BY; 10/20/95 (Friday) S3/SL

How occurred :	DJIA moved sideways after forming a valley week ending 10/13/95
Remarks:	Note that by week ending 10/20/95, S3/SL Signal also occurred and a market made a new high. Exception EG1 does not apply to S3/SL Signal per Section 105(B). However, per exception EH1, S3/SL Signal governs first before the S1/BY Signal. Refer to Option Case Studies #CO7 and #PO5 in Section 704.

What happened:

WkEd or (Date)	DJIA	OEX	Remarks
(10/16/95)	4784.38	556.15	S1/BY Signal. Wait until the week ends (i.e., 10/20/95) per Note (1) in Section 102(A)1, Chapter 1.
(10/17)	4795.94	559.93	
(10/18)	4777.52	560.56	
(10/19)	4802.45	564.72	
10/20	4794.86	561.20	Apply S3 sell signal per Exception EH1 (See Option Case Study #PO5 in Section 704)
10/27	4741.75	553.96	Close S3/SL Position. Buy per S1/BY Signal —See Option Case Study #CO7 in Section 704.
11/3	4828.37	561.89	
11/10	4870.37	564.76	

CS#95/C: 12/15/95 S3/SL with Exception EF1

How occurred :	DJIA at top and appeared to be forming a crest
What's expected:	Market might or might not decline because of Exception EF1 (note that SSR = 33.80)

What happened:

WkEd or (Date)	DJIA	OEX	Remarks
12/15/95	5176.73	590.51	S3/SL Signal with Exception EF1 (SSR = 33.80)
(12/18)	5075.21	581.90	Buying put option may be dangerous due to Exception EF1. Be guided by Exception EF1.
(12/20)	5059.32	580.14	
12/22	5097.97	584.37	
12/29	5117.12	585.92	

CS#96/A: 4/18/96 S1/BY

How occurred :	During the declining market.
What's expected:	Market might turn around because of S1/BY Signal.

What happened:

WkEd or (Date)	Zone	DJIA	OEX	SSR	Remarks
4/12/96	A+	5532.59	615.36	33.92	S9/BY Signal
(4/18)		5551.74	621.25		S1/BY/1 Signal, wait until the week ends (i.e., 4/19/96) per Note (1) in Section 102(A)1, Chapter 1. Hold S9/BY position.
4/19	A+	5535.48	622.36	32.41	Buy per S1/BY/1 Signal, HBP of S9/BY
4/26	D1	5567.99	629.58	**31.48**	Change in zone A+ of 4/19 to zone D1 revealed this WkEd per Section 209 which invalidates the S1/BY/1 Signal of 4/18 per Section 102(A)1. **See Footnote (a) for explanation.** Consider closing the buy position generated by S1/BY/1 Signal as well as S9/BY Signal regardless of SSR. Note in Table 102F that SSR did not generate S5 buy signal.
(4/29)		5573.41	630.42		For information only
(4/30)		5569.08	630.47		For information only
(5/1)		5575.22	630.20		For information only
(5/2)		5498.27	620.05		For information only
5/3	D1	5478.03	618.06		For information only

Footnotes:

(a) If zone was determined for week ending 4/19/96 using the procedure described in Section 209, S1/BY/1 of 4/19/96 would have been invalidated per Section 102(A)1.

SECTION 702
STOCKS TRADING CASE STUDIES

Some of the mistakes commonly made by some investors are illustrated in the following case studies that will be helpful and serve as references in making future decisions:

Case Study #ST1

Stock: Public Service New Mexico
What did you do? Bought at $14.00 on 12/18/89
Why did you do?

One of the investment advisory services, in their November 1989 Report, recommended this stock very highly with convincing figures and facts.

Comment: In their January 1990 report, the stock was considered to be one of the undervalued utilities and was considered as a best buy.

What happened?

For several weeks, the stock prices fluctuated around $14.00. The methodology described in Section 302 generated a buy signal on 1/26/90 at $14.75 and a sell signal on 3/16/90 at 12.875.

There after, stock prices began declining making new lows after new low.

Did you sell the stock?

No. No courage to accept loss. Hoped for the best and thought the worst was over.

Where did you go wrong?

Ignored the sell signal of 3/16/90 generated by the methodology described in Section 302.

Relied on the advisory service's report.

Relied on its low price-to-book value ratio.

Did not pay attention to deteriorating stock prices which could be an indication of forth coming poor earning report, or some other bad news.

What lessons did you learn?

Don't pay attention to lucrative and tempting articles. Investigate before investing using the methodology discussed in Chapter 3.

Do not get influenced by what you read—remember the objectives of the writers of such articles may not be the same as yours; they may be written for other purposes.

Don't ignore the signals generated by the methodology described in Section 302.

Low price-to-book value ratio or low price-to-earning ratio is no guarantee for a stable price. To determine how low is low, check the past history of last two to three years.

Learn to cut losses quickly without any feeling.

Case Study #ST2

Stock: TCF Financial

What did you do? Bought at $13.25 on 12/18/89

Why did you do?

12/11/89 issue of Barron's, under "Investment News & Views" section featured article on this company. The article brought out two major points which were attractive: (1) Company is expanding its business in nearing states and (2) Because of the low price-to-book value ratio, it is a potential candidate for a take over.

What happened?

A sell signal was flashed by 10-wk stock buy/sell rules (see Section 302) on 10/27/89 at price $12.125. Stock slowly started falling, made new low of $9.625 on 4/20/90 and kept making new lows after new low.

Did you sell it?

No. Hoped for someone to make an offer for a take-over. Relied too much on low price-to-book value ratio.

Where did you go wrong?

Not selling the stock as per sell signal generated by the methodology described in Section 302.

Stock had good fundamentals but it was technically poor.

Did not pay attention to deteriorating stock prices which could be an indication of forth coming poor earning report, or some other bad news.

What lessons did you learn?

Don't pay attention to lucrative and tempting articles; they may have been written for other purposes. Always investigate before investing using the methodology discussed in Chapter 3.

Don't ignore signals generated by the methodology described in Section 302.

The low price-to-book value or the low price-to-earning ratio is no guarantee for a stable price. To determine how low is low, check the past history of last two to three years.

Case Study #ST3

Stock: Alta Gold

What did you do? Bought at $5.75 on 1/31/90

Why did you do?

Based on the advisory service's special report on Alta Gold Company. Report strongly recommended the stock as the top pick, and mentioned that once the institutions have discovered this stock, price could double in no time, even if the gold price stayed level.

What happened?

Sell signal per Section 302 occurred week ending 3/3/90, two months after you bought the stock at $5.75. Soon after, stock began declining and declined to around $4. You thought, it couldn't go any further lower and therefore, you bought some more at $3.75 on 6/19/90 in order to average the cost down and hoped that the advisory service's prediction would come true. It didn't happen. Stock slowly went down to below $1.00.

Did you sell it in time?

No. Did not believe the sell signal of 3/3/90 generated by the methodology dscribed in Section 302.

Where did you go wrong?

Did not trust the sell signal of 3/3/90.

Relied too much on the advisory service's recommendations.

What lessons did you learn?

Don't believe what you read; there could be many reasons why someone is very bullish. You would never know those reasons. It should be noted that recommendations are opinions; they don't have to be right all of the time.

Believe the signal. if you had sold when the sell signal was flashed by the 10-wk stock buy/sell rules discussed in Chapter 3, you would have avoided the disaster.

Don't accumulate as the price declines—it is like throwing good money after bad money.

Case Study #ST4—Refer to Section 404(E) for details.

Stock: Nu-Tech-Bio-Med, Inc.

Background:

February 1997 issue of MoneyWorld, on page 23, under "Special Advertorial Feature" included advertisement of the above mentioned stock citing the following stock points:

- Stock exchange: Nasdaq; Trading symbol: NTBM; Recent price: $13.62; 52-week range: $13.50 to $16.87; Current shares out: 2,038,000 and Fiscal year ends: December 31, and many others.
- **Key investor points enumerated in the advertisement, just by reading them, were tempting, luring investors into investing their hard-earned money to strike it rich quickly.**

What happened?

By September, 1997, the stock was trading around $1.00—losing almost its entire value.

What lessons could be learnt?

Don't believe the advertisement. Investigate before investing.

It is always a good practice to monitor the stock in accordance with the methodology described in Section 302 if indeed the stock was bought with a fear of missing the opportunity of striking it rich.

Case Study #ST5—Refer to Section 404(E) for details.

Stock: InnovaCom (Symbol MPEG, Listed on Electronic Bulletin Board)

Background:

You learned about this company from an advertisement published in magazine of one of the airlines and decided to investigate. You contacted the company for more information hoping that the company would give you the facts that you need to make a wise decision. Company sent you their usual newsletters and news bulletins which, in general, sounded so good to lure any investor into investing in this stock. The company also indicated that they had applied for the Nasdaq listing and waiting for the decision. The special write-up, titled "People's Stock of the Year" dated January 2, 1997 which predicted the short-term and medium-term price ranges of $8 to $10 and $11 to $15 respectively, and a preliminary long-term price range of $40 to $50. The stock was trading around $3.50 in January 1997. This special write-up was written with convincing arguments tempting investors to risk small capital in the hope of a big gain.

What happened?

Stock was trading around $3.50 until August 1997. Stock later slowly drifted down and traded below $0.25 by August 1998—a total loss of entire capital.

What lessons could be learnt?

If a special situation like the one presented here or in Case Study #ST4 comes by and the stock was bought with a fear of missing an opportunity of striking it rich. it must be monitored, without fail, in accordance with the methodology described in Section 302 even if it takes time and effort for collecting Friday's closing prices.

SECTION 703
MUTUAL FUNDS INVESTING CASE STUDIES

The following case studies are self explanatory and reveal few helpful hints:

Case Study #MF1

Mutual Fund: Janus Venture Fund
What did you do? Sold at $43.373 on 7/26/95
Why did you do?

In anticipation of the market correction. Because the market had advanced so quickly in a relatively short period of time after the long-term buy signal of 1/6/95 (Note: DJIA from around 3700 in December of 1994 to around 4700 by July of 1995, a 1000 points gain in about seven months. By tradition, market generally performs poor during the month of October.)

What happened?

By December of 1995, the price rose to $54.33 as the market continued its advance, making new highs after a new high. Note that the price was $53.80 when a long-term sell signal occurred on June 28, 1996 (see Table 103S in Appendix B).

What lessons did you learn?

Don't outsmart the market; never predict what the market would do next.

Never sell long-term holdings without a long-term sell signal.

Case Study #MF2

Mutual Fund: PBHG Growth fund
What did you do? Invested $1000 on April 20, 1995
Why did you do?

PBHG Growth fund was featured as the best buy in one of the Mutual Fund market letters and it was noted that the fund soon would be closed to new investors.

Comment: Why invested only $1000?

- In order to participate and not to miss if the recommendation proved to be right. At the time, market seemed to be too high.
- In the hope of that market could decline and would provide better opportunity later for investing additional funds. Correction in the market was anticipated because the market had advanced over 550 points in five months from the low around 3700 in December 1994.

What happened?

Market correction occurred during July-August of 1995 around DJIA 4600-4700, i.e., after gaining additional 400 points.

After the June 1996 long-term sell signal, fund was sold in September for $1720.27 with a gain of 720.27 in about 17 months—an average annual simple return of 50.84%.

Note that the value of the fund was approximately $1580.00 when the long-term sell signal occurred in June 1996—a gain of $500.00 in about 14 months which translates into an average annual simple return of 49.71%.

What lessons did you learn?

Assumptions about the market in that the market was too high and sitting on the sidelines in anticipation of market correction could result in a lost opportunity.

Section 704
Index Options Trading Case Studies

Option trading rules are described in Section 304. Case studies are included in Appendix B under Chapter 7-Tables and they typically illustrate the methodology involved in trading options. They may serve as references in future trading. Each case study illustrates different conditions or situations; case study CO9 is worth reviewing.

Case study CO9 demonstrates what could happen if we trade options based on logical assumptions, and then not following the plan. Remember, when we incur large losses, such as in case study CO9, we can easily lose confidence and become disable to act and make appropriate buy and sell decisions in a timely manner in the future. Such attitudes will generally translate into our behavior toward the people surrounding us whom we love the most.

◆ Reminder ◆

Application of the methodology and use of the case studies
do not necessarily guarantee profits in all cases;
they merely serve as means to become a skillful investor.
No one ever knows with certainty what the market will do...

Appendix A

Contents

Appendix A

MISCELLANEOUS

A1
DEVELOPING MOVING SUMS

The calculation of Moving Sum (MS or ms) involves adding up the five (if 5-day or 5-wk Moving Sum is to be determined) most recent daily or weekly values. In the following Table, the calculation of 5-wk and 10-wk Moving Sums is illustrated.

WkEd -Row#	B = 5-Wk Moving Sum	C = 10-Wk Moving Sum
(1)		
(2)		
(3)		
(4)		
(5)	B5 = (1) + (2) + (3) + (4) + (5)	
(6)	B6 = B5 + (6) – (1)	
(7)	B7 = B6 + (7) – (2)	
(8)	B8 = B7 + (8) – (3)	
(9)	B9 = B8 + (9) – (4)	
(10)	B10 = B9 + (10) – (5)	C10 = B5 + B10
(11)	B11 = B10 + (11) – (6)	C11 = B6 + B11
(12)	B12 = B11 + (12) – (7)	C12 = B7 + B12

To calculate a 10-wk, etc. moving sums:

The calculation of a 10-wk moving sum (say C10) using 5-wk moving sum column is easy. It is simply arrived at by adding two 5-wk moving sums, 5 weeks apart (e.g., B5 & B10)

Similarly, a 20-wk moving sum is arrived at by adding two 10-wk moving sums, 10 weeks apart and 30-wk moving sum can be calculated by adding three 10-wk moving sums, 10-wk apart.

The technique is easy to learn and can be mastered using a hand-held calculator. However, use of software (for examples, Excel, ClarisWorks, etc.) designed for performing these calculations will facilitate the process if a personal computer is available.

The other term used in Table 205A is "cumulative sum" (cs), which is simply a sum of all previous values from any selected starting point to week under consideration.

A2
DEVELOPING MOVING AVERAGES

(a) Introduction

It is not intended here to dwell on this subject in detail. Ample information on moving averages can be found elsewhere and it is easily obtainable. Only that which is relevant to the objective of this book is discussed briefly.

Many technicians and investors use moving averages for timing stocks and the market, in general. The application of moving averages used here is somewhat different from that which is customarily used. There are various forms of moving averages. A simple form of calculating the moving averages is more commonly used, and it is used here, also.

There can be as many forms of moving averages as one can imagine, for examples, weighted, exponential, modified, etc. A modified moving average can be calculated in many different ways in order to approximate best the market conditions. A special form of modified moving average is used here in Section 103(F) and Table 205B.

(b) Simple Moving Average

If a 5-day or 5-wk Moving Average (MA or ma) is to be determined, the calculation simply involves adding up t he five most recent daily or weekly values and dividing the sum by five. In the following Table, the calculation of 5-wk and 10-wk Moving Averages is illustrated.

WkEd -Row#	B = 5-Wk Moving Average	C = 10-Wk Moving Average
(1)		
(2)		
(3)		
(4)		
(5)	B5 = {(1) + (2) + (3) + (4) + (5)} ÷ 5	
(6)	B6 = {5 x B5 + (6) – (1)} ÷ 5	
(7)	B7 = {5 x B6 + (7) – (2)} ÷ 5	
(8)	B8 = {5 x B7 + (8) – (3)} ÷ 5	
(9)	B9 = {5 x B8 + (9) – (4)} ÷ 5	
(10)	B10 = {5 x B9 + (10) – (5)} ÷ 5	C10 = {B5 + B10} ÷ 2
(11)	B11 = {5 x B10 + (11) – (6)} ÷ 5	C11 = {B6 + B11} ÷ 2
(12)	B12 = {5 x B11 + (12) – (7)} ÷ 5	C12 = {B7 + B12} ÷ 2

To calculate a 10-wk moving average:

The calculation of a 10-wk moving average (say C10) using 5-wk moving average column is simply arrived at by adding two 5-wk moving averages, 5 weeks apart (e.g., B5 & B10), and dividing the sum by 2.

To calculate a 20-wk moving average:

A 20-wk moving average is arrived at by adding two 10-wk moving averages, 10 weeks apart, and, dividing the sum by two.

To calculate a 30-wk moving average:

A 30-wk moving average is arrived at by adding three 10-wk moving averages, each 10 weeks apart and dividing the sum by three.

The technique is easy to learn and can be mastered using a hand-held calculator. However, use of software (for examples, Excel, ClarisWorks, etc.) designed for performing these calculations will facilitate the process if a personal computer is available.

(c) Special Modified Moving Average

A special modified moving average can be calculated by combining two different set of figures in a fashion that can best yield the results consistent with the market conditions.

The general form of the special modified moving average is:

> This week's special modified moving average = Sum of "X" times this week's current or other pre-selected value + (1-X) times previous week's special modified moving average or any other pre-selected value, such as simple moving average. The multiplier "X" must be less than 1.00.

Examples of special modified moving averages are Vm% and Im% where X = 0.20. Refer to Table 205B in Appendix B for details.

Whenever a special modified moving average is used in developing a buy or a sell signal, a initialization period of several weeks may be necessary to generate reliable signals. This is because a special modified moving average, in certain cases, is dependent upon the starting value.

A3
Developing Point & Figure (Pt/Fg) Charts

It is not intended here to dwell on this subject in detail. Ample information regarding construction of point and figure charts can be found elsewhere and it is easily obtainable. Only that which is relevant to the objective of this book is discussed briefly.

A point & figure chart is used exclusively in the stock market by many technicians and investors to detect & predict trends. The application of point & figure charts used here is somewhat different from that which is customarily used.

A point & figure chart is easier to construct and maintain than any other type of chart, and is also easier to read and interpret than other charts. A point & figure chart is constructed on a simple graph paper, consisting of 10 blocks to an inch.

There are many ways to construct a point & figure chart; each chart will look different, based on the scale selected. The basic parameter for construction of a point & figure chart is the price value assigned to each block.

X's are used when the prices are moving up, and O's are used when the prices are moving down. Columns of X's and O's alternate-they never appear in the same column.

A full three blocks of price change is necessary for a direction change from X-column to O-column or from O-column to X-column on a point & figure (Pt/Fg) chart. Once a direction has been established, each one box price change in the same direction is recorded.

When a column of X's exceeds the previous column of X's. it is considered a bullish pattern and "X" is recorded in Table 203; and when a column of O's moves below the previous column of O's, it is considered a bearish pattern and "O" is recorded in Table 203.

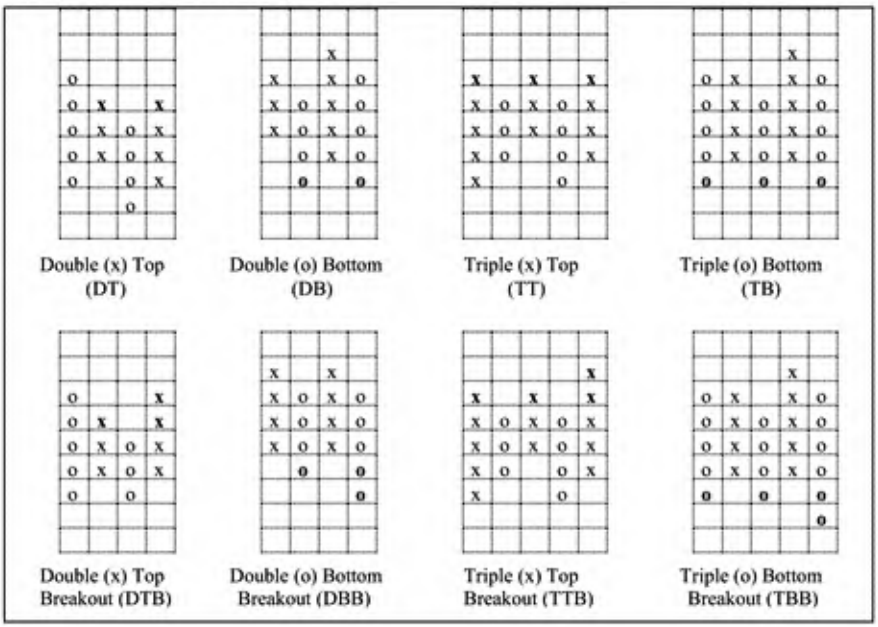
Table 203 shows the status of point & figure charts for the market indexes (DJIA, DJTA, SPX, VLG and OEX). "X" indicates the chart has a bullish pattern and "O" indicates the chart has a bearish pattern.

The units of charting to be used for market indexes DJIA, DJTA, SPX, VLG and OEX are:

For values:	up to 1250	Each block represents 2 points
	Over 1250	Each block represents 5 points
	Over 2500	Each block represents 10 points
	Over 5000	Each block represents 20 points
	Over 10000	Each block represents 50 points

In constructing Pt/Fg charts, only daily closing prices are to be used.

The following patterns will be helpful to understand bullish and bearish formation of Pt/Fg charts: double top (DT) and triple top (TT) breakouts are bullish; double bottom (DB) and triple bottom (TB) breakouts are bearish patterns.



Appendix B

Notes:

Appendix B contains market data ending July 30, 1999.

Although market data are obtained from sources believed to be reliable, but they are not guaranteed.

Contents

Appendix B

FILLED-IN TABLES

For ease in reference, the system used for numbering the tables includes section number and sub-section number where appropriate. For example, Table 102A translates into sub-section A of Section 102 in Chapter 1.

INDEX OF TABLES

Chapter 1: Tables 100

Chapter 2: Tables 200

Chapter 3: Tables 300

Chapter 6: Tables 600

Chapter 7: Tables 700

(A) OEX Call Options (CO)—Case Studies

(B) OEX Put Options (PO)—Case Studies

Table 102A—LOG OF S1 SIGNALS

Form 102A Page: 1

Yr.	Week End. (Date)	Zone	MC	Index IO	Index VI	$\frac{1+N}{2}$	$\frac{1+N}{2}$ %	Signal or Warning	Except-ion	Remarks	Act-ion
85	10/4	A	2/3							Zone A begins	
85	12/6	A+	5/0							Zone A+ begins	
86	3/7	A+	5/0	OT1						See Table 102B	
	4/4	A+							EB	Shp-Decl-wk	
	4/4	A+	2/3	OT2	Sbc			S1/SL/4	ED1a		---
	4/11	A+	1/4						WA	Per Warning WA →	CSP
	(4/14) 4/18	A+	3/2	IN1							
	(4/28) 5/2	A+	2/3	OT1				S1/SL/4	ED1a	See Remark #1	---
	6/6	A+	2/3		Sbc			S1/SL/4	ED1a		---
	(6/9) 6/13	A+	3/2	OT2				S1/SL/4	EG1	See Remark #1	---
	7/25	A+	0/5	IN1		1393	62.25				
	8/1	C1	0/5		Sbc	-496	58.20	S1/SL/4	EA1 ED1a		---
	8/8	C1	0/5			-1528	55.00			D=1783; OEX=223	
	8/15	C1	3/2		SbcV	368	55.74	WB		WB in Bull Phase →	CSP
	9/5	C1	3/2		Sbc						
	9/12	D1	0/5						EB	Shp-Decl-wk	
	(9/24) 9/26	D1 D1	2/3 2/3	IN1							
	10/24	D1	2/3		Sbc	174	56.79				
	10/31	D1	3/2			382	56.40				
	11/7	D1	3/2			364	56.49				
	(11/13) 11/14	D1	3/2	OT1		96	55.81	S1/SL/4		See Remark #1	Sell
	11/21	D1	4/1		SbcV	1649	56.94	WA, WB		Per Warning WA →	CSP
86	12/26	D1	2/3	IN2						See Table 102B	
87	3/20	E2	5/0		Sbc						
	3/27	E2	3/2								
	(4/1) 4/3	E2	3/2	OT1				S1/SL/4	EG1	See Remark #1	---
	5/8	E2	3/2	IN1						See Table 102B	
	6/19	->A+	4/1							Zone A+ begins	
	7/3	A+	5/0	OT1							
	8/7	A+	4/1		Sbc	3669	66.86	S1/SL/4	EA2b	8th week in zone A+	---
	8/14	A+	5/0		SbcV	4238	68.32	WA, WB		WB in Bull Phase →	CSP
	8/21	A+	3/2		Sbc	3405	67.86	S1/SL/4	EG1	See Remark #1	---
	8/28	A+	3/2								
	(8/31) 9/4	A+	1/4	OT				S1/SL/2	ED1a	See Remark #1	---
	9/18	A+	1/4		Sbc			S1/SL/4	ED1a		---
	9/25	C1	0/5								
87	10/2	C1	3/2								

Legend: SbcV = Sbc is voided per Section 102(A)3 = WB; BbcV = Bbc is voided per Section 102(A)3 = WB.
Remarks: 1. When S1 signal occurs during the week, it is suggested to wait until the week is concluded per Section 213 before committing funds.

Table 102A—LOG OF S1 SIGNALS

Form 102A Page: 2

Yr.	Week End (Date)	Zone	MC	Index IO	Index VI	I+N 2	I+N 2 %	Signal or Warning	Exception	Remarks	Action
87	(10/8)			OT				S1/SL/4		See Remark #1	
	10/9	C1	0/5		Sbc				ED1a	Shp-Ded-wk	
	10/30	B	1/4							Zone B begins	
	11/20	B	2/3		Sbc						
	11/27	B	3/2	IN1	SbcV						
87	12/4	B	0/5		Sbc						
88	1/22	B	3/2						EB	Shp-Ded-wk	
	1/29	B	4/1	IN1							
	2/12	B	5/0		Bbc			S1/BY/3	EB2bi ED2b	EB2bi & ED2b met R30&R40 " 1.010	Buy
	6/3	D3	4/1	IN				S1/BY/3	EA1		---
	7/15	D3	4/1	OT1						See Table 102B	
	7/22	D3	1/4		Sbc			S1/SL/4	ED1a		---
	8/12	D3	0/5						EB	Shp-Ded-wk	
	8/19	→A	0/5		Sbc			S1/SL/4	EA2a ED1a	Zone A begins	---
	9/2	A	0/5	IN2						See Table 102B	
	9/23	A	3/2	OT1	Sbc			S1/SL/4	EA2a		---
	11/11	A	2/3		Sbc			S1/SL/4	ED1a		---
	11/25	A	0/5	IN1						See Table 102B	
88	12/16	A	2/3		Sbc			S1/SL/4	ED1a		---
89	2/3	A+	5/0							Zone A+ begins	
	2/10	A+	3/2	OT1	Sbc			S1/SL/4	EA2b	1st week in zone A+	---
	(3/7)	A+	3/2	IN1							
	3/10	A+	3/2		Sbc			S1/SL/4	EA2b	5th week in zone A+	---
	(3/22)	A+	2/3	OT1				S1/SL/4	EA2b	7th week in zone A+	---
	3/24	A+	1/4						ED1a		
	4/7	A+	1/4		Sbc			S1/SL/4	EA2b ED1a	10th wk in zone A+	---
	4/14	A	1/4							Zone A begins	
	5/19	A+	5/0							2nd Zone A+ begins	
	6/16	A+	4/1	OT2	Sbc			S1/SL/4	EA2b	5th wk in 2nd A+	---
	6/23	A+	4/1						WA	Per Warning WA →	CSP
	7/7	A+	3/2								
	(7/11)			IN				S1/BY/1	ED2b	See Remark #1	
	7/14	A+	4/1						met	R30&R40 = 1.012	Buy
	8/11	A+	4/1		Sbc	4765	70.56			See FtNt. (a)	
	(8/17)			OT2				S1/SL/4	EG1	See Remark #1	
	8/18	A+	3/2			3876	69.72				---
	8/25	A+	4/1		SbcV	4498	70.17	WA,WB		WB in Bull Phase →	CSP
	9/15	A+	2/3		Sbc			S1/SL/4	ED1a		---
89	10/6	A+	2/3		Sbc			S1/SL/4	ED1a		---

Legend: SbcV = Sbc is voided per Section 102(A)3 = WB; BbcV = Bbc is voided per Section 102(A)3 = WB.
Remarks: 1. When S1 signal occurs during the week, it is suggested to wait until the week is concluded per Section 213 before committing funds.
FtNts.: (a) Sbc of 8/11 cannot be used with OT2 of 6/16 to generate a S1/SL signal because S1/BY signal of 7/11 is between OT2 of 6/16 & Sbc of 8/11.

Table 102A—LOG OF S1 SIGNALS

Form 102A Page: 3

Yr.	Week End. (Date)	Zone	MC	Index IO	Index VI	$\frac{I+N}{2}$	$\frac{I+N}{2}$ %	Signal or Warning	Except-ion	Remarks	Act-ion
89	10/13	A+	1/4							Shp-Decl-wk	
	10/13	A+	1/4	OT				S1/SL/4	ED1a		---
	10/27	A	0/5		Sbc			S1/SL/4	ED1a		---
	12/15	C1	2/3		Sbc	-2091	46.76	S1/SL/4	ED1a		---
	(12/19)			OT2				S1/SL/4	ED1a	See Remark #1. WB	
	12/22	C1	2/3		SbcV	-1478	45.86	WB		NA in Bear Phase	---
89	12/29	C1	4/1	IN1							
90	1/12	C1	2/3		Sbc			S1/SL/4	ED1a	Shp-Decl-wk	---
	1/26	D1	0/5						EB	Shp-Decl-wk	
	2/9	D1	0/5	IN						S1/BY/1 CNM	
	2/16	D1	0/5		Sbc						
	3/2	D2	2/3		Bbc	-2726	41.30	S1/BY/3	EB2bi	EB2bi cond. met	Buy
	3/9	D2	3/2			-3209	40.95				
	3/16	D2	4/1		BbcV	-3523	38.60	WB		WB in Bear Phase →	CBP
	(3/27)			OT1							
	3/30	D2	4/1								
	(4/23)			OT1							
	4/27	D2	2/3								
	5/4	D2	4/1	IN1	Bbc			S1/BY/3	ED2b,c met	R30 = 1.006 & R40 = 1.015; SSR=33.87	Buy
	6/22	D1	4/1		Sbc	-236	48.83	WB		WB/NA (Bull Phase)	---
	6/29	D1	4/1		SbcV	1004	50.49				
	7/6	D1	4/1	IN1						See FtNt. (b)	
	7/20	B	3/2		Sbc						
	(7/24)			OT1				S1/SL/4	EG1	See Remark #1	
	7/27	B	2/3						ED1b	ED1b cond. met	---
	8/24	B	0/5						EB	Shp-Decl-wk	
	8/31	B	2/3		Bbc					See FtNt. (c)	
	(10/4)			IN1				S1/BY/3		See Remark #1	
	10/5	B	2/3		Bbc	-10094	24.87		EB2b		---
	10/12								EB	Shp-Decl-wk	
	10/12	B	2/3		BbcV	-10550	23.66	WB		WB in Bear Phase →	CBP
90	10/19	B	2/3		Bbc	-9584	24.99	S1/BY/3	EB2b	IN1+Bbc = S1/BY/3	---
91	1/18	B	3/2		Bbc	346			EA1		
	(3/14)			OT					S1/SL/2	See Table 102B	
	3/15	E3	5/0			6305	66.48		(CNM)		
	(4/1)			IN1				S1/BY/3	EA1		---
	4/5	E3	2/3			6929					
	4/12	E3	2/3		BbcV	6172		WB		WB/NA (Bull Phase)	---
91	(4/25)			OT1						No S2 conditions per	
	4/26	E3	2/3			3364				§102B developed.	

Legend: SbcV = Sbc is voided per Section 102(A)3 = WB; BbcV = Bbc is voided per Section 102(A)3 = WB.

Remarks: 1. When S1 signal occurs during the week, it is suggested to wait until the week is concluded per Section 213 before committing funds.

FtNts.: (b) Bbc of 5/4 & IN1 of 7/6 cannot be used to generate a S1/BY signal because Bbc of 5/4 is voided and the distance between Bbc and IN1 is more than 41 trading days (Exception EA1).

(c) Bbc of 8/31 & IN1 of 7/6 cannot be used to generate a S1/BY signal because S1/SL signal of 7/24 is between IN1 of 7/6 & Bbc of 8/31.