

KEVIN

HAGERTY

DAY TRADING COURSE

TRADINGMARKETS.COM Members, Welcome to My Five-Week Day Trading Course

In this first week of our five-week course on day trading, we want to define what the business of day trading is and what it is not. We will discuss the differences between professional direct-access day traders, and those traders attempting to accomplish the same thing through on-line brokerage firms with internet ISP hook ups.

The SEC has expressed many concerns regarding the explosive growth of on-line day trading, and we will address their concerns in this first installment of the course. We will explain why day trading is potentially a valid and rewarding business, but at the same time, we will make you acutely aware of the various hurdles you must overcome to succeed.

Successful day traders must maintain a proper psychology, mental attitude, and focus. In addition, you must work with superior technology, have sound money management strategies, and develop a thorough knowledge of the markets. Of most importance, you must understand the risks involved in trading stocks. I realize that this information may be dry, but it is essential that you have this base of understanding before proceeding.

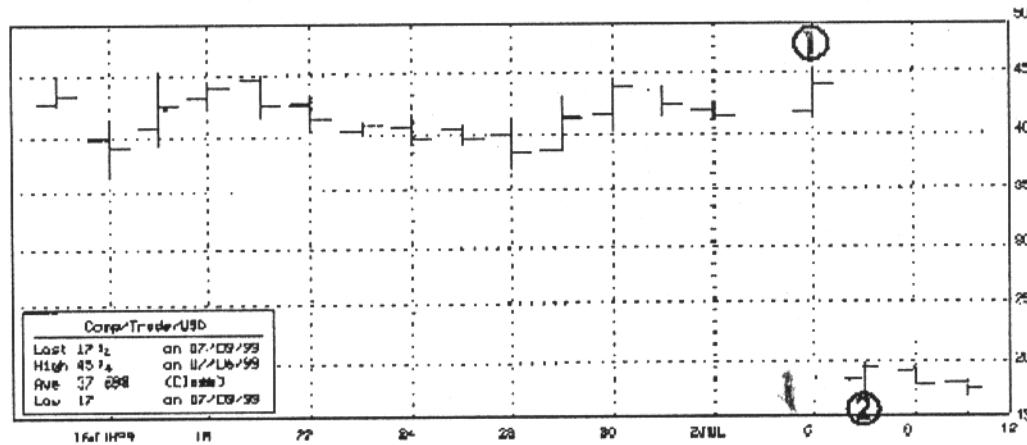
Day Trading Defined

The professional day trader is a person who trades stocks in the office of a registered broker dealer. With the right amount of training, experience and communications, some of these traders will eventually trade remote from their homes.

Registered broker dealer firms provide the direct access communications (T-1 lines) and electronic execution equipment/software that puts these traders the same execution access level as the Merrill Lynch's and Goldman Sachs's of the world. The software used for execution and monitoring the markets is often far more advanced than what I've seen or used on major brokerage firms trading desks. Day traders that work in this situation can compete on an execution basis with the NASD market makers and other electronic systems or ECN's.

Day trading by definition means that you end each day flat, meaning you go home without any open positions at the end of the trading session. Day trading is not taking home 500 shares of NEON at 44 on July 6, 1999 (see number 1 on chart) and watching it open on July 7, 1999 at 18 3/8 (see number 2 on chart). As you may recall, New Era of Networks, Inc. (NEON) announced a large earnings shortfall after the close on July 6, 1999. I use NEON as an example of the problems you can face by not ending each day flat.

NEON Daily Chart - 6/15/99 to 7/9/99



In the case of NEON, you would have lost most of, if not all of your equity and would have received a margin call that you would be unable to have met. No, this doesn't happen often but it only has to occur one time to possibly put you out of business. The media then runs a story about the perils of day trading which they, in reality, confuse with on-line brokerage trading where the person just gambled and took a shot. That kind of trade is not what the day-to-day business of trading is about.

Concern # 3

Investors buying securities on margin may not fully understand the risks involved. In volatile markets, investors who have put up an initial margin payment for a stock may find themselves being required to provide additional cash (maintenance margin) if the price of the stock subsequently falls. This is where many newer day traders run into problems.

If the funds are not paid in a timely manner the brokerage firm has the right to sell a securities position and charge any loss the investor. When you buy stock on margin you are borrowing money. As the stock price changes you may be required to increase the cash investment. You should make sure that you do not over-extend.

Translation: Don't buy it on margin if you don't have the allocated cash reserve to pay for it in cash. As mentioned earlier, a simple margin example of a trade that recently occurred was New Era of Networks, Inc. (symbol NEON). The NEON example will highlight margin risk.

Examples:

Trader B: started with \$11,000 of capital, was excited about the NEON Story and decided to maximize the position by utilizing the maximum regulation T margin allocation which is currently 2:1.

Trader B went for the roses and got the skunk. No more capital, wiped out and owed money to the brokerage firm.

Trader A vs. Trader B

Trader A made a better margin decision than Trader B because he could have met a margin call and still had capital left which was not the case for Trader B who had a deficit capital position and had to ante up cash to the brokerage firm.

As we progress in this course, we will discuss Trader A's and Trader B's understanding of money management, knowledge of the risks inherent in various types of stocks, and a trading plan that is geared to increasing capital rather than losing 50 to 100% on one trade or investment.

Almost forgot, thank you for reminding me. There is a Trader C.

Trader C: started with \$15,000 of capital, carried no positions home overnight, took no more than 1/4 - 3/8 point loss per trade, and takes trades in stocks that have a potential for 1 to 1 1/2 point profit.

On 6/6/99 Trader C made three trades in NEON profiting on one out of the three, yet used correct money management.

1. B 500 shares @ 42 1/8	S 500 shares @ 41 7/8	-\$125.00	-1/4
2. B 500 shares @ 42	S 500 shares @ 41 11/16	-\$156.25	-5/16
3. B 500 shares @ 42 1/4	S 500 shares @ 43 3/8	+\$562.50	+1 1/8
			+\$281.25
Commissions			<u>-\$90.00</u>
			+191.25

NEON opened at 41 3/4 on 6/6/99 and closed at 45 1/4. This is just an example and not an actual trade, but it points out what a good day trader is trying to accomplish. Keep your losses to a 1/4 - 3/8 of a point and try to make 1 point if the trade allows you to manage it that way.

In day trading you are limited by time and range, so you must manage your average loss and size with discipline. Trader C was correct on only one of three entries and still made a few bucks rather than being out of business on 7/7/99 when NEON opened at 18 3/8.

The Business

If you are to succeed at the day trading business, you have to run it like one. At the end of the trading day you take no position home overnight. By adhering to this discipline you avoid the overnight risks that traders A&B both had with NEON. Day trading is limited by time and the average range of the stock, but you will be in better position to control your risk and the size of your losses. This is the key part of the "traders equation".

The average size of a day trader's profit will be smaller than that of a short-term position trader because of time and range. Day traders will be stopped out much quicker than position traders due to daily market noise such as programs and announcements from brokerage firms and the companies themselves. The most important thing you must manage as a day trader is the size of your loss. Secondly you must manage a winning trade to maximize the profit on each trade. Your motto will become "make a point - lose a quarter". And you want to do this as many times as you can.

The Business (con't)

Day traders can maximize margin (Regulation T)

EXAMPLE: \$50,000 of capital with Reg. T margin of 2:1 can control \$100,000 in stocks. You can liquidate your position(s) and repeat the procedure time and again over the trading day.

Proprietary traders working for a NASD broker dealer are allocated increased leverage, which varies according to each firm. To qualify as a proprietary trader you must be U-4 registered at the firm, pass series 7 and series 63(or 62) and then pass the new series 55. This of course assumes you qualify as a trader.

Day trading margin of your full capital is certainly not as risky as overnight carry, but if they stop trading in a stock before you can liquidate your position and the news is bad you might find yourself in the same position as trader B.

"Day Traders Equation"

Maximum % of profitable trades + Maximum profit per trade - Small losses x Multiple trades = 's
SUCCESSFUL DAY TRADER

This equation is the real money management of day trading. Place it where you can see it the entire trading day to remind you of the objective - make money - control risk.

Maximum % of Profitable Trades

Day traders in an effort to keep losses small will get stopped out often and this makes it hard to maintain a high percentage of profitable trades. Our trading plan is to select the most promising opportunities; that is the stocks which are most likely to move in the direction of the trend with maximum range.

In order to accomplish this you will select from the strongest of the institutional stocks that have pulled back from their swing point highs or are coming out of consolidation in the direction of the trend (sells reversed).

You will be even more profitable if you learn to recognize the dynamics of supply and demand and not just some shape of a pattern or a formation. Buyers and sellers are constantly making decisions and we, as

traders want to be on the same team that is currently winning the war. We will cover these dynamics later in the course. Meanwhile, for practice when you are watching your stock(s), focus on:

1. Where the volume is trading, on the bid, midpoint or the ask.
2. What are the bid & ask doing – moving up or down?
3. Is the stock showing strong relative strength versus the day's trend?
4. How does the stock react to programs?
5. Does the volume increase on up days and decline on down days (sells reversed)?
6. Where are the blocks trading, on upticks or downticks?
7. Is stock closing better or worse than its VWAP (volume weighted average price).

It is not a pattern or system that makes you profitable but rather the dynamics that bring life to the stock's pattern. I will cover all these topics in the upcoming weeks.

Maximum Profit Per Trade

The stocks we look for must have room to run which means an average daily range of two points or more. When you enter the trade a good portion of the range should be available for profit. This is not a factor if your entry is above the previous close, but it can be if you are entering from a 5-minute chart pattern. Most traders have a tendency to take profits prematurely as they get nervous when a stock makes its normal pull back. You haven't traded if you haven't experienced taking a quick " point profit and then watched the stock run another 1-1/2 points. You probably sat there frozen, unable to pull the trigger again as the stock made new highs. Managing your trade to higher profit levels after normal pullbacks is harder than it seems. You start thinking about the money and your emotions get in the way.

Part of your learning process is to understand the normal characteristics of the stocks you trade. Is it a 1/2 up 1/4 back, or 1 pt up 5/8 back? Once you understand the normal pattern of the stock then you must decide by watching the dynamics of the stock as it trades to determine if the intra-day trend has changed, is supply definitely larger than demand, or is it just backing off on light volume and small programs. Your decision will determine whether you hold or exit the trade.

The better you get at understanding and recognizing the dynamics, the more proficient you will get at selecting stocks about to accelerate which will help in maximizing the profit per trade.

Small Losses

This is the part of the equation where you have the most control. If you can manage your losses, the profits will have a higher likelihood of happening even with average stock selection. It takes discipline and the proper mental attitude to determine your stop levels and execute the stop as planned.

What usually happens to new traders is they determine for example a stop loss level of no more than \$300 per trade. This can be .30 on 1000 shs or 1 point on 300 shs. It all depends on your money management plan and available capital. The stock gets to the stop level for the trader that is using a mental stop. The trader hesitates to pull the trigger because he sees a quick uptick but the stock then ticks 1/8 below his stop level and is offered there. The trader freezes and is now in a position of hope, which is forbidden territory for the day trader. If you keep taking bigger losses than normal you will have to increase the profit on your winning trades and/or the percentage of profitable trades. It is easier to control your loss side than to accomplish both of those because as a day trader we must trade under the limitation of a shorter time period and range of the stock. (Repeated for a reason!)

My advice to you is you will be better off if after you receive confirmation of execution that you immediately enter either a stop loss or a stop loss limit order to protect your exit from the trade. This takes the judgement out of your hands and protects you from your emotional-self, which is almost always wrong. This one rule alone will go miles in improving your trading.

The next most important thing to keeping your losses small is you don't have to wait until your stop loss point is hit before you exit a trade. When you enter a trade the market must prove to you the trade is correct by turning profitable within a short period of time. If the stock or the market dynamics change after your entry and

appear negative, just get out of your position. Don't wait for the market to collect your \$300 by taking out your stop. It is better to exit the trade. If you are correct you save some money. You are better off entering the trade again as it turns around and trades up through your entry point.

Multiple Trades

You don't have to be a math major to figure out that if your percentage of profitable trades is positive you want to maximize the amount of trades. A good example of this would be all the recent splits we have seen in many of the top institutional trading stocks such as GPS, EMC and DELL. Instead of average daily ranges of 3 – 4 points they are now 1 3/4 – 2 1/4 points.

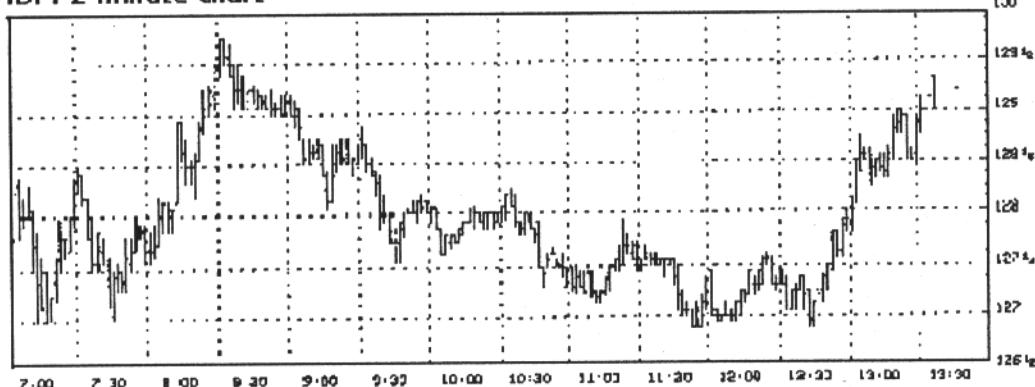
This decrease in range size makes it tougher to get the 1 – 1 1/2 point profit from each trade, but you can take a larger amount of 1/2 – 3/4 point profits and do it more often because these kinds of stocks have what I call an excellent "Travel Range."

A recent example of travel range is IBM on July 21, 1999 (shown on next page). The stock opened at 127 1/2, down 3/4 from the previous day's close. We don't include this gap down in our calculation. On the day, IBM ranged from a high of 129 3/4 to a low of 126 7/8, only 2 7/8 points.

The Travel Range

Measuring between intraday highs and lows as the day progresses, the travel range for IBM that day was 21.47 points or 16.8% if you divide that by the opening price of 127 1/2. It had 11 moves of one point or more. After the opening at 127.50 the sequence is as follows from left to right:

IBM 2-minute chart



Yes, it was a volatile day with the S&P futures and program trading but there are many stocks that have travel ranges at least twice their average daily ranges. Do the homework and find these stocks because when you do you will realize that stocks take on their own life because of such things as specialist tendencies, active options traders and market makers, programs and of course the institutions (The Generals).

There is another group called the accelerators, which we will discuss, in another chapter.

Concluding Remarks

After reading this CHAPTER ask yourself if you will do the following:

- 1.Understand the risks of day trading.

2. Take no position home overnight.
3. Act on what the market is telling you and not what you hear or read. Free yourself of any preconceived notions of imposing your will on the market.
4. Cut your loss on a position when the market proves it not correct. This doesn't mean you wait for your stop to get hit before you exit.
5. Work hard at developing a trading plan to select trades, manage trades and exit trades.
6. Select the technology and communications necessary for direct access execution.
7. Manage the "Traders Equation". You must understand how when each part of this equation changes it effects your profitability. Manage the loss side and your hard work will take care of the profit side

These are all cut-and-dry rules. As boring as they are, they must become the cornerstone of your trading.

Enjoy your week, re-read this chapter, and next week we will start in on the good stuff.

Best regards,
Kevin Haggerty

TRADINGMARKETS.COM Members, Welcome to Week Two of My Day Trading Course

Stock Selection

The stock selection process that I believe is most beneficial to day traders is one which focuses on the primary stocks that institutions depend on to outperform the S&P 500. These stocks demonstrate strong relative and absolute performance to the Index. Most of these stocks are in the S&P 500 index and have excellent liquidity.

Our job as traders is to identify the stocks that the Generals are currently adding to and overweighting in their portfolios. It is the herd mentality which creates the momentum that leads to many of the parabolic rises we have seen in this bull market. There is nothing better than getting good entry in strong momentum stocks that have pulled back only to have the Generals and momentum players take them up again. Also helping this process are the "ACCELERATORS," which are the hedge funds, program traders and sometimes the specialists and option market makers.

To better appreciate the stock selection process I will try to give you some background on how a growth fund manager thinks, and how he builds the fund portfolio.

How Fund Managers Think

In order to beat the S&P 500, institutions must be in the right sector and in the right names. Their goal is not just to match the S&P 500, they want to beat it. In order to achieve this they must differ from the Index. To help accomplish this they have built excellent internal research capabilities and, in addition, they have access to the best brokerage firm research that is available.

There are many talented analysts and portfolio managers at these institutions so there isn't much left to chance in the search for good companies. They get page one information because of the multi-millions of dollars they pay in commissions to the brokerage firms.

Most growth fund managers are bottoms up stock pickers, which means they closely examine the business prospects of each company and build their portfolios stock by stock. They adhere to the fact that stock prices tend to follow earnings over time, and to the extent that earnings forecasts are revised upward or downward, stock prices often will head the same direction. Most managers don't try to predict near term stock performance. Instead, they spend their time looking for companies that can grow earnings faster than the overall market and that are trading at attractive valuations. There are many factors that can make stocks rise or fall over the short term, but in the long run, earnings determine stock valuations. Therefore, a fund manager looking for the best chances of appreciation will choose those stocks that are fairly priced or undervalued.

When mutual funds receive new money, a fund manager will often add to existing positions as long as the fundamentals remain solid for a particular stock. This assumes a stock still has strong relative and absolute

performance to the S&P 500, and it is this buying that creates a trend. A fund manager will attempt to buy good stocks on pullbacks and sell weak stocks on strength. Many of the momentum players just want to keep buying if the stock is up, but as soon as they have any sizable amount of shares offered to them by a brokerage firm's trading desk they might just disappear and turn seller themselves because the stock has reached a supply level and the stock can't be pushed any higher until the seller(s) complete what they are trying to get done.

The herd mentality prevails when it gets down to the high relative performance stocks such as we have seen in the technology and Internet sectors. A fund manager may think there is a high degree of risk in certain tech stocks, but those companies may be producing fast earnings and helping the performance of the fund in the battle to beat the S&P 500. (So they might even stay too long.) This helps prolong the upside action as we get multiple upside breakouts after brief pullbacks. With a little help from momentum players, programs, hedge funds and the media hype that goes with these stocks, you are given many opportunities for strong day trading action.

The AOL Example

A good example of this mentality is AOL, which was the largest contributor to several funds' performance during the last part of 1998 and the first quarter of 1999. It had a parabolic move to the upside. Only those managers that had the stomach to bet on investor psychology instead of visible earnings got the full performance benefit, but many jumped on the bandwagon at higher and higher levels afraid to be left at the gate. Surprisingly, even some value funds rationalized reasons to buy AOL. While arguing that AOL made sense for a value fund is a bit of a stretch, it does show how a herd mentality can drive a stock substantially higher. I hope those managers made good sales on the way down. If the fund managers decide to play the AOL game again, price and volume will let us know the "GAME IS ON."

Portfolio Adjusting

Institutions are constantly increasing or trimming existing portfolio positions based on valuations, and they are also adding new positions or deleting underperformers from the portfolio. For example, a fund might have held a maximum of 10 million shares of AOL and because of the first-quarter froth and subsequent weakness, the fund may have cut back to 4 million shares. With the stock now down over 60% from its highs, fund managers might again decide to start adding to the position. Once the decision to add to a position is made, it often attracts the attention of other large players. This is what trend reversals are all about.

Reversals like this usually take place around the 200 day moving average as more institutional players become confident that the move is for real. As the perception sinks in, the Generals jump aboard.

Another example would be an institution that is taking a bearish top down view of the market and now must realign its sector weightings. The theme would favor stable earnings, quality, low beta and yield, which translates to consumer, staples – utilities, energies, and maybe gold. Energies and golds both usually do relatively well in a bear market. This defensive list of groups would be overweighted and sectors such as high beta technology stocks would be underweighted.

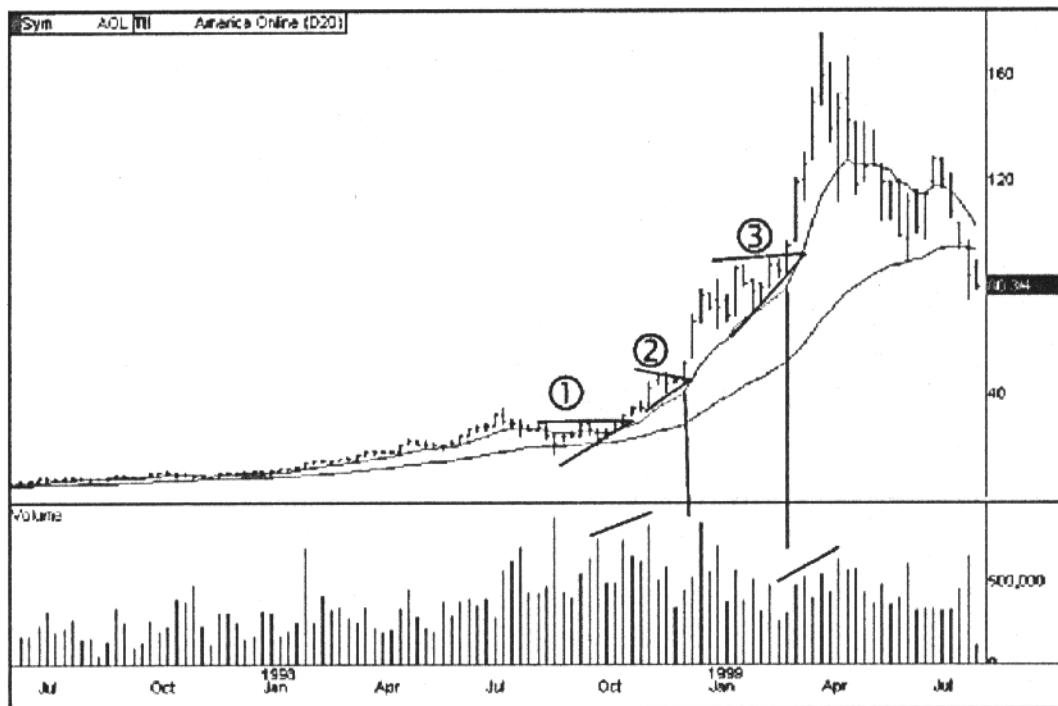
This flow of money moving between sectors is very visible because most institutions are on the same page. It's just that some are ahead of the pack. A good example of this is when many of the institutions loaded up on some of the techs during the market crack from July – October of 1998. Two other recent examples of money flows going into unloved sectors are the energies and basics during March and April of this year. [See Charts Later in Chapter]

The selection process will detect these moves based on price and increased volume in addition to increasing relative strength. When stocks trend they become tradable for day traders as the many different institutional players get involved.

Day traders that select stocks from a matrix of high relative strength and earnings are by definition picking the stocks with the best technical and fundamental prospects to move significantly higher. The institutions will have to own and overweight many of these stocks if they are to beat the S&P 500. Their research analysts will continue to be our research department.

The following charts address the topics that I have just discussed. I provide brief analyses at the bottom of each chart that should draw together the various points I want to emphasize to you.

America Online (AOL)

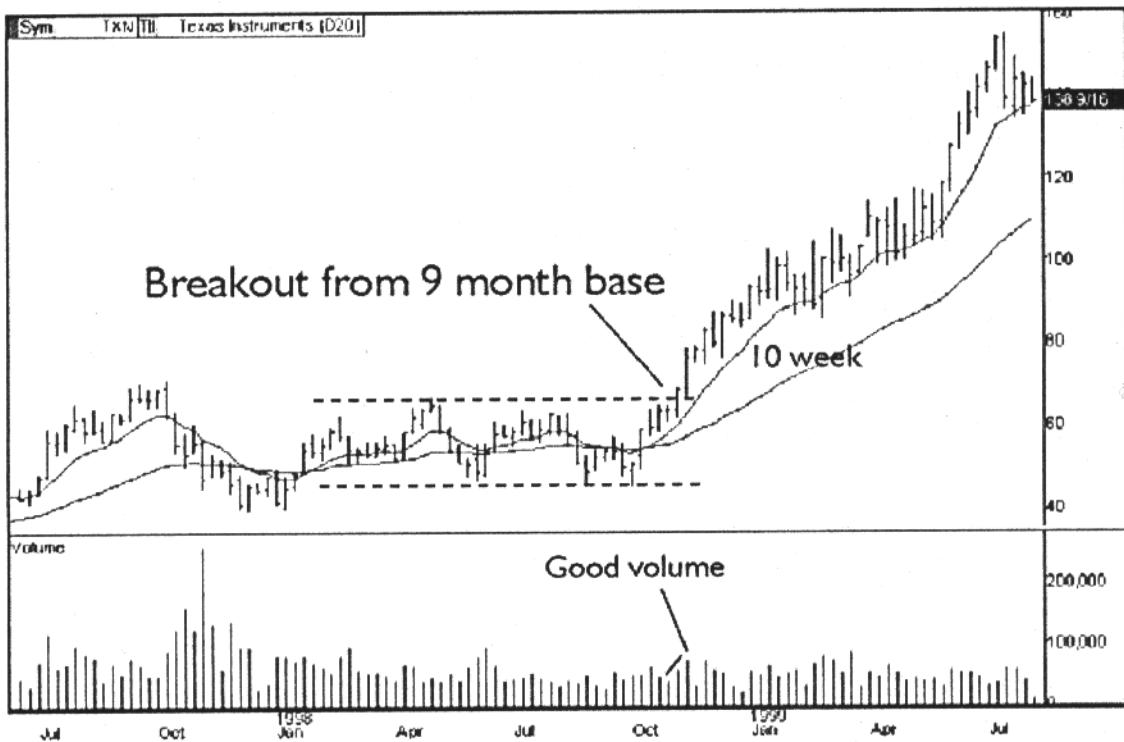


1. & 2. WRB (Wide Range Bar) breakouts on panic volume. If you did not get in at 1 the left behind portfolio managers entered at 2, afraid they would miss a further major move.

3. This run up from an ascending triangle was again on a WRB or Runaway Move as Mark Boucher refers to in his course. He refers to them as a Thrust Breakout, Breakaway LAP, and Breakaway GAP.

This AOL example contains three favorite institutional patterns that they will aggressively attempt to breakout, market permitting.

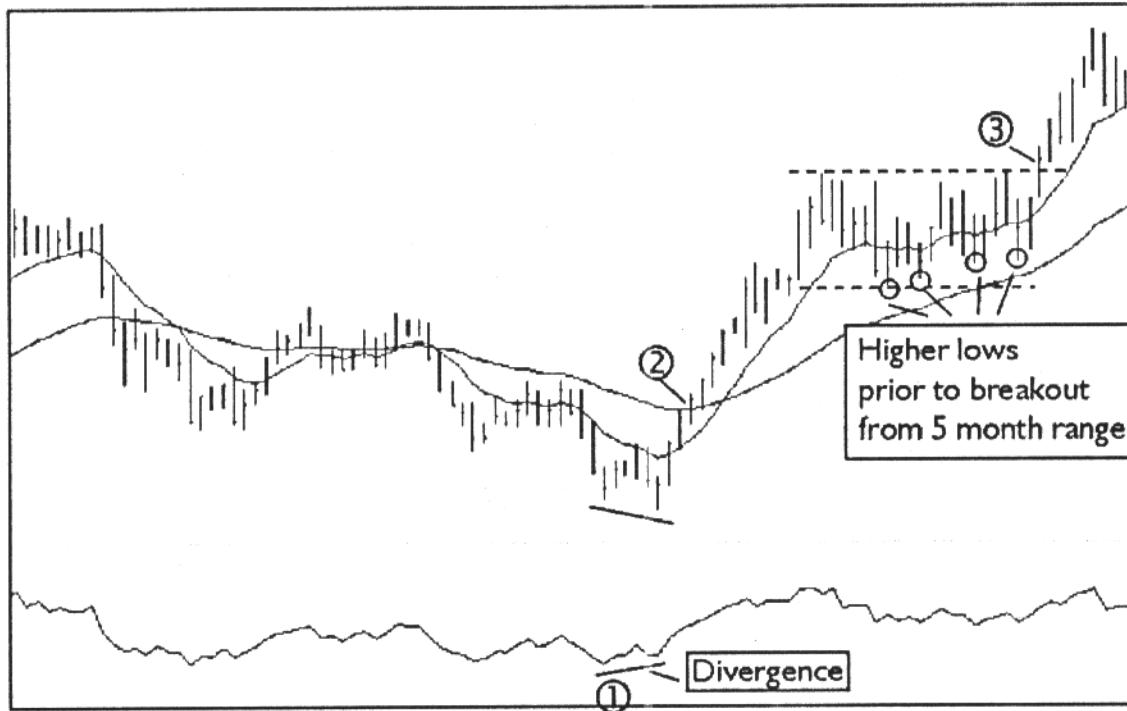
Texas Instruments(TXN)



1. Breakout of 9 month base on good volume. This breakout was confirmed by S&P 500 trend (see Spyder Chart)
2. The 10 week and 40 week EMA's were both rising and the 10 week was above the 40 week.
 3. The S&P 500 was also above its 10 and 40 week EMA's.
 4. TXN was now trending as it traded above both its 10 week and 40 week EMA.
 5. TXN became a day traders stock at this point, and now you start looking at your daily charts for entry at inflection points which we will cover in Weeks 3 and 4.

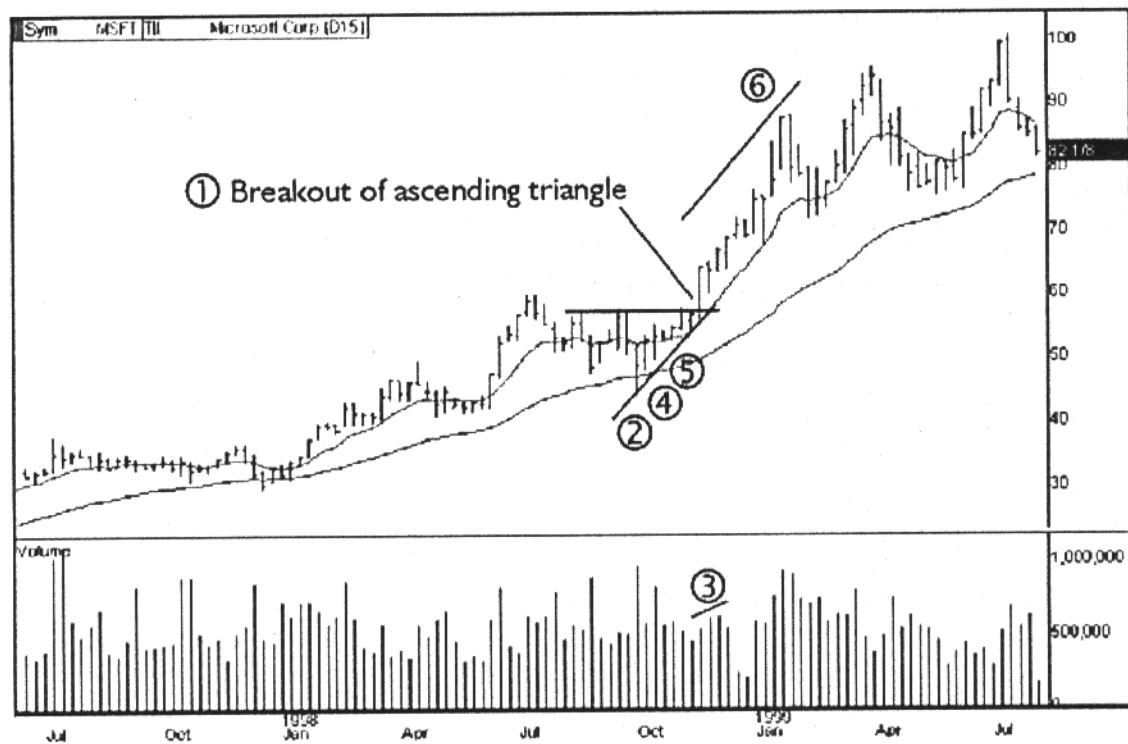
1. SPY which is a proxy for the S & P 500 broke out to a new level and is above the rising 10 week and 40 week EMA's.
2. The trend in both TXN and SPY were up.
 3. You want to day trade advancing stocks in an uptrending market.

Phix Semiconductor Index (SOX)



1. Positive Divergence preceding breakout 2 above 40 week EMA.
2. The breakout by TXN from a 9 month base was confirmed by the rising trend in SOX.
3. Five month trading range breakout preceded by rising lows in the range. The semiconductor stocks entered a prime daytrading zone after this breakout because of the strong momentum.

Microsoft (MSFT)

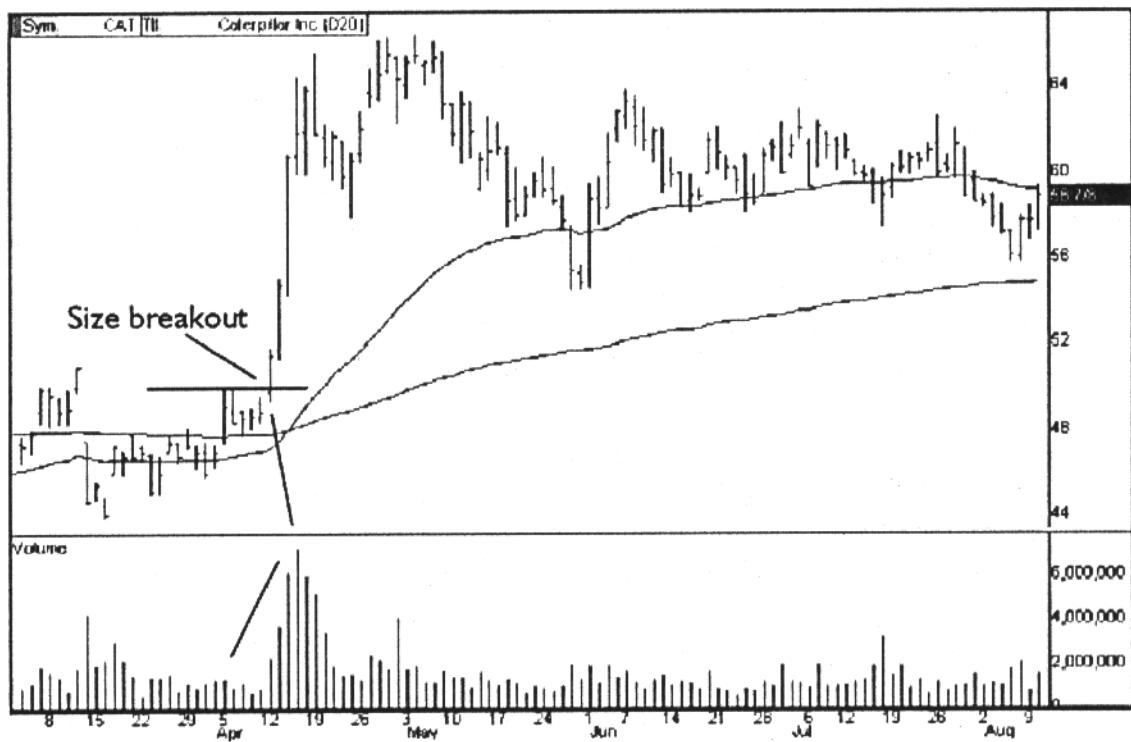


1. Breakout of ascending triangle on a WRB (wide range bar) with expanding volume. (See 3).

2. Bottom fishing as MSFT broke below and closed above 40 week EMA for the week and had higher highs and higher lows the next two weeks. (see 4 & 5) During this time, the Generals were adding to their positions.

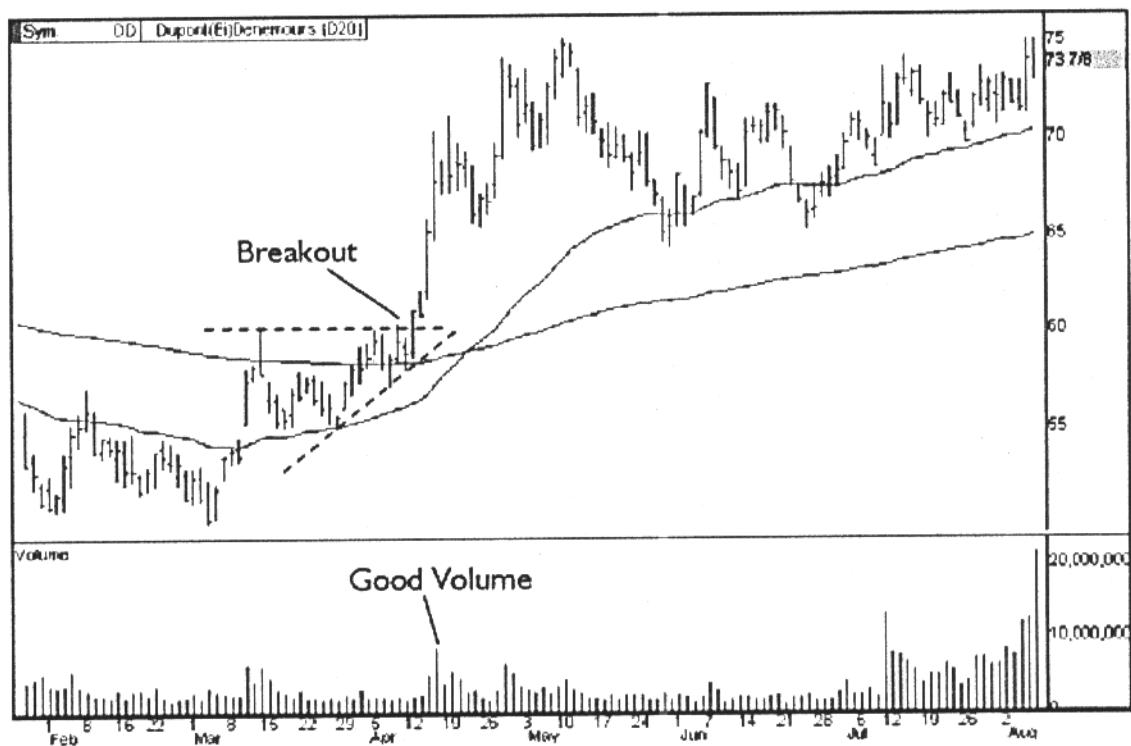
6.GREAT DAY TRADING ZONE, MOMENTUM PLAYERS WERE IN BIG.

Caterpillar (CAT)



1. There was a rush to cyclicals such as CAT, DD, and AA as the Generals all jumped in at the same time.
2. Volume had been building prior to WRB breakout.
3. Institutions love to break them out of the consolidations just above the 50 and 200 day moving averages.

DuPont (DD)



1. Breakout above rising 50 and 200 EMA that is turning upward.
2. Breakout is an good volume.

Key Points Re-Cap

Before we identify and discuss the filters to select your day trading stocks (same filters can be used for short-term position traders), lets quickly recap some key points:

We want stocks that have:

Strong relative and absolute performance versus the S&P 500

Excellent liquidity, which means good volume and narrow spreads.

The best technical and fundamental prospects to move higher

Are members of S&P 500 or NDX 100 indexes, so we can benefit from the added volatility that program trading provides. If the market shifted away from big caps, which is unlikely near term, we will make the same adjustments the General make to outperform the S&P 500.

Uptrending stocks (sells reversed) are better day trading stocks than range bound stocks.

We want the momentum players on our team and as many accelerators that want to play the game as possible.

Stocks with volatility and good average daily range.

Use the Generals as our research department. Let them select the stocks – no one does it better. We will select those stocks to day trade that are in the strongest uptrends and where we spot those situations when the buyers are more aggressive than the seller(s). In the final part of the process it's what IBM is going to do in the next two minutes that matters most. Remember, though, that you don't go to war unless you prepare for war.

Understand that stocks will present more dynamic short term trading opportunities when they are under or fairly valued and they run out of buyers at the extreme valuations.

General Filters

A. Skim Investors Business Daily (IBD) and The Wall Street Journal for any stock specific news or pending economic announcement.

B. Review the market action of the prior day -- which I keep by hand -- it takes 10 minutes and all the data is available from IBD. If you keep it by hand, you think about it, and you have records of how the market reacted at certain inflection points such as volume, breadth, moving average, swing point highs and lows. You would be amazed at how often markets repeat. This simple worksheet will be an exhibit in chapter 5 with a full month of data recorded for you.

C. Check the earnings calendar for next four weeks and the brokerage firms' upgrades and downgrades. The site I use for this is www.dailystocks.com. This site is free, comprehensive and includes many other links of information and data you will find useful.

Specific Filters

TRADINGMARKETS.COM Interactive RS Investigators Search

This filter gives you the top relative strength stocks versus all other stocks from a universe of 5,000 most actively traded stocks. It is not the RSI (Wells Wilder RSI) that measures the stock against itself which we all use as a momentum indicator. The filter covers the past 12 months weighted more to recent action. If the stock has corrected sharply but still shows a RS of 98 or 99, its because the 12 month advance was significant and the current correction is probably small, in terms of percentage of the overall advance.

Search # 1

RS value = between 80 – 99

Price Filter = more than 25 (only because of recent splits, the higher priced stocks will give you better absolute move)

Volume Filter = more than 400,000 shares

The volume is what the stock traded that day, not the average daily volume of the stock. I prefer the stock to have an average daily volume of at least 500,000 shares for the past 30 – 50 days. The filter for 400,000 allows for a lower than normal volume day.

Search #2: The second part of the filter is to run it again with RS values between 60 and 79.

This catches stocks that might be correcting back to their 50 and 200-day Exponential Moving Average's (EMA's), which present some good opportunities. After these corrections you will often see the Generals add good stocks on short-term market weakness and where the brokerage firms like to time their recommendations.

Search #3: The third part of the filter is to run it with the RS value between 90 and 99 and no other criteria. This gives you the top relative strength stocks of the 5000 stock universe regardless of price and volume.

The first three examples give you an idea of whether a stock is in a runaway mode, pulling back briefly from swing point highs, or consolidating after Wide Range Bar (WRB) thrusts or gaps. To understand the filters and which stocks are found you must go through each chart so you get the feel for any lag in the filter.

Search #4: If you decide to trade the 50 dollar and over big cap stocks only, then a good filter to use is:

RS Value: between 80-99

Price Filter: more than 50

Value Filter: more than 750,000

TRADINGMARKETS.COM ADX Trend Finder

If I had to choose one filter from TRADINGMARKETS.COM it would be this one: The higher the ADX the stronger the trend up or down. When you combine ADX with Plus Directional Movement (+DMI) and Minus Directional Movement (-DMI) you will always discover a good trade opportunity. The ADX filter allows you a maximum of 10 values. For uptrends you set up +DMI > -DMI (reverse equation for downtrends).

Search #1

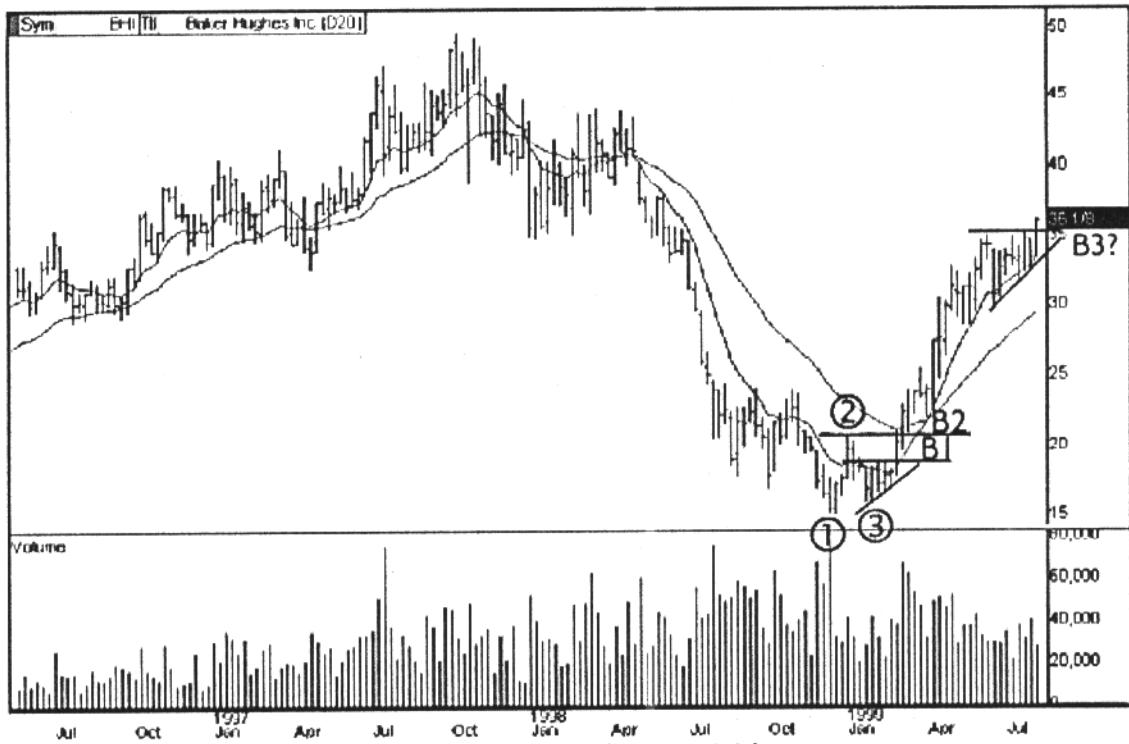
ADX Value 1 – 10
PX Filter more than 30
Vol. Filter more than 500,000
Trend Filter +DMI > -DMI

The next step is to increase your ADX value by ten until you run out of stocks (11-20, 21-30, 31-40 etc...), but everything else remains the same.

Yes, I know the higher the ADX the stronger the trend but you are forgetting about directional movement. Often times a stock that has had a WRB or gap breakout will consolidate and trade sideways before the next runaway move or reversal in trend. These consolidations are great spots for the Generals to show their cards. Halliburton (HAL) gave us a warning on August 4th with increased volume that it might break out of an ascending triangle. The next day we got good entry at 48 1/8 and the stock traded to 50 7/8 before closing at 50 1/2. On August 4th the energies all did well on increased volume, which told us the Generals, were working the floor and had to reach for stock. Baker Hughes (BHI), which you see on Search #1, has an ADX value of only 10, but is one of the top 10 stocks in percentage gained for the last six months with an 83.5% gain. We want to play this stock as soon as we see a volume signal from the Generals with a close in the top part of its daily range. (Charts illustrating this follow).

By starting with a low position ADX and working upward, we are sure to catch all of the consolidations that usually lead to excellent moves or the beginning of a trend reversal. When you look at the charts, start with the highest ADX values first because that's where you will find the 3 – 5 – 8 day pullbacks, WRB Thrusts, and dynamite short term continuation patterns. When you get to the lower ADX values you pick up the consolidations such as the HAL and BHI. As long as +DMI is > than -DMI all of the ADX values can find you an opportunity to monitor for a high probability trade.

Baker Hughes (BHI)



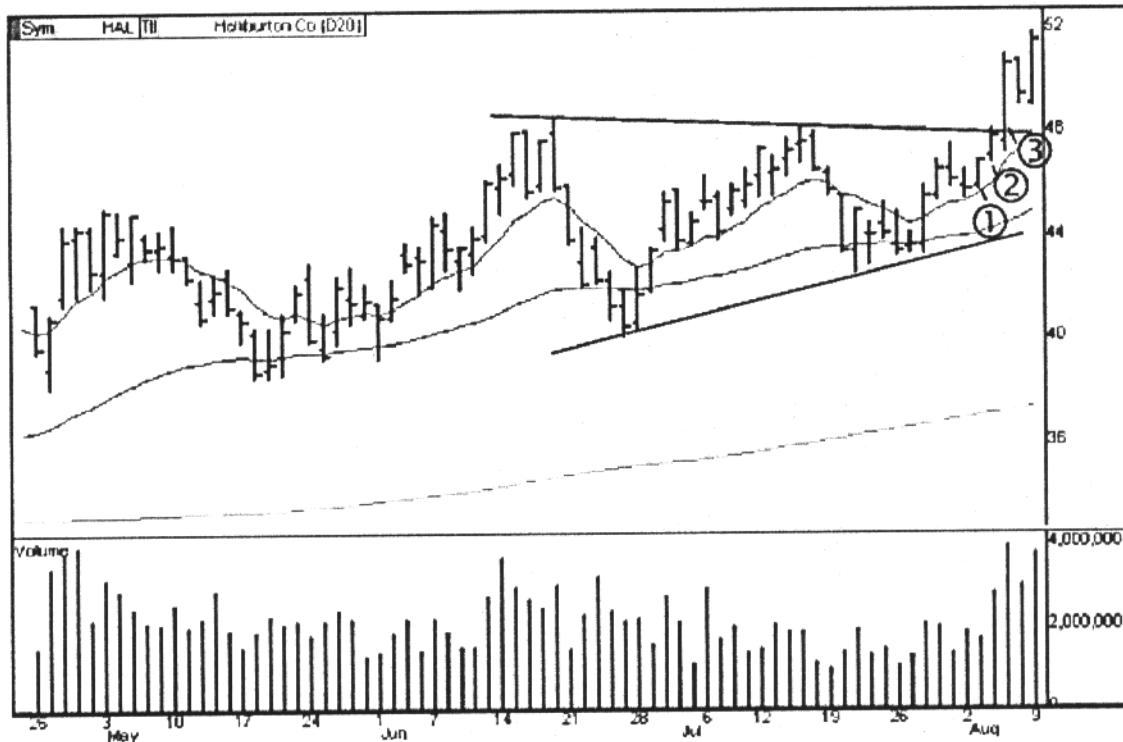
1. After a big, 5-wave down move, BHI forms a 1-2-3 bottom.

2. At B1, the Generals come for the stock in size, breaking it out of the ascending triangle, ascending wedge, or whatever else you would like to call it. The key point is that at the B1 inflection point, BHI traded above the highs of the previous 4 – 5 weeks and did so on big volume. The "GAME WAS ON" at that point.

3. At B2, BHI makes a new high above swing point 2 after making a high low at swing point 3. The stock trades and closes above both the 10 and 30 week EMAs. The trend at this point is up, and BHI becomes very tradeable regardless of whether you day trade or position trade.

4. At B3, will BHI breakout of this consolidating range? I don't know, but we will see the Generals give us a warning before it does. (Note: As I am writing this, BHI breaks out of the ascending triangle on good volume at 11:30 AM on 8/9/99 and is trading at 35 5/8, up 2 1/2).

Halliburton (HAL)



1. (8/3) HAL closes in top of range.

2. (8/4) Closes in the top of range on good increase in volume. The Generals look like they want to break it out. Entry will be 48 1/8 on 8/5.

3. (8/5) HAL opens at 47 1/2 and gives good entry at 48 1/8 and trades to high of 50 7/8 and closes at 50 1/2. Volume is excellent.

(8/6) Pullback day.

(8/9) Surges to 51 3/4

Note: This was good day trade and also good position trade.

Concluding Remarks

After reading this chapter and working with the Filters, you will be on your way to gaining part of your edge which is the selection of high octane trading stocks which have the following characteristics:

- Strong relative and absolute performance versus the S&P 500.
- Strong trending stock with high ADX and confirming directional movement.
- High RS and EPS combination which puts you in the top momentum stocks.
- Excellent liquidity and good average daily range.

By selecting stocks with the best technical and fundamental prospects to move significantly higher you will often be trading stocks that are beginning or are in the explosive stage of their trend.

The key to that movement is for you to recognize early that the Generals are coming for the stock and then take only the well planned entries you will learn or re-discover in weeks 3 and 4.

Have a good trading week. We'll see you in Week 3.

Best regards,
Kevin Haggerty

TRADINGMARKETS.COM Members, Welcome to Week Three

During week two we presented a successful and proven method of selecting stocks to trade for any time frame. By selecting stocks with the best technical and fundamental prospects to move significantly higher, you will often be trading stocks that are beginning or are in the explosive stage of their trend. These stocks will be the ones needed by the Generals to outperform the S&P 500 and the same stocks that the momentum players will run and gun.

Our selected time frame is day trading, and in this chapter we will explain the various market and stock dynamics that will help you identify when the Generals are active which will lead to higher probability trade selection. Remember, we are talking about S&P 500, NDX 100 or any other high volume liquid institutional stock. We are not talking about illiquid momentum OTC stocks with very little depth below the bid or offered side of the market.

Illiquid OTC Stocks

The patterns and trade recognition that you will learn in weeks 3 and 4 don't require you to be a pro at level II execution skills which are much more involved than many trading firms advertise. If you expect to enter the day trading business and start trading OTC momentum stocks with spreads of 3/8-1/2 with big travel ranges and you have no real experience in this trading business, I will sell you ice in January. You might as well donate the money to your favorite charity because 95% of you will lose. The only place you should attempt to learn those skills is at a direct access-trading firm, and learning those skills takes time.

Liquid Big Cap Stocks

There is excellent volatility and momentum in the Big Cap liquid OTC names that you can trade just as you would IBM in the New York Stock Exchange. You don't have to be concerned with SOES and SelectNet which are shadows of what they were when the OTC day trading business heated up. The market maker requirements are 100% (and 100 shares only) in favor of the market maker. The expansion of ECN's has helped and hopefully will continue to help expand liquidity, improve execution speed, and remain relatively inexpensive.

Herd Mentality

Sooner or later every stock runs out of gas, or in other words, the rubber band has stretched the limit. Brokerage firms never sell, they just hint at it. Fear of heights and not booking profits start the ball downhill then the herd mentality sets in and you get a severe correction as we have just witnessed in AOL. Once it starts, there are opportunities on the short side for day traders, which we will illustrate in weeks 3 and 4. I strongly recommend that as an individual trader or investor that you never take a naked short position home overnight. If you feel that strongly about shorting an institutional stock you should do it in one of the following ways with options: 1.) Long Put; 2.) Bear Spread (Put or Call); 3.) Put ratio backspread, which has limited risk and unlimited reward; 4.) Synthetic Straddle, which would be long calls/short stock or long stock/long puts. The synthetic straddle is for traders that want to trade the position by making adjustments according to the deltas of the options. This course is not about options so unless you are educated in options don't utilize them in your trading plan unless you understand everything about their usage.

Short Selling Risks

Why do you think so many short selling funds have gone belly up or have suffered drawbacks so large that money has run to the exits from these funds? Also, there are many institutions and hedge funds that can't wait to squeeze an obvious short or sector when the opportunity presents itself, and it usually occurs when your short looks perfect. With limited funds and experience are you ready for that kind of risk and exposure? Forget about it. Get an education in options where you can define or limit your risk or just stay with intra day shorts.

Every day, institutions, hedge funds, momentum players, program traders, specialists and market makers are making decisions to buy or sell stocks for various reasons. Other than the very few neutral days, either the sellers or buyers have the upper hand on a given day(s). As day traders you don't pick a stock's direction, (which is chance at best) you get on the trade as the stock changes direction which is considerably different.

Individuals vs. Institutions

As a day trader you have the least amount of information of any of the players involved in the stock. The institutions buying and selling the stock that day know what they want to get done. The brokerage firms that are talking to these specific accounts are trying to generate commissions by getting a good piece of business done. They know to a great extent what the institutions are trying to buy or sell and at what levels. Once the institution gives a brokerage firm the order to, in this case, sell stock (AOL), that order is passed along to the firms in-house floor broker or to an independent floor broker who is called a two-dollar broker.

As the brokerage firm is working the AOL sell order for the institution, their sales trading desk is making calls to various kinds of institutions trying to find buyers for AOL which would help the seller and also generate more commissions. The information flow now includes the institutions that gave the sell order to the brokerage firm, the floor broker on NYSE, the specialists on NYSE who now know there is an institutional AOL seller, and the various kinds of institutions that were called by the brokerage firm that was trying to leverage the AOL sell order. The institution that initiated the AOL sell order is also getting calls from other brokerage firms regarding different stocks and possibly AOL. All of these institutional players have various levels of information regarding the supply/demand level of AOL that day which could influence their trading decision.

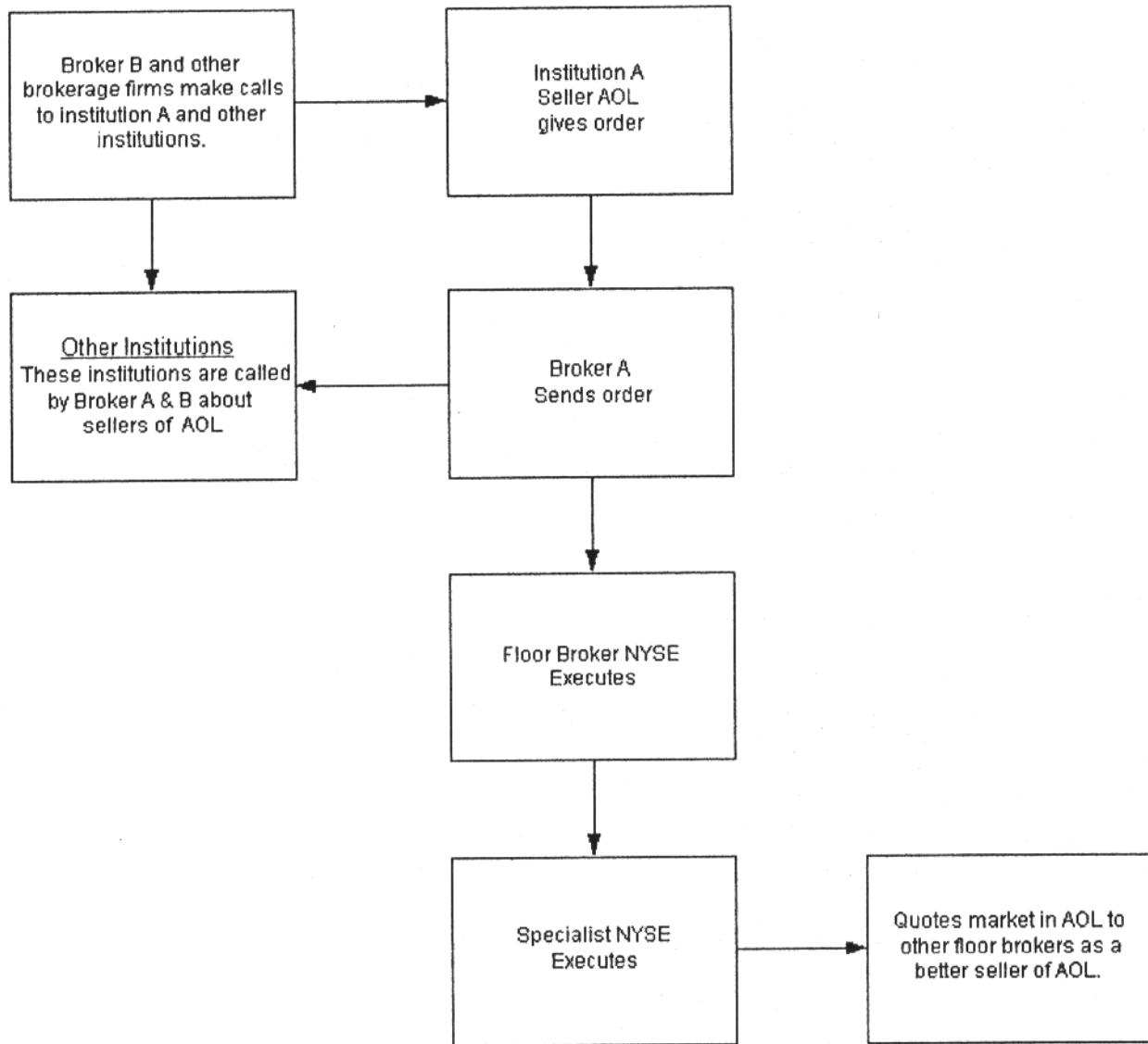
Order Flow Charts; Tracking the Generals

We are going to assume that the institution that initiated the AOL sell order received a call from other brokerage firms that there was another seller of AOL in the market. The order flow chart will give you a thumbnail sketch of the information flow that takes place between buy side, (institutions) sell side, (brokerage firms) and the NYSE floor, or in the case of a Big Cap OTC stock, possibly a major market maker.

As a day trader you don't get that information so you must understand and be able to identify the dynamics which tell you that the Generals are active in the stock and whether it is a high probability trade.

Order Flow Chart

This order flow chart gives you a good basic idea of how the information flow might influence the institutional urgency to buy or sell a stock.



Flow Summary

Institution A gives sell order to broker A.

Broker A sends order to NYSE floor broker for execution.

Floor broker works with specialist to execute order.

Broker A is calling other institutions trying to find a buyer for AOL. Sometimes the other institutions might be a seller of AOL, but won't tell broker

A if they are working their order with say broker B.

Broker B and the other brokerage firms are calling Institution A during normal course of business about stocks they have to buy and sell. Broker

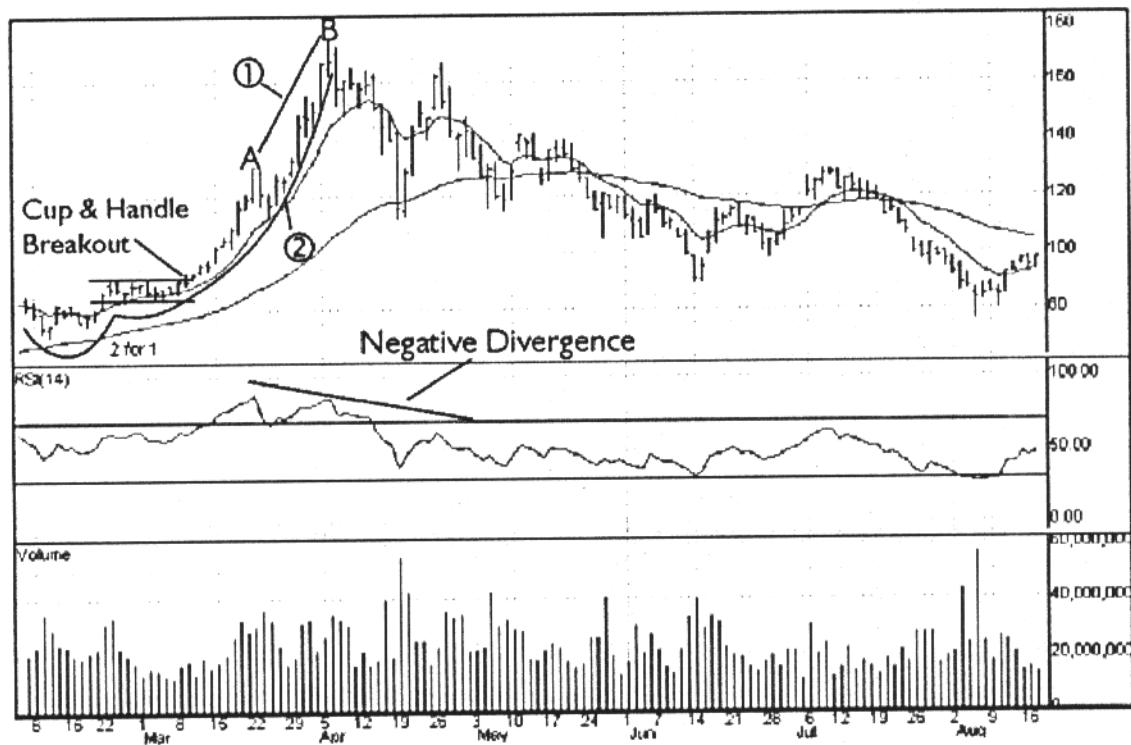
B tells Institution A that they are a large seller of AOL. Institution A doesn't respond because it is working a sell order with Broker A.

Broker B and the other brokerage firms are also making calls to many of the same institutions that broker A called as a seller of AOL.

Get the picture? Everyone now knows there is more than one institutional seller in AOL, and unless some buyers show up, the sellers will probably have to give up some price to get their orders completed.

The following charts illustrate how to effectively select key inflection points for short sales in a stock that has lost momentum and sellers obviously are stronger than sellers (buys reversed).

AOL Chart



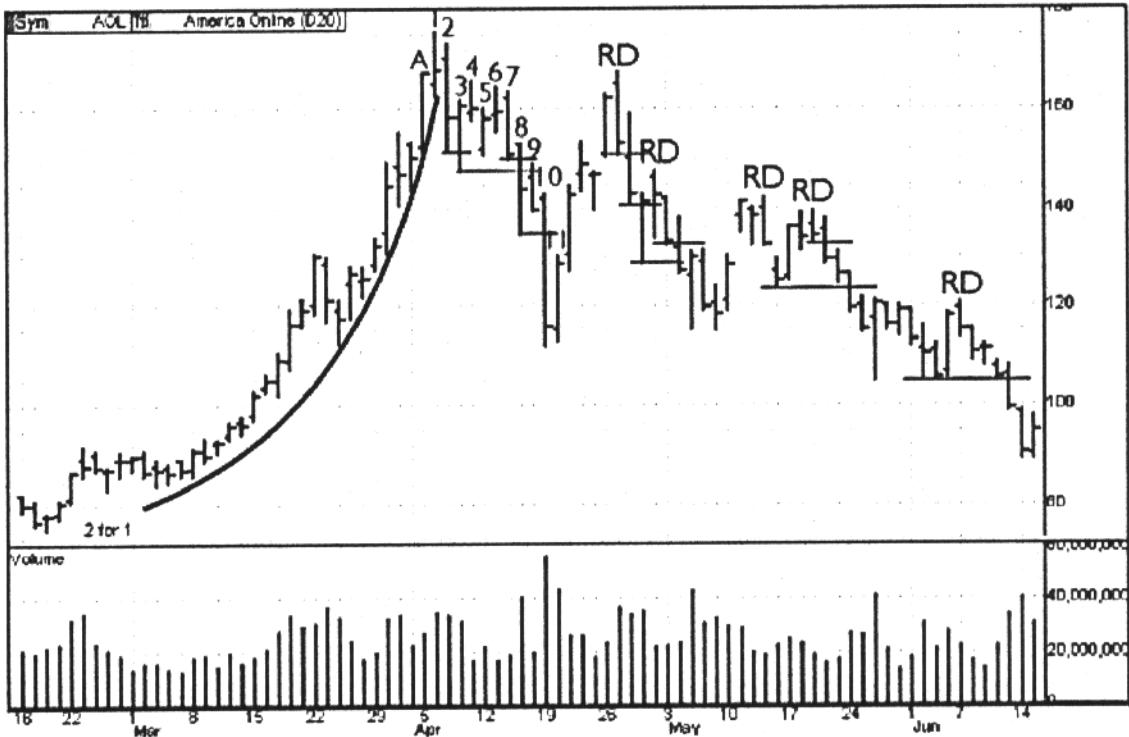
1. Parabolic rise by AOL after breakout of Cup and Handle pattern at 91 3/8. A negative divergence developed on this momentum player induced move to top.

2. It helps to utilize a curved trend line for parabolic moves which are usually broken by the first WRB reversal day as you see above.

After momentum fades on a parabolic move, there are usually some outstanding shorting opportunities for the day trader.

In this case we saw a negative divergence, breaking of parabolic trend line, and WRB reversal day on strong volume that followed a mini blow off top. AOL was now on your short side radar looking for a good entry point.

AOL Chart 2



(In the following discussion, please refer to this volume table).

4/5 A : WRB to a new high.

4/6 Day 1 : WRB to new high on strong volume, but closes below the midpoint of daily range.

4/7 Day 2 : Big reversal day on WRB. 20.625 points which is the largest range of recent data. Volume is heavy as AOL closes below the open, below previous low and in bottom 30 percent of its range. It also closed below parabolic trend line.

The close below the low of the previous Day 2 also confirmed change of direction and defined Day 1 as a swing point high.

4/8 Day 3 : Gave you a good short sale entry below 152 which was Day 2 low. Stock traded down to 148 before reversing and closing in top of range at 160.50. How did you manage your trade? In your trade plan you marked the 148 level as another possible short sale entry point.

Days 4, 5, and 6 : Gyrated up and down in a fairly narrow range, but you must notice they couldn't close above Day 3 close or high. Their opens and/or closes were all within Day 3's daily range. We have a consolidation that has now developed below the high, and we know that we plan to sell short breaking 148 low if AOL resolves to the downside.

4/14 Day 7 : Also closed within the daily range of Day 3, but this close on a WRB at bottom of its range at 150.875 raised our short trade entry point to 150 which is Day 7's low.

We still will enter a short sale below 148, but the Day 7 bar told us to enter first at a move below 150. If you look closely at Day 7 bar, you will see that it closed below the low of the last three days and below last seven closes. This told you the highest probability was down.

4/15 Day 8 : You get a trade through entry below 150 as the stock opened at 152.75 and went south to a low of 135. You could have added to your position as stock traded below 148. AOL closed the day at 143.875. Your next entry point is 1/8 below 135.

4/16 Day 9 : Inside day closes at absolute bottom of its range at 139.75. Momentum is still down, so you decide to enter short 1/8 below 139.75 on Day 10. The close is below the open, below previous close, and at bottom of range after sharp drop told you the sellers were still in charge.

4/19 Day 10 : AOL opens at 142, gives you entry at 139.75 and an add if so wanted trading below 135. The stock hit intra day low of 112 before closing at 115.875. This was selling climax volume for AOL as it rallied the next day on 42.7 million shares.(see table)

After a parabolic rise AOL lost momentum. Institution A started to sell stock as did Broker B's seller, and then the process starts to feed on itself as portfolio managers rushed to the exits in fear of not booking profits at windfall prices. There was, without much doubt, some able hedge funds that with a particular options strategy were able to accelerate the stock move down and capitalize on the herd mentality. As a day trader you were still able, without the same information, to trade in the correct direction by reading the stock.

You were able to enter trades at high probability inflection points on the daily chart that indicated the ease of movement was down. When you can combine this with solid intra day patterns you will get better at this business. The change in direction or reversal indicators we observed can be found on intra day trading charts as well.

On Chart II we discussed the initial three entries that saw AOL hit a low of 112. There were seven more good short sale entries from the daily chart after AOL rallied to almost 90% of the 175.50 high which is quite common for right shoulder tops which you see with AOL. I marked them on the chart and also identified the reversal day preceding entry.

Chart Summary

When you analyze a potential trade you are simply looking at the supply/demand situation of a stock. Is it higher highs and higher lows or lower highs and lower lows? Did the stock close above or below the midpoint of its daily range? Was the close in the top or bottom of its range? If it is to change direction it must trade above or below the previous periods high or low regardless of time frame. The longer the time frame the more significant the move.

As in our AOL example the Generals can't hide. In this case AOL ran into trouble on day 1 making a new high and just barely closing above the A day's high and close. Day 1 closed below the midpoint of its range on heavy volume, which indicated the stock might change direction. On day 2 the stock made a significant reversal as it closed below its open and well below the Day 1 low. It reversed on heavy volume, closed in the bottom 30 percent of its range and also took out most of the A day WRB move to new highs.

The sellers were clearly in charge as the Day 2 range expansion on a reversal day which was a wider range than anything preceding the 175.50 high was telling you that there was significant selling and sellers were giving up lots of price to get it done. All of this and the breaking of the curved trendline spoke of a change in trend and strong institutional participation.

Day 7 clearly defined a further downside move when it closed below the low of the last three days and below the last seven closes. The more lows or closes the higher probability of a move in direction in the close. At this point the sellers were getting more anxious because that 148 low was staring them in the face. Also, any of the accelerators that were in position to attack the sellers were salivating.

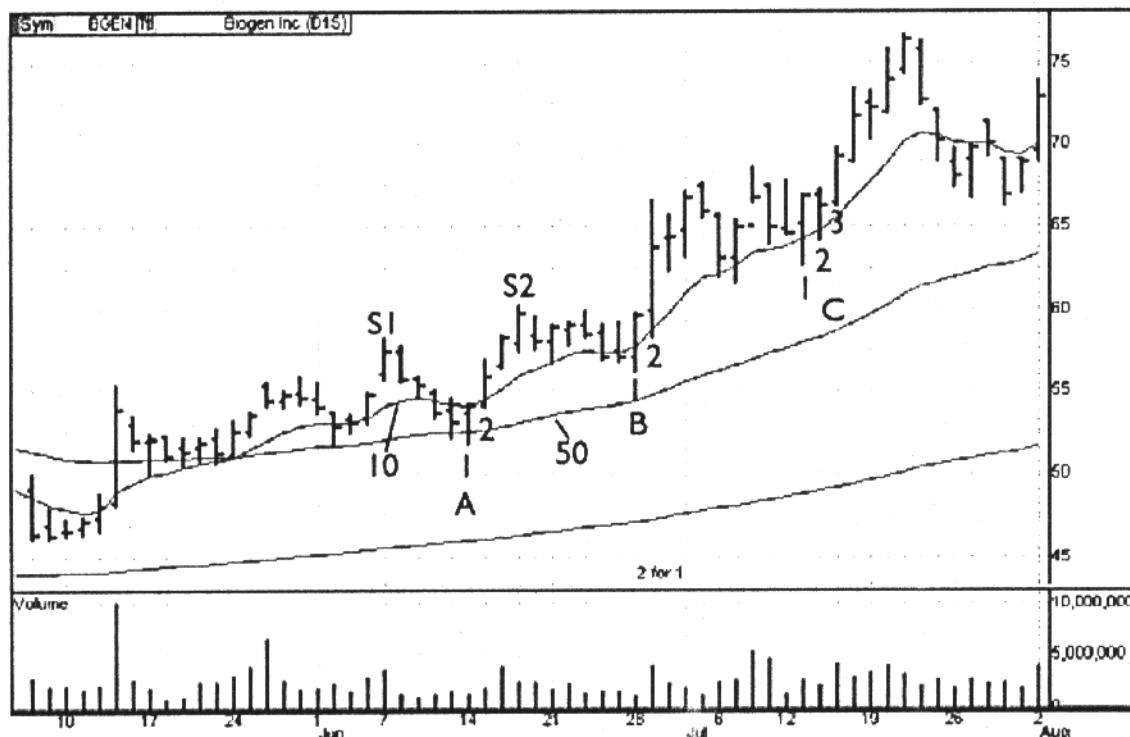
The hedge funds with married puts and the specialist if he were short and in position to run the obvious 148 inflection point and stops. Any option players that were set up to put pressure on AOL and benefit from a significant move below 150 could also help to accelerate the downmove.

Go back and read this example several times so you start to think of what you are seeing. It's not about memorizing a pattern. You could look at ten identical head and shoulders tops but each one tells a different story based on many of the things we have pointed out in the AOL example. When your skills improve you won't

even be thinking patterns anymore just direction and the balance of buying or selling pressure. After all, we only have to be right for several minutes.

Biogen Chart (BGEN)

I have included the Biogen (BGEN) chart as it includes three different buy situations. BGEN had made a 60.25 all-time high on 4/8/99, corrected down to 45.125 on 4/26/99 and was trading back up over its 10, 50, and 200 day EMA's. The pullback to the 20 and 50 day EMA's got my attention. They are oftentimes excellent entry points in up-trending stocks (sells reversed). Shorter pullbacks of 3, 5, 7 and 8 days often provide the strongest trades.



TRADE A

Day 1 - After a 5 bar (daily) pullback, BGEN re-crossed the 50 day EMA and closed at 54 1/16, at the top of its range and right at the 10 day EMA. The stock had made a swing point high of 58 1/8 (S1) on 1,787,000 shares and pulled back on average volume of less than 600,000 shares. The BTK (Biotech Index) had the same pattern as BGEN and with increasing RSI.

Trading plan entry point was 54 1/4 on Day 2 which was 1/16 above Day 1's high of 54 3/16.

Day 2 - BGEN opened at 54 1/8 and got good entry at 54 1/4 and stock traded to a high of 56 1/4.

TRADE B

After a 3 bar thrust move from our Day 2 trade BGEN hit 60 3/16, just under the 60 1/4 high, then consolidated for 7 days. (Sound like a familiar number?) All of either the opens or closes of the seven bars were within the range of the S2 swingpoint bar.

Day 1 - After two bottom range closes on average volume of approximately 740,000, BGEN gives us an excellent outside reversal day on 1,029,500 shares and closes 1/8 under the top of the range at 59 5/8. This told me that someone was anticipating a breakout to new highs above 60 1/4.

Trading plan entry point for day 2 was 59 7/8 or 1/8 over outside days high of 59 3/4.

Day 2 - This was a second entry after getting stopped out, but it proved successful as BGEN traded to a high of 66 1/2 on 3,914,500 shares. (More about reversal days in pattern chapter next week). Once again you saw that expansion in range on Day 1 with an increase in volume and close in the top of range. You had to sense that if we had a decent tape on Day 2 that the Generals would take it to new highs, but it wasn't an easy entry. The stock traded down to 58 3/8 before recrossing entry point. It happens often.

TRADE C

After the big WRB move up on Day 2, BGEN went sideways for 10 days. This is very normal after these kinds of thrusts.

Day 1 - BGEN closes in top of range on move that doubled the previous day's light volume.

Day 2 - Stock has a higher high, higher low, and closes in top 30 % of its range just below the day 1 close. This was enough action to plan entry the next day for possible run to new highs again. The momentum players love this kind of play.

Day 3 - BGEN opens at 66 3/8, ticks to 66 1/4, and then takes off. We enter at 67 1/4 which is 1/8 above Day 2 high. Stock trades to high of 69 11/16.

Now, I can draw some lines over the pattern, and we can make it a symmetrical triangle, trading range, or whatever other names you can think of, but who cares. You saw enough on Days 1, 2 and 3 that told you to get on the same jet as the Generals.

BGEN Volume Table

Date	Open	High	Low	Close	Volume	
15-Jul-99	66.375	69.6875	66.25	69.1875	4,036,500	Day 3
14-Jul-99	66.9375	67.125	64.25	66.1875	2,022,600	Day 2
13-Jul-99	65.125	66.8125	62.8125	66.75	2,432,100	Day 1 Trade C
12-Jul-99	65.5	65.875	64.5	64.5625	1,114,900	
9-Jul-99	67.375	67.375	64	64.875	4,406,100	
8-Jul-99	67	66.5	66.5	66.6875	5,207,100	
7-Jul-99	62.8125	65.25	61.625	64.9375	2,475,300	
6-Jul-99	65.5625	65.625	62.0625	63.0625	2,322,600	
2-Jul-99	67.375	67.5	65.5	65.8125	1,202,300	
1-Jul-99	64.6875	67	63.25	66.6875	1,796,800	
30-Jun-99	64.25	65.5625	62.375	64.3125	2,154,400	
29-Jun-99	59.875	66.5	58.375	63.6875	3,914,500	Day 2
28-Jun-99	57.1875	59.75	56.1875	59.625	1,029,500	Day 1 Trade B

Trade Entries

The information flow network is always in motion. The other part of the network is the brokerage firm analyst contact with the money manager. Some accounts are on page one and might get some early pertinent research information about earnings, products, etc. which could influence their trading decision on any given day.

Once you select your entry point from the daily chart you must make a decision based on intra day market dynamics whether or not to enter the trade.

The different entries you will be using are as follows:

1. Stock trades through your entry price.
2. Gap open (sell reversed) and pulls back to entry price.

3. Second entry. This is when you enter a trade, get stopped out and enter again if the stock trades back through your entry price. The market and stock dynamics must look good to take the trade. Remember, you don't necessarily have to get stopped out to scratch a trade. The dynamics are changing all day based on this information flow. If the market doesn't prove your trade correct in a reasonable time frame or in the case of buys, if you see selling pressure get the upper hand get out of your position. You can always re-enter if the dynamics change.

We are always looking to enter the stock where we can identify the aggressive buyers or sellers. Not all stocks exhibit this, but when the institutions are aggressive and they have competition on the same side of the trade the identification process is much easier. A neutral stock is a dead stock until trading decisions are made to change the supply demand equation.

First, I will show you a simple table that I use to monitor the market dynamics. Second, I will cover some of the telltale indications of strong stock dynamics. We will finish up with how specialists and market makers interact with the stocks.

Market Dynamics

This is a table to use so you can monitor changing market dynamics during the day. I keep this every 15 to 30 minutes depending on activity in market. A top to bottom explanation of headings is as follows:

SPU : Near term S&P 500 future which is now the September contract.

SPX : S&P cash index.

TICK : Net difference of all NYSE stocks trading on plus or minus ticks. I always keep a S&P 500 futures intra day tick by tech chart with the NYSE tick chart right below it. If you see the futures making lower lows and the NYSE ticks showing positive divergence and making higher lows (sells reversed), look for entry in stocks showing positive relative intra day strength.

PREM : This is the difference between the S&P Future that you are monitoring and the S&P Cash Index. I use Track Data Fast Trac and can set the spread on my screen. If you don't have that on your system you can just eyeball the two and subtract.

A-D : This is the net difference between the advancing and declining stocks on the NYSE.

UVOL : Up volume of stocks on NYSE.

DVOL : Down volume on the NYSE.

DOW : Dow Jones 30 stocks. Net change.

NDX : NASDAQ 100 stocks. Net change.

BD : 30 year treasury bond. Net change.

SOX : Semiconductor stock Index.

MSH : Morgan Stanley High Tech Index.

DRG : Drug Index

RLX : Retail Index

BKX : Banking Index

XOI : Energy Index

USX : Oil Service Index

RUT : Russell 2000 Small Cap Index

These are the major sector indexes and you can add indexes at the bottom if they are active such as FPP, XBD etc.

Market Table

This is actual market data for 8/19/99 9:45AM to 11:00AM EST. This is the table that monitors overall market dynamics.

	9:45	10:00	10:20	10:30	10:45	11:00
SP'U	-10	-10	-10	-8	-14	-14
SPX	-11	-12	-12	-10	-16	-16
TICK	-482	-474	-528	-172	-181	-470
PREM	3.85	3.80	3.85	3.70	3.75	3.60
A-D	-1032	-1014	-958	-908	-1035	-1098
UVOL	13	26	44	48	51	58
DVOL	41	61	93	99	126	149
DOW	-91	-84	-79	-71	-105	-97
NDX	-21	-27	-33	-28	-45	-44
BD	-9	-5	-9	-8	-5	-6
SOX	-	-	-	-	-	-
MSH	-	-	-	-	-	-
DRG	-	-	-	-	-	-
RLX	-	-	-	-	-	-
BKX	-	-	-	-	-	-
XOI	-	-	-	-	-	-
OSX	+	+	+	+	+	+
RUT	-	-	-	-	-	-

This table takes less than 45 seconds to complete. You round off numbers for the S&P Futures, all the averages and the volume figures. You use exact numbers for TICK, PREM, A-D, and BD. For the sectors, they are either plus or minus (green or red on your screen).

At the bottom of the sheet I make notes on which stocks are showing strong or weak intra day relative strength and look for set ups on the 5 minute charts.

You should also make note of any key market news that should generate a reaction and observe how the market reacts to the news.

Start to use this table on a daily basis, and you will start to see the relationships develop. Is it just program selling seeing that the sectors are all pretty and the breadth is still good, or are the Generals in there selling because up volume / down volume ratio keeps getting worse with all sectors turning minus?

There are many market clues that you will only start to understand if you keep the table. After a period of time your market feel will improve ten-fold, and this will improve your entry into good trades. You will observe that trending days will all have similar traits as do the over reaction days that also provide good opportunity. The neutral days tell you little by flat averages, but maybe breadth, volume or certain sectors will provide pertinent information.

Note - I use 26 boxes for table so you can record market every 15 minutes if needed.

Stock Dynamics

Once you have located your stocks to trade either from the daily chart or from the 5 minute bar intra day chart, you are watching how those stocks are trading. Remember, we want to enter trades with the Generals on our side. It is not always so clear cut because there is so much noise on an intra day basis. You can enter a trade, get lucky, and have a big buy program kick in along with institutional buying and you feel smart in addition to making a profit. The problem is that it works the other way just as often.

Option market makers are constantly buying or selling stock to hedge position risk, and programs go both ways. The specialist might have an axe to grind. Upstairs position traders might be working down a long or short position, and portfolio managers are making daily trading decisions at different levels. There is no crystal ball, so as day traders you must go with the flow. This means you can make all the correct decisions for entry into a trade but might not get proven correct because of the constant intra day noise that stops you out once or even twice your stock trends. When that happens, most day traders don't re-enter the trade and miss the major move that day.

Stocks will still react to the major supply/demand pressure with minor interruptions by programs or some of the various noise mentioned above. We want to recognize which side is stronger before we enter the trade. Since we are in a bull market, we will assume we are buying stock. There are very simple and easy to see dynamics, but you must adhere to them with discipline in order to be successful.

- 1.- Did the stock open up on the day?
- 2.- Is it trading above the open?
- 3.- Is it trading above the VWAP? This is the volume weighted average price on the day.

Several quote vendors such as Track Data, Bridge, and Bloomberg have this information. These are the only vendors I have used, so I am not aware of who else provides this information.

When the buying pressure is neutral, or maybe there is one good-sized institutional buyer that has no real competition, then the buyer will try to scale down the order. If the market is soft and the buyer is getting enough stock, then we won't notice the buyer. If the market firms up or another buyer or two show up, we would probably see some buying pressure build. No institution will pay up for stock unless they are able to get volume, but they must participate if volume starts to trade.

When the stock is trading above the VWAP it means the buying pressure is stronger, buyers are competing for stock, the market is probably, option market makers are probably buying stock to hedge short calls, and if the specialist is on the right side of inventory it means an stock. When all these ingredients are put together and the stock is at a key inflection point on the daily or intra day chart, then day traders have a good shot to make money.

- 4.- Is the volume trading on the bid side, or is it trading at the midpoint or offered side?

We are buyers today in the stock, so we want to see it trading on the offered side (ask) or at least the midpoint. This tells us the buyers are aggressive, and it is a sellers market. All of you who have direct access software have time and sales tickers that are dynamic and that you can load with stocks you are monitoring. This is an absolute necessity if you are entering off intra day patterns or retracements.

- 5.- Where is the volume trading? Bid, midpoint or ASK?

Bridge and Bloomberg also provide this information. Two stocks could close in the top of the range, but one might be due to late program trades, and the other because 75% of the volume was on the ASK side where there were multiple buyers.

- 6.- Watch where the blocks are trading. (5000 shares or more) This will precede range expansion.
- 7.- Where is size reflected? Bid or Ask? In OTC stocks you won't see this near as often as on the NYSE.
- 8.- Is the Bid and Ask moving higher?
- 9.- Are the other stocks in the group behaving in a similar fashion? It is always better to buy strong stocks in a strong group.

Note: Your best trades will come from trending stocks above the open for buys (sells reversed) either on continuation or pullback entry. Often times programs are very helpful on pull back buys or shorts as they give you entry at good levels, but you must be fast to execute. Also, you will get some great opportunities when stocks reach certain standard deviations based on the implied volatility of the stock for one day. We will explain this opportunity next week.

NYSE Specialists

Specialists interact all day long with the order flow. If you are not talking directly to the floor you have no way of knowing when the specialist is involved. They are very regulated in how they can interface with the order flow unlike the large OTC market makers that can still sell short on minus ticks. If you are a wholesaler you get to talk to the buy side, the sell side and you see order flow from many retail firms because they pay for it.

The NYSE specialists are down there to make orderly markets, but you must also understand they make money primarily by trading. Commission billing revenue for specialists is not what it used to be so there is a much greater emphasis on trading. The day trader's shot of utilizing knowledge about specialists is primarily on openings and the subsequent trading after the open. That is enough to give you a profitable day anytime we get those "tail-wag-the-dog" openings due to the S&P futures. Another good opportunity is happy program time when the specialists step aside and let the robots do their thing.

If you asked me the one thing about specialists that you should be aware of and can capitalize on, it would be: "Specialists will take the stock to the volume, and where it wants to trade. They will get it there by buying or selling only the required amount of stock that complies with market making duties."

Concluding Remarks

After reading this chapter you should understand that despite not being included in that vast institutional information network, you can compete at a high level by recognizing the various dynamics that point to high probability trades.

Practice with the market table, and get a good feel of how the market dynamics are constantly changing intra day. Pick several stocks that are close to what you think are good inflection points and watch them all day. Relate their action to your market table and notice how they react trading near or through these inflection points.

Put the time in, and your efforts will take you to a different level or at worst get you started on the right level and in the right direction.

Next week is pattern week, and there will be some highly effective intra day and daily patterns that are easy to identify. With your better market feel, you should be able to contribute to the profit side of the Trader's Equation.

Have a great week.

Kevin Haggerty

TRADINGMARKETS.COM Members, Welcome to Week Four

This week we want to focus entirely on patterns and some of the key interpretation of bar charts. It is essential that you try to keep it simple, believe what you see, and act on it. Many traders spend thousands of dollars looking for complicated formulas because when they observe something that appears so obvious, they are not capable of believing it.

Remember, as a trader you can't impose your will on the market because then you are attempting to trade what should be instead of what is. If you are that good or think that you have some optionized system that will work at all times, then this chapter isn't for you. On the other hand, if you can observe the tape action for what it actually is, ignore what you read or hear, and then enter a trade based on what that action is telling you, you will be on the path to being a better trader.

Week 3 Review

During week 3 we demonstrated some of the key price, volume, range and time relationships that if followed with only average ability will place you in trades that have high predictive probability.

Volume precedes price – is stock advancing on increased volume or declining on light volume. (sells reversed)

Range Expansion – WRB's on increasing volume with close in top or bottom of range tells us about the supply/demand situation of the stock. Are the buyers reaching for stock or are the sellers having to give up price to get out?

Price & Time – Where is a stock closing relative to previous days. Trading above or below previous 5 days is more significant than one day. Closing above or below the same 5 days is most significant.

Range Contraction – If after a move up you see a narrowing of range and increased volume it could mean the sellers have arrived and the buying/selling pressure equation has shifted. It is the reverse on the downside if you see narrowing range and increase in volume.

Remember; always look to see if you are at any key inflection points which would help confirm your observation. Are their rising lows prior to key buy inflection points? (Sells reversed) Is stock closing above or below the midpoint of its daily range? More importantly is the stock closing in the top or bottom of its range?

Spotting Momentum Changes

When you are day trading you are working primarily with daily and intra day charts. You are selecting uptrending stocks to buy and downtrending stocks for short sales. There will be times when you enter stocks just as momentum changes as in the AOL example. Regardless of the time frame, you are looking for the same clues that the Generals are active and which pressure is greater – the buying or selling?

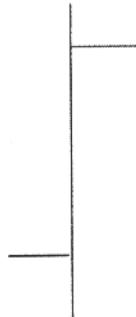
Before we start talking through the charts, I thought it would be beneficial to review some basic bar relationships that you must see clearly and let frame your thought process so you free your inner self to trade what is.

Bar Pattern Review

The strongest sign that a stock wants to get some where in a hurry is when you observe the following relationships.

Bar Pattern (BP 1) - SELLS REVERSED

TD



PD

- Higher high than prior day (PD) high
- Opens above PD high
- Closes up on the day, above PD high and above today's open
- Today's low higher than PD high

This relationship is the strongest indication that the direction will continue. If you also get expanded range and increased volume it is even stronger.

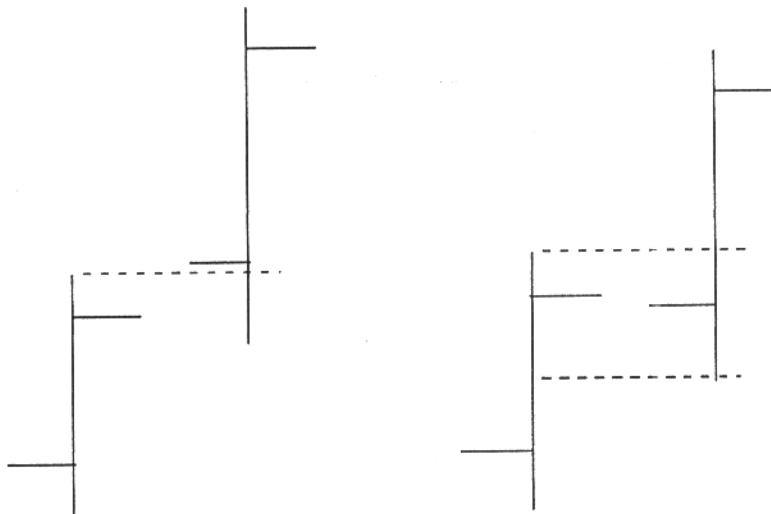
When you see this bar relationship your logical progression of thought is to relate it to previous bars. Remember that it doesn't matter which time frame you are tracking in, the relationships have the same significance.

How many previous closes and highs did today's close expand? Did today's bar and close take stock above a swing point trendline, out of a consolidation, above a significant moving average or did it attract buying/selling at a key geometric retracement level such as .38, .50, .618, or .786. Those are fibonacci levels and institutions are very much aware of them for stocks, so you should understand their usage. You look for reactions at the various retracement levels you don't trade the levels blindly just because they hit a number.

Bar Patterns 2,3

Bar Pattern 2 (BP2)

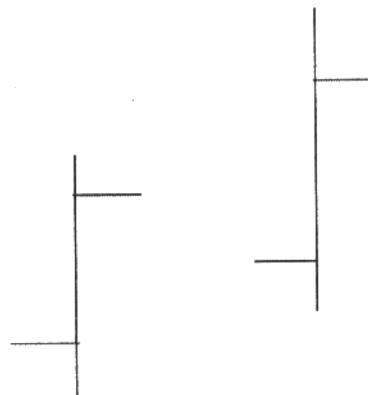
Bar Pattern 3 (BP3)



BP 2 is the same as BP 1 except that today's low is the same as prior days high. BP 3 is only different than BP 1 and BP 2 in that today's range is slightly within prior day's range.

All three relationships tell a strong story. Simple – yes. Important – you bet, especially when deciding which one of your trade selections to choose from.

Bar Pattern 4



BP 4 is your normal higher high and higher low continuation in direction

If you were to see a higher high and higher low except that today's close was below prior days close it would be neutral and you would wait for the next bar to confirm direction. If today's close was below the open even with the higher low it might indicate a failure move or possible change in direction. What will the next bar say? We will discuss reversal bars and outside days with some of the patterns.

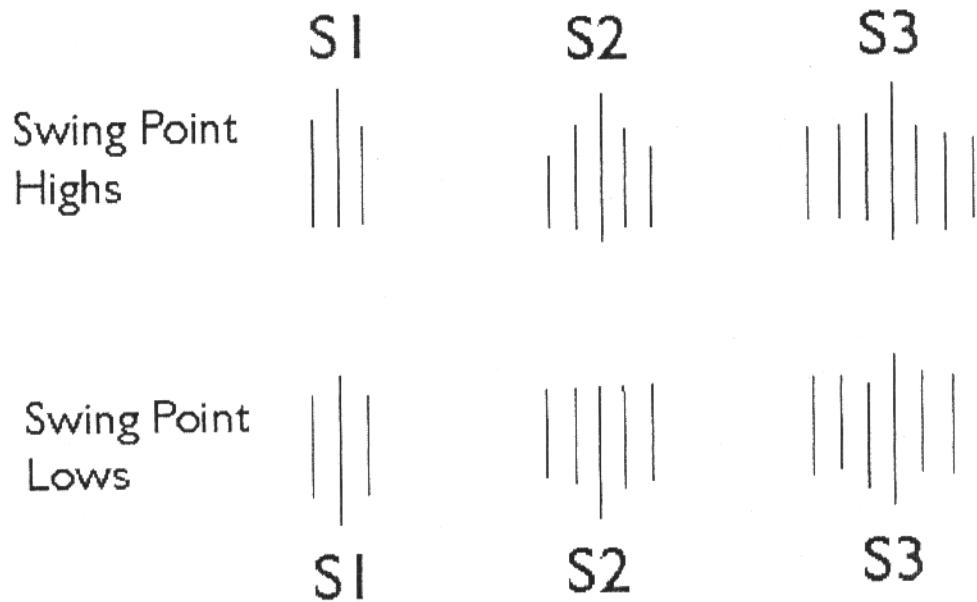
Another important aspect of looking at these relationships is to compare your stocks related to stocks in the group and to any sector index that is pertinent in addition to the S&P 500 if in fact that is the correct bogey that your stock tracks.

Swing Points

You hear me often refer to swing points or confirmation of a swing high or low so a quick review of swing points might be helpful, as they are key inflection points. Stocks don't go straight up or down they generally

make higher highs and lows in an uptrend (Sells reversed). The high will have a lower high on each side of it and the low swing point will have a higher low on each side. If the swing point has only one on each side it is S1, two S2 and three is S3.

EXAMPLE



As you can see a S3 would have more significance than S1.

Nextlink Communications (NXLK)

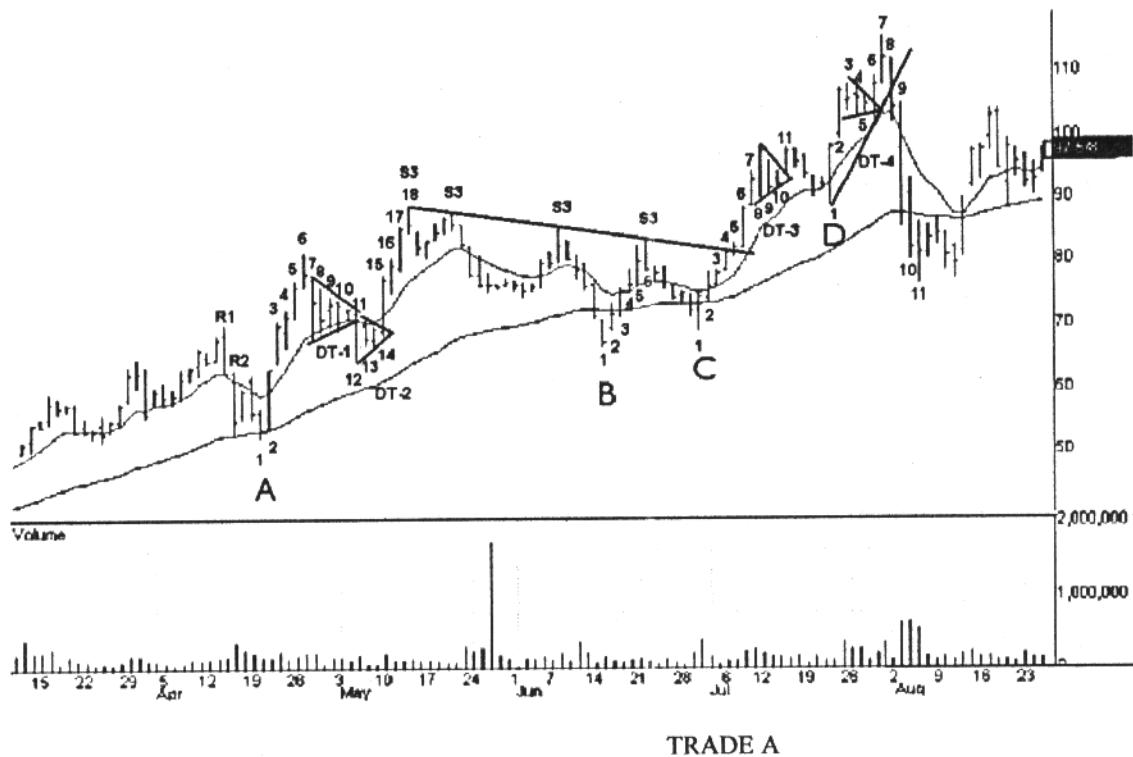
Primary trade entries selected from the daily charts consist mostly of the following:

1. Wide range bar expansion (WRB).
2. Pullback entries in the direction of trend.
3. Consolidation patterns such as dynamite triangles, flags, trading ranges etc...

Note: The name of the consolidation patterns and definitions can be found in any textbook on the subject. What you must concentrate on is to recognize when a stock is moving or is about to move to new levels. I will name the patterns as we walk through the examples.

The following chart of NEXTLINK Communications A (NXLK) illustrates some WRB expansions, which demonstrate BP patterns 1 – 4. It also shows you some dynamite triangles and flags which often form the consolidating phase after a sharp WRB move. There are also several pullback and go patterns at the 50-DAY EMA.

The following chart of NEXTLINK Communications A (NXLK) illustrates some WRB expansions, which demonstrate BP patterns 1 – 4. It also shows you some dynamite triangles and flags which often form the consolidating phase after a sharp WRB move. There are also several pullbacks and go patterns at the 50-DAY EMA.



TRADE A

4/20 - DAY 1

NXLK pulled back 5 bars to the 50-DAY EMA. Most of your PB trades in strongly trending stocks seem to be 3, 5, 7.8, or 13 day PB's. After that, momentum is not quite the same until stock bases a bit. You count bars by starting with actual low (High) or by the preceding bar if a low, or the next bar if a high. In this example we started with the actual low bar on Day 1. It is an either/or count. NXLK closes in bottom of the range at 53 1/4 right on the 50 EMA. The 5 bar PB was from a new high of 70 to low of 52 on Day 1.

4/21 - DAY 2

WRB up to close at 63 confirming Day 1 as a swing point (S3) low. Checking the volume chart you see that R1 is a big WRB outside reversal day on increased volume. This sets up a counter trend short trade for R2, which is a big down day on 1,000,200 shares. Notice how Day 1 low (S3) was on declining volume. No unusual volume on this WRB move up.

DAY 3

Is a bar pattern BP1 strong gap move up, no entry unless you were able to trade intra day pattern from the 5-min chart.

DAY 4,5,6

All gave good entry above the previous days high before Day 7, which was a reversal day. Three good day trades.

DAY 7

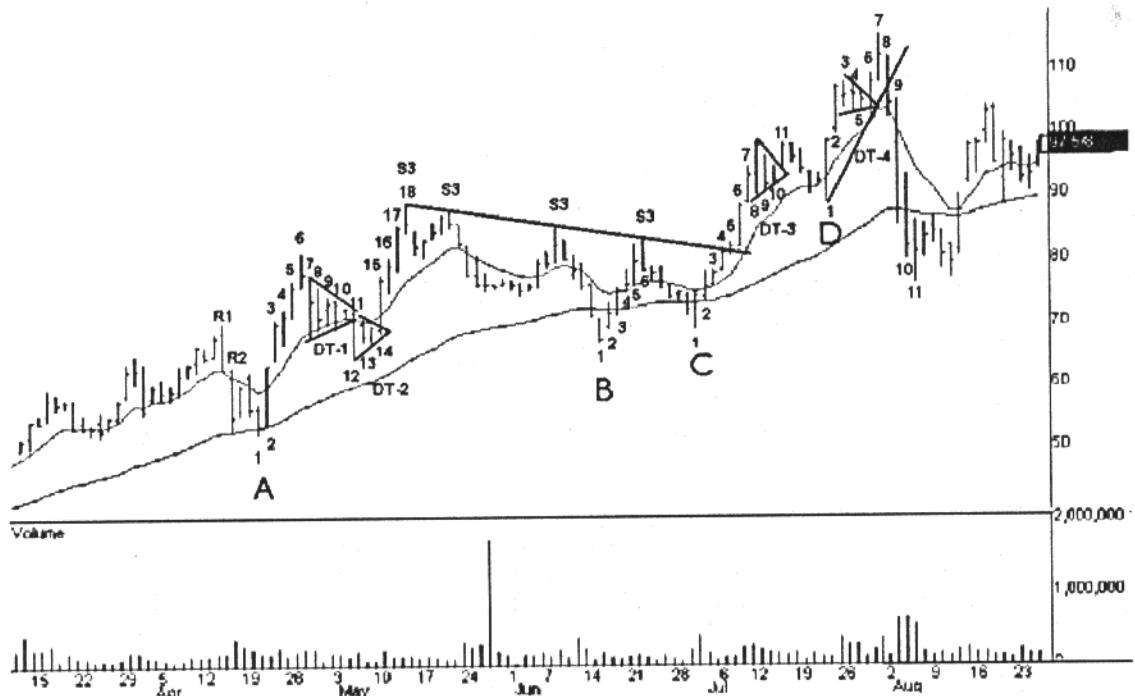
Is a WRB down which then consolidates to a dynamite triangle which is usually a minimum of 2 inside days as volatility and volume diminish. The move out of the triangle is usually a good trade as you see on the day 12 bar which is a WRB to downside. It doesn't have to be a perfect shape but will have mostly lower highs and higher lows as it narrows.

Day 12

WRB is a 7 bar low and then you got two inside Days 13 and 14 forming another dynamite triangle with an explosive upside breakout from 69 7/8 to 77 3/4 on Day 15 with good volume. Days 16 and 17 gave you two more great day trades with multi-point moves.

NXLK ran from a Day 1 low of 52 to a Day 6 high of 81 1/4 with only a 5 BAR move. That is traders' volatility. The Day 6 high of 81 1/4 sold down to 64 on a 7 bar move which retraced 59% of the prior swing before the dynamite triangle breakout took NXLK to another new high at Day 18 of 88 3/4. The power of a high RS value and strong ADX coupled with volatility is the formula.

TRADE B



TRADE B

NXLK trended down to the 50-DAY EMA from Day 18 hitting a low of 66 3/4 on 6/15 closing at

67.

DAY 1 5 bar PB from S3 high of 85 to close below 50-DAY EMA at 67

DAY 2 is a BP4 day closing right at 50 EMA confirming Day 1 as a swing point low

DAY 3 Good entry 1/8 above Day 2 high

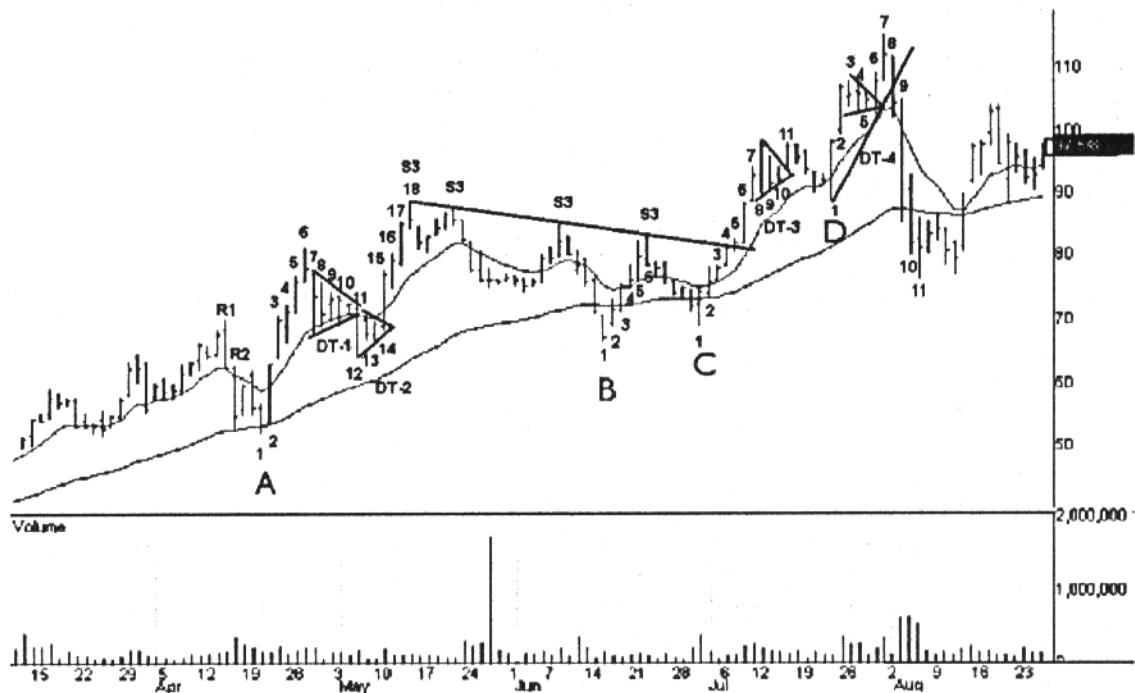
DAY 4 Good entry 1/8 above Day 3 high

DAY 5 Good entry 1/8 above Day 4 high

DAY 6 Good entry, but stopped out, no profit

The trades on days 3, 4 and 5 were multi-point trades. Day's 2 through 5 were all BP4 or BP3. Day 6 was a reversal day and also a 5 BAR swing point top at 82 7/16. This Day 6 top then traded 7 bars down to the 50-DAY EMA once again. This is the 4th PB to the 50 EMA.

TRADE C



TRADE C

DAY 1 Outside reversal day and a re-crossing and close above the 50 EMA after a 7 bar pull back from previous S3 high of 82 7/16. This was another higher low of 69. This was a strong reversal on 1,098,000 shares setting up the trade for Day 2.

DAY 2 Good entry at 75 which is 1/8 above the Day 1 high stock trades up to 78 1/4 high

DAY 3 No entry, narrow range.

DAY 4 Good entry 1/8 above Day 3 high.

DAY 5 No entry, narrow range.

DAY 6 Good entry 1/8 above Day 4 high on a BP3 move. Explosive 6 point move

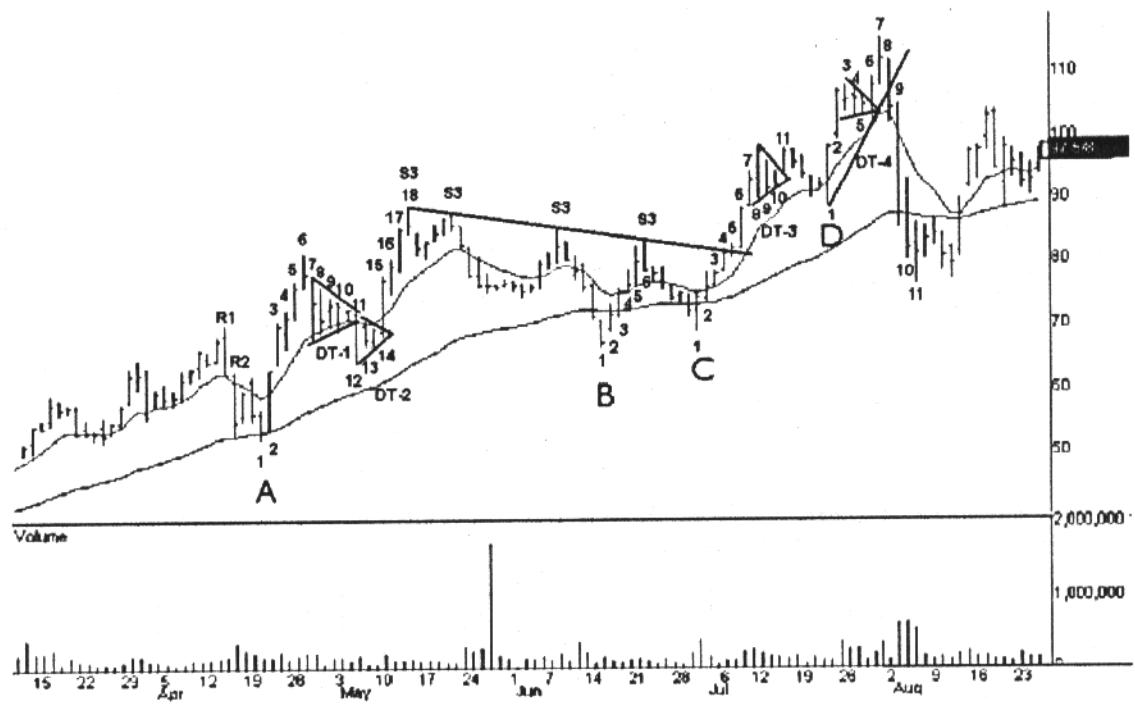
DAY 7 BP2 bar pattern with explosive continuation move.

DAY 8 Good entry, multi-point move on WRB expansion which is biggest thrust of this move up from the 50-DAY EMA. This WRB move was followed by Days 9 and 10, two inside days, which formed, YES you are correct, a dynamite triangle.

DAY 11 Break out from DT in direction of trend on a BP2 move. Good entry and almost a 4 point advance from entry. This is a S2 swing top.

Note: Day 6 was a S3 swing point trendline breakout on strong volume of 687,300 shares followed by another WRB of 738,700 shares. The Day 8 WRB was on only 592,000 shares then came the two inside days.

TRADE D



TRADE D Starts with Day 1

DAY 1 5 BAR move down from Day 11 – S2 top. This is a huge reversal of the 5 bar downside move from the Day 11 high on light volume. It was due to an upside earnings surprise. It closed at 98 3/4 versus Day 11 high of 98 3/16.

DAY 2 the Generals came for stock again on a BP1 pattern. The low was 3/4 of a point above Day 1 high. There was no inflection point entry unless you entered off a 5-min chart pattern. Volume was big at 1,026,400 shares.

After this second WRB move up NXLK consolidated for three Days 3,4 and 5 in another dynamite triangle or some would call it a FLAG. Who cares what the name is, we are ready to enter above high of second inside Day 5.

DAY 6 Good entry above inside Day 5 high as it trades and closes at a new high of 108.

DAY 7 Good entry 1/8 above Day 6 high makes another new all time high of 115 3/8 but on only 477,800 shares. Give me a break, the stock is up 7 3/8 points from Day 6 close of 108. Great end of the month move isn't it? You are aware Day 7 is July 30. These are the moves all traders dream about.

DAY 8 August 2nd, first day of the new month. What a surprise. NXLK opens at 112 - trades down to a low of 102 1/8, before closing in bottom of range at 104 7/16. This big move down on only 357,100 shares. No more mark up buyers, but this WRB expansion move to the downside in price shook the tree.

DAY 9 Panic City, stock opens at 104 7/8 and trades down to 85 3/8 on 1,894,600 shares than closes at 87 7/8. Home Run. The Generals couldn't get to the exits fast enough and no market makers in sight. This was a pull back entry and break back below Day 8 low.

DAY 10 opens at 90 7/8 trades below entry point of 85 1/4 the prior day's low and a key inflection point. It trades down to low of 80 and closes at 82 on volume of 2,036,000 shares, which means more panic. Closes below 50 EMA.

Note: Day 8 had broken an S3 swing point trendline from Day 1 to the S3 point on Day 6. If you were in this stock, short entry on the downside crossing of this trendline was profitable.

DAY 11 Good entry below Day 10 low of 80 and NXLK trades to a low of 76 3/8 on more big volume by the Generals of 1,658,500 shares.

Note: After Day 11 volume dried up as the sellers backed away. The stock consolidated before starting a weak up move relative to volume.

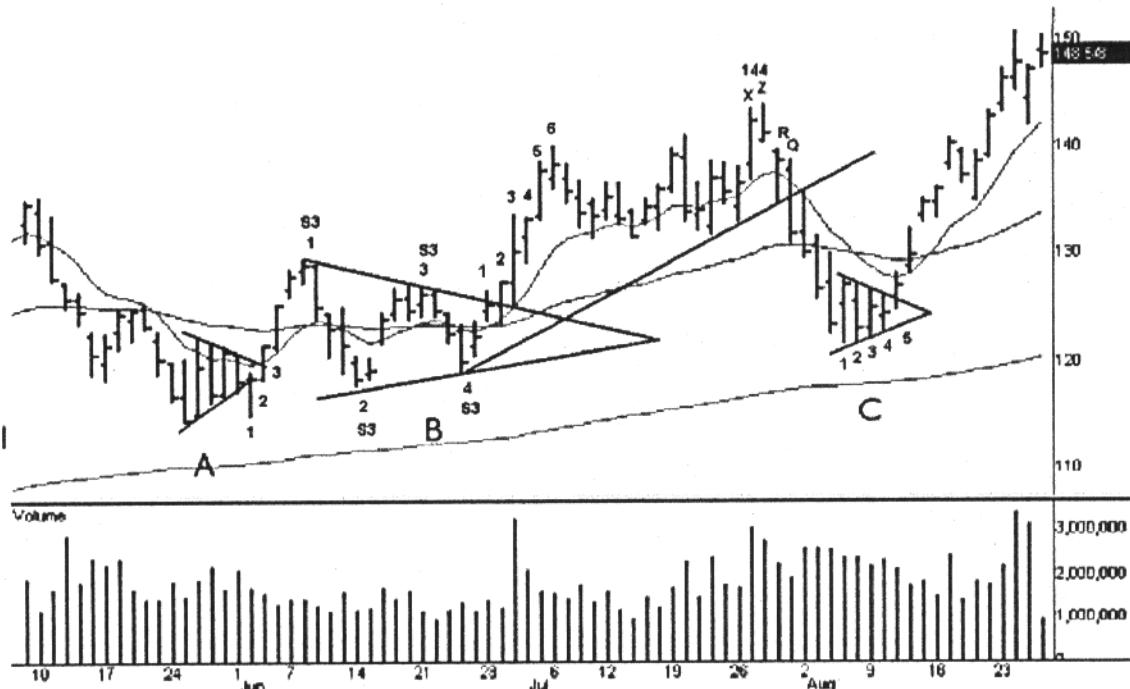
REVIEW NXLK

WRB's, BP's 1 – 4, dynamite triangles or flags, pullbacks to the 50-DAY EMA, Outside Reversal Days on good volume and momentum crack and panic on Wide range reversal bars.

Also, you saw the action at the swing point trendline breaks. Any combination of S2 or S3 points will form your trendline. The strongpoint is the S3 to S3 TL as in trades B and C. You draw the trendline (TL) from right to left as that is the most current data. That is why my S3 TL isn't straight as it would be if I drew it from Day 18.

I hope this example brings some life to your thought process and to what you see on the chart. You can take these examples down to the 5-min chart level.

American Express (AXP)



Trade A

This chart shows you in order a dynamite triangle (Trade A) that breaks to the downside at Day 1 but closes in top of its range indicating the failure of the move. Had you entered coming out of the triangle which is an entry below the low of closest inside bar you had a good day trade. Day 2 gave you good entry above the triangle line extended. Day 3 was good continuation entry and an excellent move. Entry was 121 3/4 and it ran to a high of 125 1/4.

Dynamite Triangle Entry Guidelines

1. Enter below the low or above the high of the closest inside day (it doesn't have to be a perfect inside day).
2. If the triangle trend line extended gives you earlier entry, take it if the dynamics are good.

Trade B

After the upside breakout from the dynamite triangle in Trade A, AXP ran to a high of 129 3/8 which was a S3 swing point high and consolidated forming a symmetrical triangle which is shown by points 1, 2, 3, and 4. They happen to be all S3 swing points.

Day 1 - AXP breaks above the swing point trend line and also out of the symmetrical triangle. If the stock and market dynamics are ok then you take the trade.

Day 2 - Good entry above Day 1 high, small profit, but stock closed in top of range. Volume not exciting yet. Your Day 3 trading plan calls for entry 1/8 above Day 2 high. This would also be a good entry for a position trade. Day 2 closed above its 10 and 50 day EMA. Both these averages are above the 200 EMA and are rising. Day 2 also closed above the ST and in top of range and above the last 13 closes and highs. The S&P 500 index was also up in a favorable pattern and you now have the perfect setup.

Day 3 - Home run. You get 127 5/8 entry and stock runs to a high of 133 5/8. S&P 500 also made strong up move so the dynamics were good. Volume was big at 3,215,900 shares.

Day 4 - Inside day, no entry, but stock closed on top of range ready for tomorrow.

Day 5 - Another gift BP2 day. Stocks at high of day 4 which is 133 1/4 and you get entry at 133 3/8 and stock trades to a high of 138 1/2. The low of the day is 133 1/4. BP1 and BP2 are strong indicators.

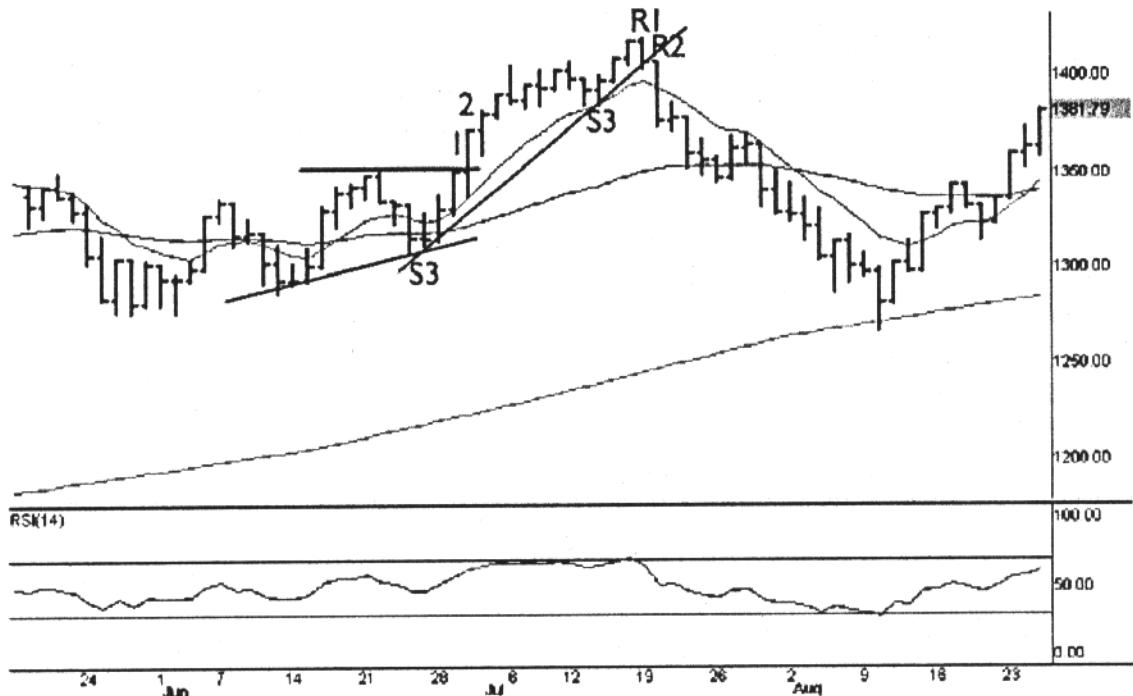
Day 6 - Good entry, 1 1/2 point run and end of this thrust out of the symmetrical triangle.

Trade C

AXP had rallied to a 144 high (2) which was a narrow range bar on strong volume of 2,727,800. This followed a WRB(x) to new highs on 3,000,000 shares. This contraction of range on strong volume is a sign that the supply/demand equation might be changing and a possible reversal in trend. The next four days provided continuation entries from the short side after breaking swing point trend line (see point 4 to Q bar).

AXP bottoms at 121 7/8 at day 1 which is a higher low than Trade B. Once again we get our dynamite consolidation and AXP breaks out for a good trade on Day 5. The rest is straight up to a new high of 150 5/8 on 8/24.

S&P 500 Chart



Day 1 Same situation as Trade B, day 2. AXP ready for continuation entry to further highs.

Day 2 Good breakout and the market dynamics were strong when AXP made its move.

R1 Outside Reversal Day

R2 Big reversal day that breaks a swing point S3 trendline and the decline is from the 1420.19 top.

Intra Day Patterns

Intra Day Patterns

It is easier and more effective to day trade if you limit your self to a few simple but easily recognized patterns. All of your entries will be determined by your interpretation of the market and stock dynamics at the time you are deciding to enter your trade.

1. Opening Reversal (OR)

This is a trade you will usually get in the first 30 minutes of trading. The trade sets up after an emotional opening due to early morning S&P futures activity or some news announcement that creates the usual overreaction.

Trade Set up (Buys, Sells are reversed)

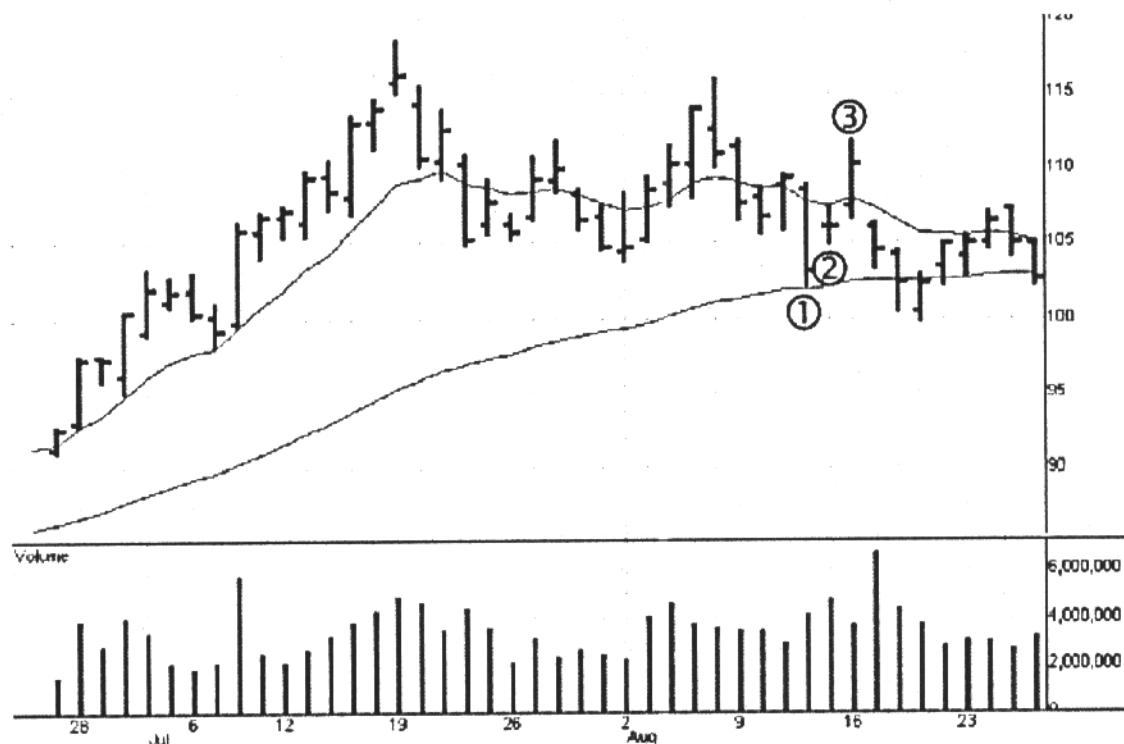
1. Stock opens and sells off no more than 25% of its daily range. (maximum is 33%)
2. The stock makes a quick reversal in price and trades back through the open.
3. Entry is 1/8 above opening price.

OR's will be selected from your list of high RS value stocks and from your Trading Plan stocks for the day. If you see a stock(s) that is demonstrating strong relative strength as the market opens lower, and this stock is only slightly below its opening price, then this will usually be your best selection, especially if it is a high RS value stock.

Because of the early trading noise, (9:30 – 10:00 AM EST) you must keep tight stops. This trade must be accompanied by improving market dynamics, (going up) and the stock dynamics which you have been observing must be good.

Also, be ready for a second entry if stopped out and if the dynamics are still solid. If the futures are on a search and destroy mission, i.e. taking out both the early low and early high before the first trend of the day, you will often get second entries.

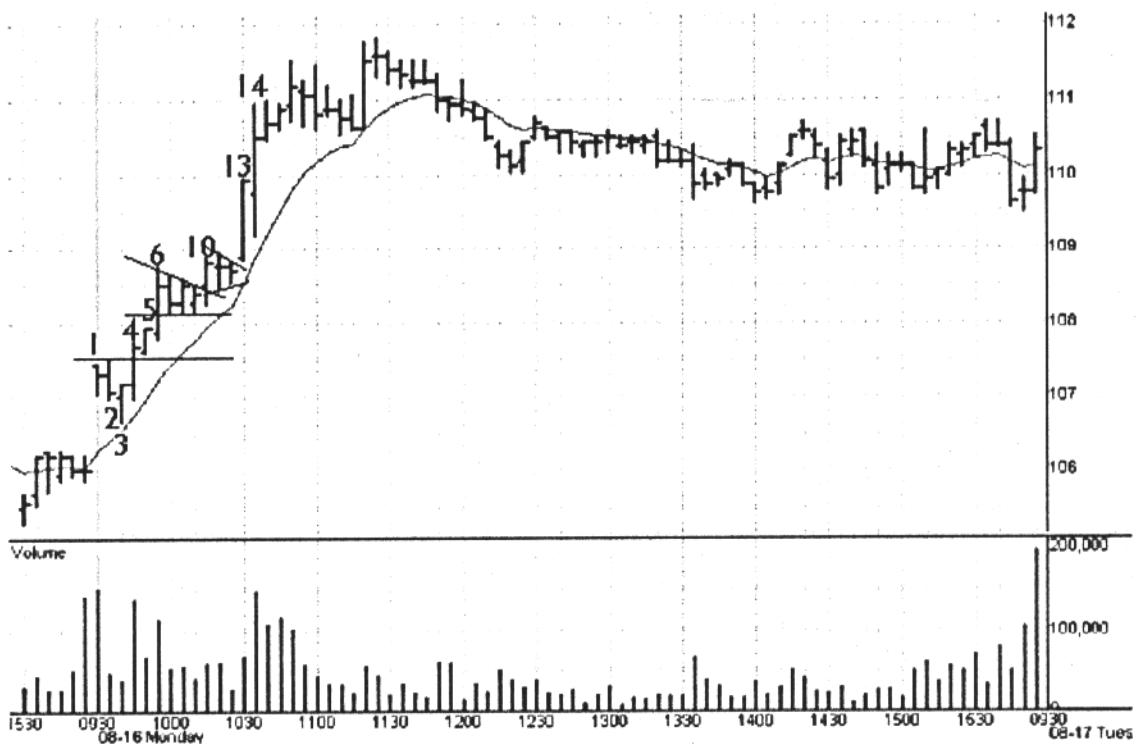
HWP



Day 1 - HWP trades down to and closes just above its 50-day EMA. The stock is down 6 5/16 on the day. The S&P 500 cash index is only down 3 3/4 points. The company is expected to announce earnings after the close on 8/16.

Day 2 - HWP rallies and closes up 2 15/16 (2.8%) and the S&P 500 finishes up 2.3% on a good market day. I circled HWP as a possible trade on Day 3 because the company was supposed to make the whisper earnings number. If you get trade entry 1/8 above the Day 2 high get on it because the momentum traders will probably front run the earnings.





I mentioned HWP on the call this morning. Take it if they come for it to front run the earnings.

The stock gapped open 1 7/16 points to 107 7/16 from the prior close of 106 (BAR 1). It traded down to 106 11/16 (BAR 3) showing strong relative strength, as it didn't come close to filling the opening gap. The stock quickly reversed on volume and traded back above the opening price. It traded to 108 1/2 on a WRB (BAR 6), consolidated to a FLAG and broke out again at BAR 10, moving straight to 111 1/2 before fading.

The discipline of the pattern and the dynamics put you in the trade. We got lucky that the momentum front runners took it so high. They got their lunch handed to them the next day as HWP closed down 5 3/4 points.

Opening Reversal Recap

It is important to note that this HWP example is a stock that gapped up, traded down, remaining above prior close and reversed opening to the upside. Most of your OR's will be stocks that open below or trade below the prior close then reverse opening to the upside (sells reversed).

Slim Jims

This is a tight consolidation pattern that will have you buying or selling new intra day highs or lows. It will also have you entering a reversal trade of the day's extreme move (See BBY Chart below) or a continuation entry from a consolidation above or below the days high or low. (see SPY Chart)

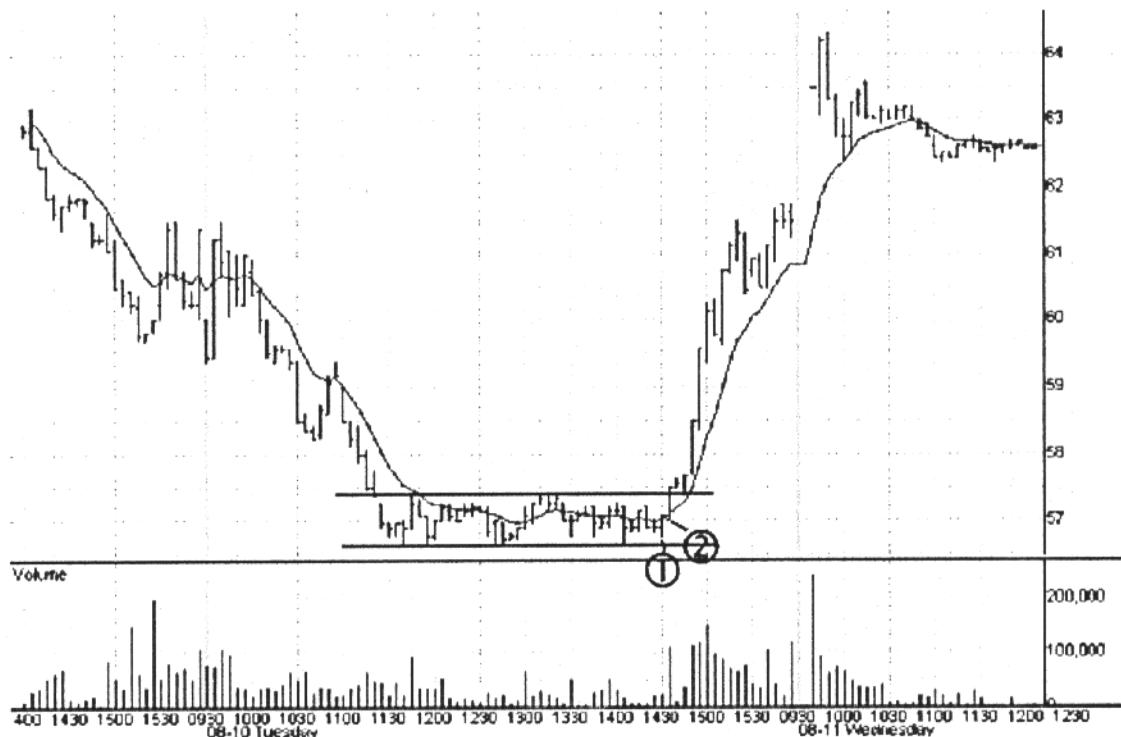
The longer and tighter the consolidation, the more powerful the breakout. If you see these consolidations in the first hour of trading they won't be as long, but if it's a narrow range and are rising lows (sells reversed) as it bumps up against a price, be ready for a good first move to new highs or lows.

If you can interpret the stock dynamics that we have outlined, (week 3) as you watch the dynamic time and sales ticker in addition to getting a decent feel for the market dynamics prior to entering your trade then Slim Jim is your main man. This pattern will take you there.

The first thing you must do is load up your charts with as many of your high RS value stocks with strong ADX and +DMI > -DMI (reverse if you are just looking for shorts). After the first 3 or 4 5-minute bars start

flipping through your charts to see what is setting up. This process takes place all day long. There is never a day that you don't have probable trade candidates.

BBY

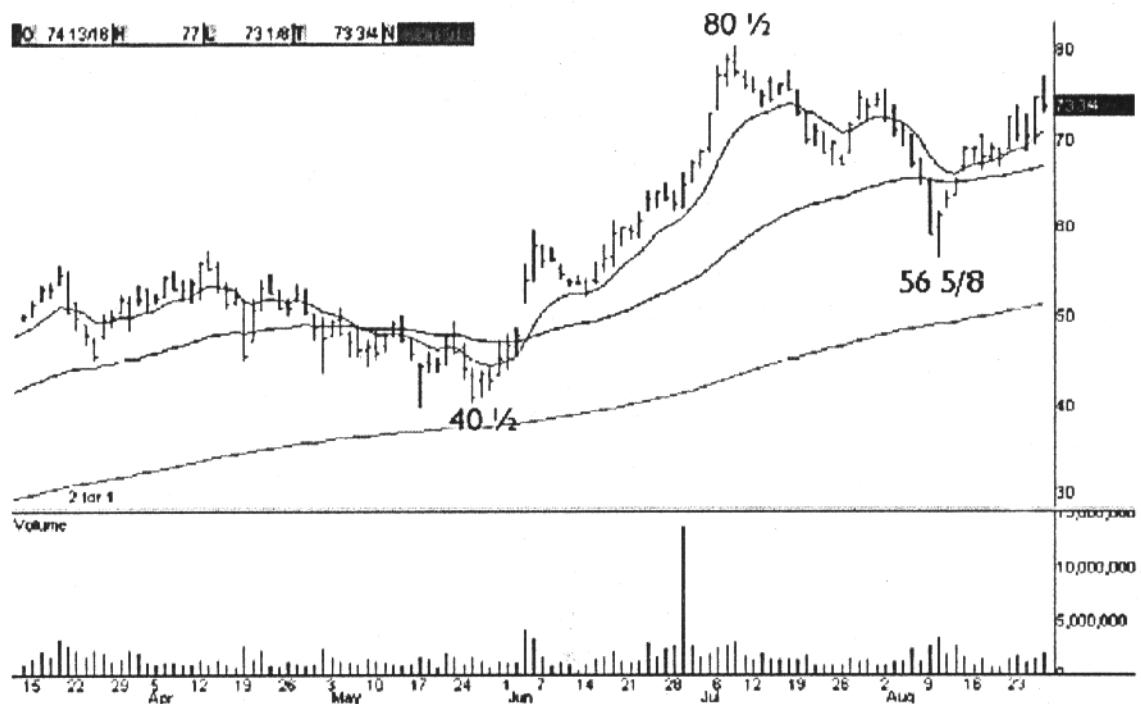


BBY opened at 60, made a high of 61 3/4, and then traded down to 56 5/8. It then entered a long, tight consolidation between 56 5/8 and 57 3/8. It was a 37 bar range from 11:30 AM to 2:30 PM. The market started acting really good as the S&P futures started to run. Buyers came immediately to an oversold BBY. It was a fast move, (Bars 1 and 2) but the entry proved very rewarding as the stock and S&P 500 took off to the upside.

All you did was identify the pattern, mark down in your trading plan that you would enter 1/8 above the trading range high, and decide based upon your own parameters what your money stop would be. The entry was of course predicated on whether the market was rallying and whether there was buying pressure on the stock.

This was a strong move and it didn't re-enter the range possibly stopping you out. If that happens, be prepared to enter a second time out of the range. Second entry is almost the norm in OTC stocks.

Remember, always look at your daily chart (see chart below) in conjunction with your 5-minute charts. It will tell you whether or not there are any inflection points that might help or hinder the trade.

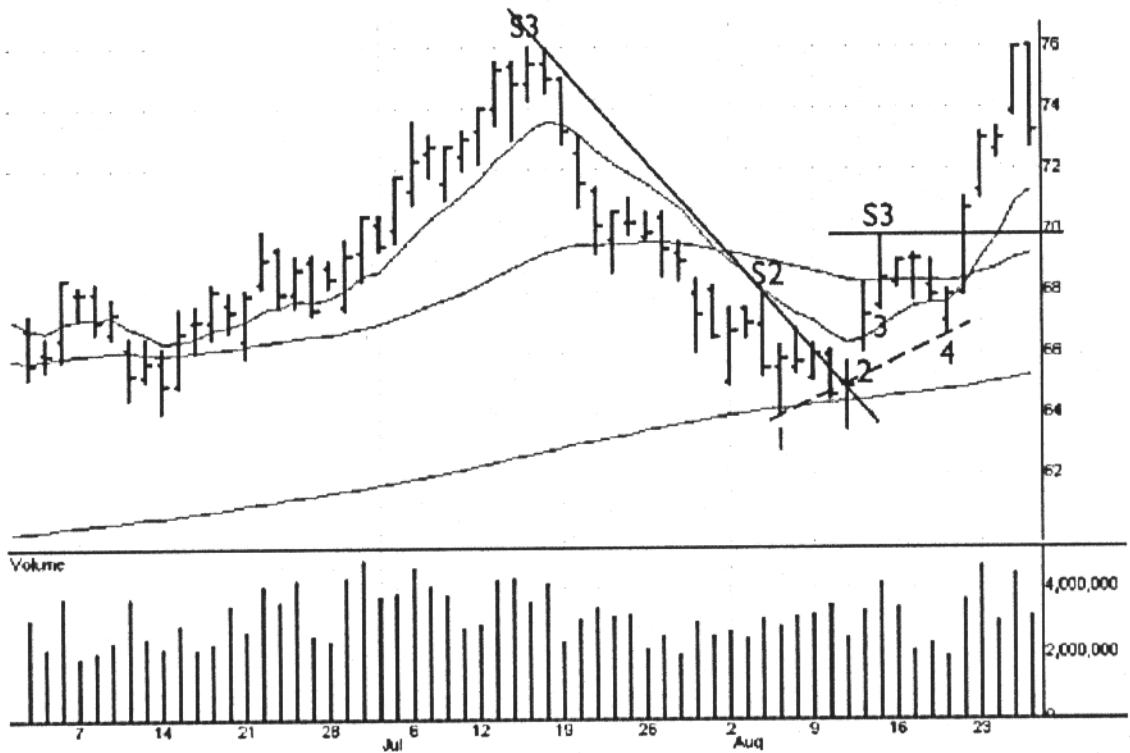


As you see on Chart 2, BBY moved from a low of 40 1/2 to a high of 80 1/2. The 56 5/8 low on the 5-minute chart was a 60% retracement of the entire move. Institutions are well aware of these levels, and maybe a few decided to add to their position, which was the first opportunity after such a powerful advance.

When a Slim Jim forms at the high of the day and it coincides with a key inflection on the daily chart you definitely want to take the trade. This pattern will also take the form of a rising wedge or ascending triangle if you would prefer names, but the bottom line to me is that it is bumping up against a key price level with rising lows and closing above mid point of the closest bars.

The following example of BMY is a Slim Jim with rising lows that breaks out the following day at the same time it moves above a key inflection point on the daily chart.

Bristol Meyers BMY



1. BMY pulls back to its 200 Day EMA which is rising. It is acting much better than the other drugs such as MRK, PFE, WLA and the sector index DRG, all of which have traded below and closed under their 200-day EMA's. BMY has much better relative strength versus the group.

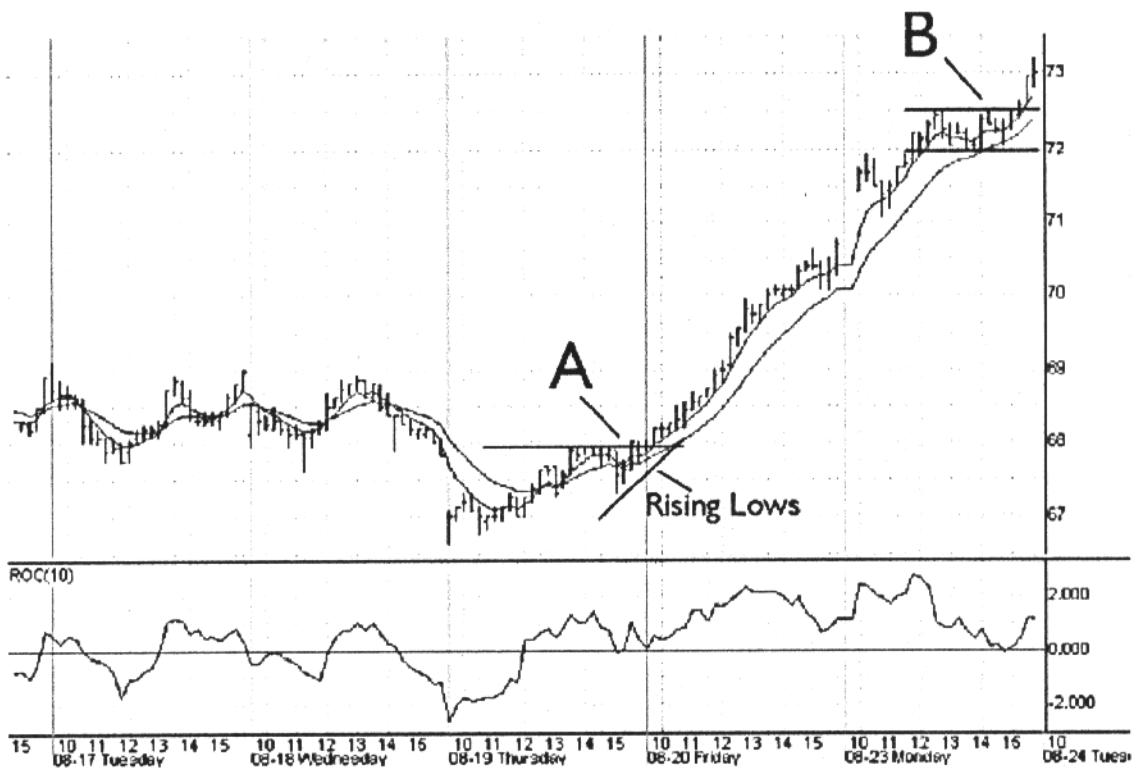
You draw the swing point trend line connecting a S3 point to a S2 point. You draw these TL's from point to point, and it doesn't matter if it intersects any other bar. This line puts me in alert to watch for a change in direction on increased volume. I am looking for closes above the midpoint and top of range. The odds are strong that the institutions will return to the drugs because valuations have come back to better levels.

2. BMY makes a significant move above the trend line on BP 1 pattern which is the strongest indication and it does this on good volume. It closes above the previous 11 highs which certainly tells you we are looking at a directional change. Your trading plan should include a planned entry 1/8 above the 2 BARS high for the next day.

3. Good entry at 68 7/8 and stock runs to a high of 69 3/4. It is usually the case that you will get a continuation move after BP 1, market conditions permitting (rally mode).

4. This is a 5 bar pullback that closes in the top of the range. The move from the low of 64 at 1 to 69 3/4 was 5 3/4 points. The retracement to 66 5/8 at 4 is a 54% retracement. The entire world will be entering above S3 at 69 3/4 which is a completion of a 1-2-3 breakout from a significant low (Some call it an A-B-C Chart) To me it just means the Generals are taking it higher and you want to be there with them for the ride. The action at 4 with a close in the top of range after a 5 bar pull back and after the BP 1 breakout of a swing point TL sends me right to my trading plan for the next day. Buy 1/8 above 4's high. Remember you are always looking for the earliest entry that has sound reason.

5. Good entry and excellent move. 68 1/8 entry and stock traded to a high of 70 3/4 on the day. Relative to BMY's range, this is good action. (See BMY chart)



BMY formed an intra day Slim Jim right at the 68 high (A) of 4 bar. (see chart 1) You had a planned entry off the daily chart confirmed by a Slim Jim with rising lows on the 5 minute chart. Signal is go. Bar 6 was a BP as all the action was above Bar 5. Pigs at the trough. When they want them they come in with the herd mentality. Recognize it and go with it. Bar 6 was a gap day but you got another Slim Jim at R which broke out as the S&P 500 mounted a 3:00 PM charge. BMY formed an intra day Slim Jim right at the 68 high of 4 Bar.

Slim Jim Reversal

These consolidations can take the form of horizontal trading ranges, slim triangles or wedges with rising lows. They can be very explosive breaking out to new intra day highs and lows. By trading these patterns on high RS value strong ADX stocks you capitalize on the momentum caused by Institutions, program traders and any of the accelerators that are involved (sells reversed). The higher priced stocks >50 give the best trades unless it has unusual volatility.

Key Point

When you see a Slim Jim in the last two hours of trading, be ready to act. Institutions, when they are buying futures at fair value to put money to work, will have to run in and buy the underlying stock late in the day because they were not able to buy enough futures at fair value. This is why you see some explosive moves late in the day. This always occurs during an up day as institutions must give up price to get in the market that day. Specialists won't short size to the buyer late in the day unless it is at an expanded price. These explosions will be in the S&P 500 program stocks.

The Slim Jim patterns take on added significance used in conjunction with higher time frame charts. Also, when today's patterns breaks out and it is also above a Slim Jim from the prior day, it can be explosive.

Remember, the longer and tighter the consolidation, the better the move. The dynamics must be clear for you to enter the trade.

Trap Doors

These are momentum trades that take advantage of emotional openings due to pre 9:30 AM S&P 500 futures trading. They can be played long or short, but because of how fast they set up, it is tough to get the tick on the short side. We are talking about NYSE stocks only because we can follow the volume and see bid and ask size shown with much more consistency. This is the best strategy to take advantage of a potentially profitable trade as you get in gear with the NYSE specialists.

Trade Criteria

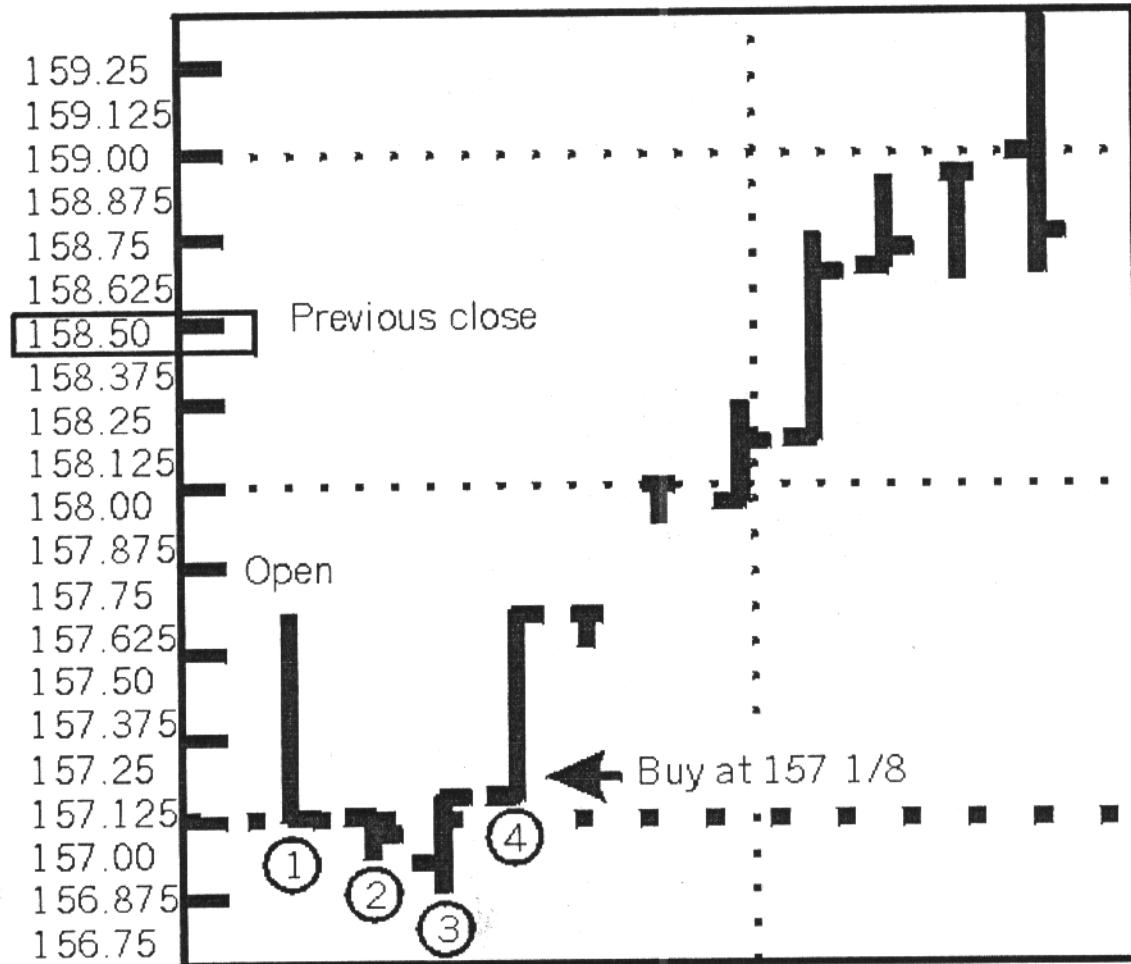
1. Best trades are in high RS value S&P 500 stocks.
2. Average daily trading range should be a minimum of 1 1/2 to 2 points.
3. Stock should also be trading above its 50 and 200 day EMA's. this is usually the situation with a high RS value stock.

Entry Rules (For Buys, sells reversed)

1. The stock must open below the previous close and trade down at least 1 point from that close.
2. After the opening bar, the second bar must make lower high and a lower low.
3. Enter long if the 3rd bar trades above the high of the 2nd bar. This indicates the market isn't going to follow through on the bad news that caused the down opening and a reversal may be in order. This is the earliest you can enter the trade. Under normal conditions you will enter on the 4th or 5th bar. The specialist takes out the emotional sellers on the opening and leaves the trap door wide open to take the additional selling out at lower prices. If he/she has to get long it might as well be at lower prices. Take it to where the volume is.

At some point this stock will have a good reflex rally as buyers return, programs kick in and the specialist lets the stock up fast as he/she unwinds inventory. You as the trader must recognize the market and stock dynamics (Week 3) that make you enter the trade.

Merck Chart MRK



1. The trap door is set when MRK opens at 157 5/8, down 7/8 from previous close of 158 1/2. (The volume on the open is 80,700 shares.) It quickly trades down to 156 13/16 on only 19,000 shares. This low volume helps create the vacuum that will make a reversal that much more forceful.

2. MRK trades at 156 13/16 and buyers start to enter the market.

3. The third bar closes at 157 1/16 (at its high) and above the high of bar two, giving the early buy signal (bar three trading above bar two). MRK is now trading at the midpoint of bid/ask spread and then quickly moves to the ask size, another indication of buying pressure (the bid has been raised three times at this point).

4. MRK is now offered at 157 1/8. When bar four trades above bar three (at 157 1/8), you go long, 1/16 over the bar three high. When the trigger was pulled on the trade, the following conditions existed:

NYSE ticks had increased by +200.

The S&P futures had started to rally.

Other key market leading stocks had also started to rally.

Buy programs were starting to kick in.

The stock had reached a level down 1 1/16 points from the previous close that began to attract some buyers.

The stage was then set to climb past the trap door. Probabilities now favored the trade because the specialist wanted the stock to rally so he could move some inventory, buy programs were kicking in, and major S&P stocks were rallying. Institutions buying MRK had to move up with the rally and maintain their share of the volume because the low-volume drop after the opening meant they had not bought enough stock at the lower levels.

Note: On your 5 minute charts you are going to have a 3 to 5 bar reversal on 90% of the trap doors. You are looking for that move back above the high of the low bar if the close of that low bar was above the midpoint or on top of range. This is a trade can quickly change direction if the dynamics don't remain positive.

Concluding Remarks

At the conclusion of this chapter you should be comfortable identifying stocks that are in strong momentum patterns or are changing direction and about to trade at new levels. It matters little whether it is a pullback trade, consolidation trade or WRB moves. You are always working versus inflection points such as previous highs, lows, range, closes, swingpoint trendlines, volume, volatility, price and time.

Plan your trade, and use the inflection points in conjunction with the market and stock dynamics. You can't force an up trade on a down tape. In Week Five, I will conclude with putting it all together with several more patterns including the implied volatility measurement for an extended stock.

Have a great week.

Kevin Haggerty

TRADINGMARKETS.COM Members, Welcome to Week Five

In the fifth and final week of an all too short course on day trading we want to leave you with a good outline of the key points that we have discussed so that you have a good guide to refer to going forward in what I trust will be a successful trading experience.

Day Trading Defined

The professional day trader is a person who takes no positions home overnight. The risk profile doesn't include a NEON type of trade that closes at 44 and due to company news opens at 18 3/8 the next day (Week 1).

To be successful, assuming you have acquired the necessary market and execution skills, you must be utilizing the proper technologies. Most traders that attempt to trade for a living do so out of an office of a registered broker dealer. Broker dealers' communications are the fastest and most dependable, and they are available with access to T-1 lines for all direct execution hook ups to Super Dot, NASDAQ, ECN's, etc. Day traders that trade in a remote office or their homes should attempt to get direct access communications. T-1 lines are expensive but try for ISDN or 56K-frame relay.

If you can't go fixed direct access communications then you should have ADSL or cable box access through ISP. These are both fast but your ISP is the potential problem.

You must adjust your trading to the communication speed. I highly suggest you trade through a direct access NASD broker dealer that will also provide you with some excellent analytical and execution software.

Margin

Review the examples in week 1. You must understand the rules and risks of margin before you begin trading.

Don't buy it on margin if you don't have the allocated cash reserve to pay for it in cash. Day trading has less risk using margin than taking home a position overnight but a stock can and will again stop trading during the trading day due to news. You can find yourself in the same situation as the NEON trader that took it home at 44 and saw it open at 18 3/8 the next day.

Short selling is extremely dangerous. If you have enough capital to pay for it in cash when you use margin the stock can only go to zero, but what about a short sale? Lets say the stock stops trading during market hours, with news pending because of a takeover. The price can be way beyond your margin reserve and now what



will you do? A long can only go to zero but a short is unlimited to the upside. It does happen, so be aware of the kind of stocks you short and don't ever take a naked short home overnight. Buy a put if you think stock is a short.

The Business

You have done the initial due diligence (it's never complete) and fully understand the risks of trading. The difference between direct access firms and on-line brokers is clear, as is your knowledge of direct access communications such as T-1, ISDN, 56-frame relay (week 1) and ADSL or a cable box through an ISP. If you have anything less than what I've mentioned please don't day trade unless you are prepared financially and mentally to buy and hold the stock because of the current fundamentals.

Excellent, you have made the correct decision going through a direct access broker dealer because you have decided to day.

Just like any other business you must make a financial commitment to starting the business and realize that you run the risk of losing 100% of your initial investment.

Financial Commitment

Your capital must be enough to sustain your positions. Most traders start in the \$25,000 -- \$50,000 range if they expect to make a living in a reasonable period of time. Anything less and you are just probing the business to see how you do, which is an excellent way to do it provided there is no pressing need financially to have the business return enough of a profit margin for you to live off the business.

The financial commitment is not the amount of capital; it is the amount you can afford to lose. You are willing to continue trading after a stretch of losses because you believe in your trading plan and have allocated X amount to make the business profitable.

Lets look at a simple example that you might use as a new trader. You have decided to start with \$50,000 in capital and will make a financial commitment of \$15,000 or 30% of the initial capital to turn this business profitable. If you lose the \$15,000 you walk, or if you decide at anytime that you are not suited psychologically to day trade close down the business and find something else to do.

Maximum Loss Per Trade

The next step is to determine your initial maximum loss per trade. A good way to do this is to paper trade your stock selections for a period of time to approximate the percent of profitable trades you get assuming entry. If you select a stock in your trading plan but don't get good entry it doesn't matter – no entry no loss. Keep track of the range from entry to high because this is so important in the traders' equation regarding maximum profit per trade. It will be rare if you manage the trade to its full range, but it will tell you that the volatility and trade selection was good. Allow room when judging shorts because it's not easy to get the tick.

Paper trade from entries off the daily charts utilizing inflection points such as a previous high or low, and swing points (see Week 4). Only use the 5-min charts if you have a clearly defined pattern such as a slim jim with a definite entry price.

Don't get too excited if you have great success because it's not nearly the same until you find out whether or not you can pull the trigger (enter) or push the buttons (exit) with real money. That is the psychology they talk about but never define. It is not that difficult if your selection process is good and you have enough self confidence to realize the market controls us (not vice versa) and that a good trading plan will succeed over time.

Paper trading was successful, ready to go live, but still nervous. Here is a very conservative plan to use.

Conservative Plan

Your financial commitment is for \$15,000 or 30% of your \$50,000 in capital. We are going to use 50 trades as the maximum number of consecutive losses before you lose the entire \$15,000: with these two numbers you can determine your maximum loss per trade.

$$30\% / 50 \text{ trades} = 0.006 \% \text{ maximum \% of capital}$$

$$\$50,000 \times 0.006 \% = \$300 \text{ MAX loss per trade}$$

Note: You can increase the 50-trade number and lower your max loss per trade if you need more cushion getting started.

This is a very conservative plan for a trader but why not? You are starting a new business. Most traders tend to use 1% to 2% as guidelines. We have dropped to less than 1% giving you lots of room for your trading plan with a 50-trade consecutive loss allowance.

Your trading plan is better than that so in reality you are probably only going to blow up if you don't control the loss side of the traders' equation. Remember, if the market doesn't prove your trade correct in a reasonable time frame you get out immediately. You don't just sit and wait for the \$300 loss number to come up.

You can't control what the market does, but you can control your risk. Unless they stop trading on you, that \$300 loss can't be violated.

Yes, you should be encouraged, this business has an excellent chance at being successful provided you have the discipline of keeping to the \$300 max loss per trade and your trading plan is decent. The combination will keep you in the game as you get better in your trade selection and market feel.

You can allocate the \$300 max per trade loss in different ways. Starting out, I suggest you trade a smaller amount of shares. The more volatile the stock, the less shares per trade. It is always easier emotionally to give yourself more room on the stop with less shares than trading say 1000 shares of IBM and trying to keep your loss to \$300. It puts too much pressure on your entry timing.

It might be better to have two trades of 300 shares per trade allowing 1/2 point (\$150) stop room for each trade than 1,000 shares risking a 1/4 (\$250). This assumes the stocks have reasonable volatility.

If GE has an implied volatility of 40% and your normal trade is 300 shares and you decide to take a trade in MU with IV of 80% I might cut my trade size in half so I wouldn't have to keep my stop to close in such a volatile stock. The average daily range of the stock in addition to its travel range will determine your share allocation. GE and AOL are two different stocks.

Regardless of how you allocate maximum loss per trade the "Day Traders' Equation" must be balanced.

Day Traders' Equation

Maximum % of profitable trades + maximum profit per trade - small losses X multiple trades = SUCCESSFUL DAY TRADER.

If you have some very large winning trades and your losses remain small then your % of profitable trades can be less (Week 1, NEON, trader C). A high % of profitable trades and losses still small takes pressure off of how big your profit per trade must be. If you tend to take profits too soon then your stock selection must be extra good to compensate for narrow margin of profit on winning versus losing trades.

The constant that you have the most control over is your loss number. This must remain small. If your % of winning trades is positive and your profit per trade is greater than loss per trade don't forget to maximize the amount of trades for a higher absolute profit.

There are many different ways to manage a winning trade, and I believe you have to be more aggressive with moving your stops up once your trade is profitable when you day trade stocks. This is because of range and time limitations.

Managing a Winning Trade

For example, you are long 400 SHS of XYZ with a 1/2 point stop loss (\$200) and it is now trading up with a 1/2 point profit what will you do?

1.Sell 200 SHS, lock in 1/2 point (\$100) and leave the stop as is so the worst you will do is break even if your stop is hit which is now 1 full point away from current price.

2.Sell 200 SHS, lock in 1/2 point (\$100) and move the stop up to entry price, which essentially guarantees you the \$100 profit if you subsequently get stopped out.

3.Do nothing because the dynamics of your stock still look good and market direction is still up

I would eliminate #1 because it is a day trade and you don't want to give back 1/2 point profits when your average profit per trade might range from 5/8 to 7/8. Also, you only want to remain in the trade if the market proves your trade correct so how can sit and do nothing while your stock trades down a point.

#2 is my choice because I have locked in a \$200 profit and am giving the remaining 200 shares a chance to run until the market that I exit the trade. Yes, you might get stopped out by the first normal pull back, but you can always re enter the trade.

#3 is a choice you might make if the stock dynamics are very strong as the buyers are very aggressive with no visible selling pressure. You will have this decision very often on a strong up trending day. By keeping the entire 400 shares in play you have a good multi point opportunity. You can move up a tight stop under the 1/2 point profit and if it runs great, if not, you have what you did in #2. If it's early in your day you will probably take the 1/2 point sale on 200 shares to get the ledger.

In an effort to keep your losses small you will get stopped out often in day trading. There is lots of daily noise due to S&P 500 futures and program trading so you must maximize your profit per trade. That is why your stock selection should consist of the RS value, high alpha, and strong EPS stocks. We want to trade these stocks in their advancing stages when momentum is strongest.

Stock Selection

Stocks all go through four major phases which include the following: accumulation (basing), advancing, distribution (topping), and declining. Short-term traders want to be involved in the dynamic advancing stage (Wave 3 for you Elliot Wave fans) and in the declining phase for shorts. During the advancing phase stocks will run and then consolidate for a short period or pull back 3, 5, 7, 8,13 days then explode again to the upside (sells reversed). I point out these pull back days because they are most common but not a rule.

All moving averages will be rising during this explosive phase, and the stock will be above its 20-, 50- and 200- day EMA's. If you did nothing else in stock selection except pick stocks in momentum phases (advancing/declining) how bad can you do? However, to make your selection process more powerful, we want you to do a little more work.

Key Point

If a certain stock is outperforming the S&P 500 and is part of the index or is some other liquid big cap name, you can bet that the institutions will overweight this stock and build a large position as new money comes in. They have to beat the S&P 500 regarding performance so they must chase winners in this pursuit. This aggressive performance game to stay ahead of the S&P. 500 is responsible for the explosive moves out of short-term consolidations and pullbacks during the advancing (declining). As day traders we want to ride these waves.

The big cap S&P 500 hysteria helps us as traders because we will often get a major assist from program trading, momentum that are front running the institutions, option-related trading and the specialist/market makers propensity to commit capital to the big cap stocks.

There will be times that you will spot the stocks just as they break out of the accumulation or distribution phases, and you can get involved early, but I believe as a day trader you are better served going right to the high relative performance stocks already into the explosive advance. Remember, when the Generals are running then we want to be on board.

TRADEHARD Filters

TRADEHARD has some excellent filters to select these momentum stocks. (see Filters Week 2)

The primary filters I use to find these high RS stocks (sells reversed) are the TRADINGMARKETS.COM Interactive RS Investigator Search. Make sure you filter for a minimum of 500,000 shares, and you will do better with higher priced stocks. I look for stocks with RS Value of 80-99 for longs and 40 and below for shorts.

The second filter I use is the TRADINGMARKETS.COM ADX Trend Finder. As I said in Week 2, if I had only one filter this would be it. For longs, don't forget to search all ADX Values with $+DMI > -DMI$. (shorts $-DMI > +DMI$)

These two filters give me a good master list. The next step is to look at a daily chart of each stock on the list looking for set ups. After you have done this several times, you will develop a sense of what is close to being tradable and what isn't. There is some on the search results as fast changing momentum won't necessarily show up in reduced or increased RS right away.

Key Point 2

ADX tells us how strong the stock is trending, and the DMI tells you which direction. When you combine this with High RS value stocks, you will end up with a solid trading list of stocks in the momentum phase. After I have scanned the charts I will check some of the other specific searches on TRADINGMARKETS.COM such as Pullbacks, Explosions and "Where the Action Is" list. I will then work my way through the site for stocks I might have missed from checking my master lists.

Mandatory reading for you everyday is the Top Relative Strength and Earnings New Highs List found in the Hedge Fund Manager's Corner. These stocks have made new highs, and also are ranked in the top 15 - 20% of both relative strength and earnings. Normally these stocks have the best technical and fundamental prospects to move higher. You can check any of your other stocks for EPS in IBD (Investors Business Daily).

As you have learned during the course, WRB breakouts to new highs from consolidations or pullbacks are usually followed by strong continuation moves which is what the day trader can easily enter as it trades through an inflection point.

One other site I use everyday is www.fntn.com. This is a free site that gives you market summaries of the S&P 500, Dow 30, NDX 100 and some of the other major sectors. These summaries give you key data such as volume relative to 50-day average volume and where the stock finished in its daily range which is key to your trade selection. There is a quick guide to the summary charts on the site.

Stock Dynamics

The trading list you are now working from has the top RS stocks versus the entire database of all stocks that satisfy a minimum volume requirement. You should also favor the top RS and EPS combination for better results. These are the stocks that the institutions will be pushing provided they are outperforming the S&P 500. They screen for earnings, so why can't you?

Once you have selected your entry point from the daily chart, (assume it is not intra day pattern) you must be keyed on the stock and market dynamics to decide if you will take the trade.

Quick Checklist (Buys, Sells Reversed)

1. Did stock open up on the day?
2. Is it trading above the open?
3. Where is the volume trading, on the bid, or at the midpoint and offered sides which is what you want to see as a buyer.
4. Where is size reflected? Bid or ask?
5. Are the bid and ask moving higher without unusual volume trading.
6. If there are blocks (5000 shares or more) trading are they at midpoint and offered side?
7. How are related stocks trading? Is rest of group ok?

Key Point 3

Your best trades will always come from trending stocks above the open for buys (sells reversed), and with the market averages moving in the same direction as your trade. There are contra trades such as Trap Doors, Slim Jims in stocks that are oversold intra day and snap back for a good trade, but many of these are reflex trades, and you must be nimble because they can reverse in direction of trend quickly.

When the Generals are in and buying pressure is strong you will get expansion of range, (higher prices) help from programs kicking in and momentum players buying strength. Throw in the hedge funds front running, and it makes for multi-point moves. As a day trader you are not in the information flow between Institutions, brokerage firms and specialists/market makers, but you can see when the stock dynamics favor buying pressure and if the market looks good (sells reversed). (Week 3)

The Generals get very aggressive when they have competition on the same side, and when the Accelerators get going it can to multi-point moves.

Market Dynamics

The following table is a simple but effective tool that will help your decision on both entry and exit more than you can imagine. It will take you some time to see different situations develop, but your intra day market feel will improve dramatically.

Market Table

This is actual market data for 8/19/99 9:45AM to 11:00AM EST. This is the table that monitors overall market dynamics. (Week 3) A glossary of symbol definitions is on the following page.

	9:45	10:00	10:20	10:30	10:45	11:00
SP'U	-10	-10	-10	-8	-14	-14
SPX	-11	-12	-12	-10	-16	-16
TICK	-482	-474	-528	-172	-181	-470
PREM	3.85	3.80	3.85	3.70	3.75	3.60
A-D	-1032	-1014	-958	-908	-1035	-1098
UVOL	13	26	44	48	51	58
DVOL	41	61	93	99	126	149
DOW	-91	-84	-79	-71	-105	-97
NDX	-21	-27	-33	-28	-45	-44
BD	-9	-5	-9	-8	-5	-6
SOX	-	-	-	-	-	-
MSH	-	-	-	-	-	-
DRG	-	-	-	-	-	-
RLX	-	-	-	-	-	-
BKX	-	-	-	-	-	-
XOI	-	-	-	-	-	-
OSX	+	+	+	+	+	+
RUT	-	-	-	-	-	-

This table takes less than 45 seconds to complete. You round off numbers for the S&P Futures, all the averages and the volume figures. You use exact numbers for TICK, PREM, A-D, and BD. For the sectors, they are either plus or minus (green or red on your screen).

At the bottom of the sheet I make notes on which stocks are showing strong or weak intra day relative strength and look for set ups on the 5 minute charts.

You should also make note of any key market news that should generate a reaction and observe how the market reacts to the news.

Start to use this table on a daily basis, and you will start to see the relationships develop. Is it just program selling seeing that the sectors are all pretty strong and the breadth is still good, or are the Generals in there selling because up volume / down volume keeps getting worse with all sectors turning minus?

There are many market clues that you will only start to understand if you keep the table. After a period of time your market feel will improve ten-fold, and this will improve your entry into good trades. You will observe that trending days will all have similar traits as do the over reaction days that also provide good opportunity. The neutral days tell you little by flat averages, but maybe breadth, volume or certain sectors will provide pertinent information.

Note - I use 26 boxes for table so you can record market every 15 minutes if needed.

Trade Selection

During the advancing and declining phases of a stock you will be using some simple trend-continuation strategies to enter these momentum stocks. These strategies will have the highest probability of a profitable trade. You will be entering trades after WRB (wide range bar expansion) moves out of consolidation and breakouts from consolidating volatility patterns such as dynamite triangles, flags and pullbacks from swing point highs.

These minor pullbacks in a trending stock usually only last 3, 5, 7, 8 and 13 days and take place above rising 20-, 50- and 200-day EMA's. Your entries will be in the direction of the trend. If the momentum phase is still strong there should only be minor corrections to the trend. Thirteen day corrections are the exception with the strongest trending stocks. When you are going through the charts from your master RS and ADX lists you will be looking at the current OHLC bar in relation to the previous highs, lows, closes and range. You must also be observing volume, volatility and swing point trendlines.

Key Point Review

A review of these comparisons and observations is best done by looking at some charts, but first let's review some key points.

1. Volume precedes price
2. Increased volume with narrow spread on downside is strength and usually precedes a reversal.
3. Decreased volume and narrow spread on upside is weak and reversal can follow.
4. Breaking of swing point trend lines on good volume is significant while breaking TL on low volume is not as important.
5. WRB breaking out of congestion or closing over at least two previous closes with increase in volume is usually a strong indicator of change in direction.
6. Stock rallying on heavy volume from a higher low is bullish, especially if preceding low was on light volume. This happens often at 1-2-3 bottoms which occur at significant swing point lows.
7. Closing above midpoint and in top of range are both bullish. Below mid point and the bottom of the range is bearish.

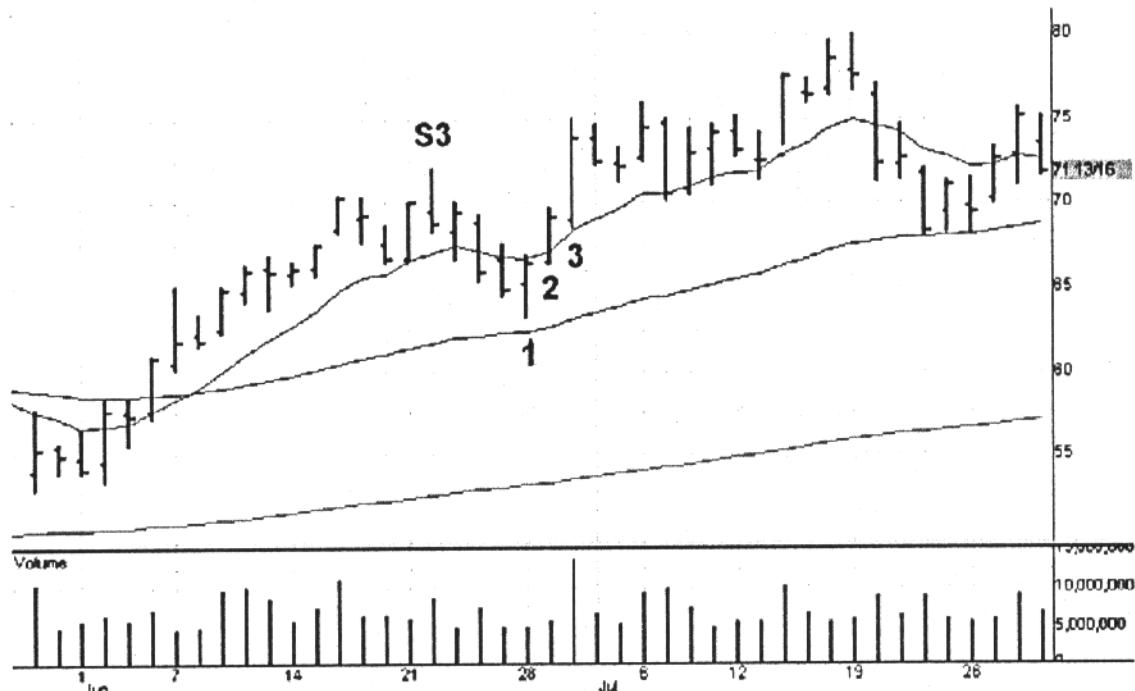
Note: Buys (Sells reversed) for all key points.

8. Stock closing above last five closes is more significant because of time than above prior day. The same applies to highs or lows if looking for shorts.

9. Higher lows on last few bars in congestion puts you on alert for breakout of pattern to upside.
Lower highs alerts you to possible downside break.

10. Draw the swing point TL's and draw more than one rising or declining TL from a common point which will give you a stronger buy or sell signal.

Applied Materials (AMAT)

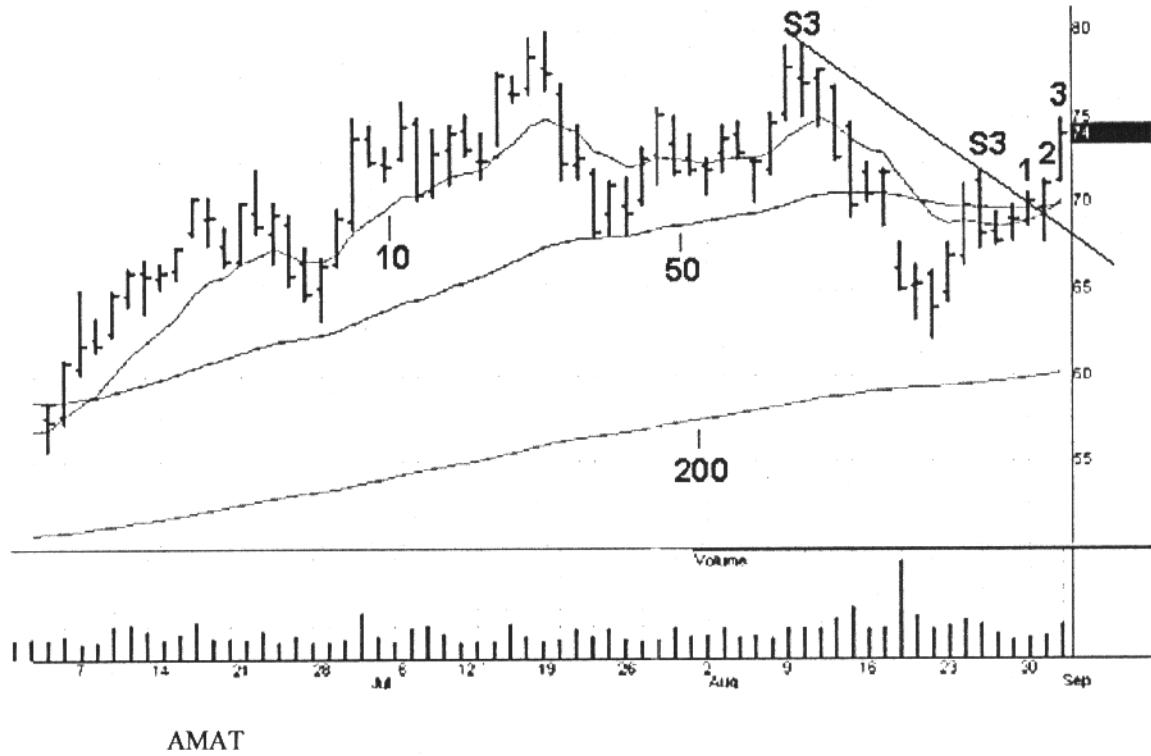


AMAT

1. - 5 day PB (pull back) from swing point high (S3).
 - Closes in top of range and above previous two closes.
 - Entry for Day 2 is 66 7/8 which is 1/16 above Day 1 high.
2. - Enter at 66 7/8. Stock traded to high of 69 5/8 and closed in top of range at 69 1/8 on increase in volume from Day 1. This was good thrust.
3. - Enter at 69 1/4, 1/8 above Day 2 close of 69 1/8. Stock traded to a high of 75 and closed at 73 7/8. This was a big WRB day that led to an 8 bar consolidation before final high.

This was a high RS stock that had a minor pull back to a rising 50-day EMA which enabled us to enter on a simple trend continuation strategy for two days in succession.

AMAT Chart 2



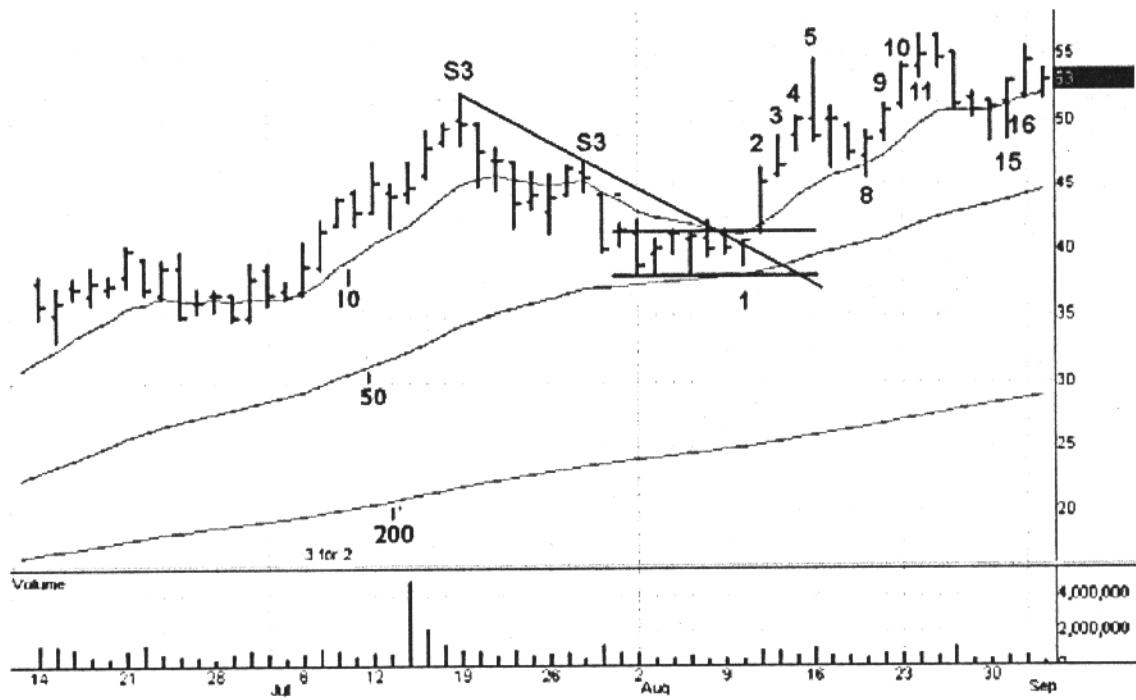
AMAT

1. Stock closes above its 50 Day EMA in the top of its range, above the last seven closes in addition to being the sixth higher low in succession. AMAT closed up 1 9/16 on a day that the S&P 500 cash index was down a big 29 points. AMAT also closed above a swing point TL. The volume wasn't unusual, but the buyers held their ground.

2. Good entry at 70 5/8. Stock trades to a 71 1/4 high and closes in top of range at 71 1/16 on Outside Reversal Day and WRB, setting up trade for the next day.

3. Good entry at 71 3/8. AMAT trades to a high of 74 7/8.

TriQuint (TQNT)



TQNT (Sequence of 8 trades in 15 days)

This sequence of trades gave continuation entry above the prior day's high. It started with a WRB out of a consolidation at the 50-day EMA.

1. TQNT closes in top of range at 40 5/8. You are on alert if TQNT trades above 41 1/2 which is high close of the eight bar consolidation.

2. Stock opens at 41 3/4, back to 41 3/8, then makes a move to a high of 46 1/4 on good volume. This opening was a BP1 (Week 4) pattern where all of its range was above Day 1. The WRB closed above the swing point trend line and above the last 9 highs and closes.

3,4,5. Momentum carry forward with entry from daily chart each day.

8. TQNT pulls back 3 days and closes in top of range after prior day's closing in bottom of range. It also closes above the 10-day EMA. This pull back is from a new high at Day 5 of 54 9/16.

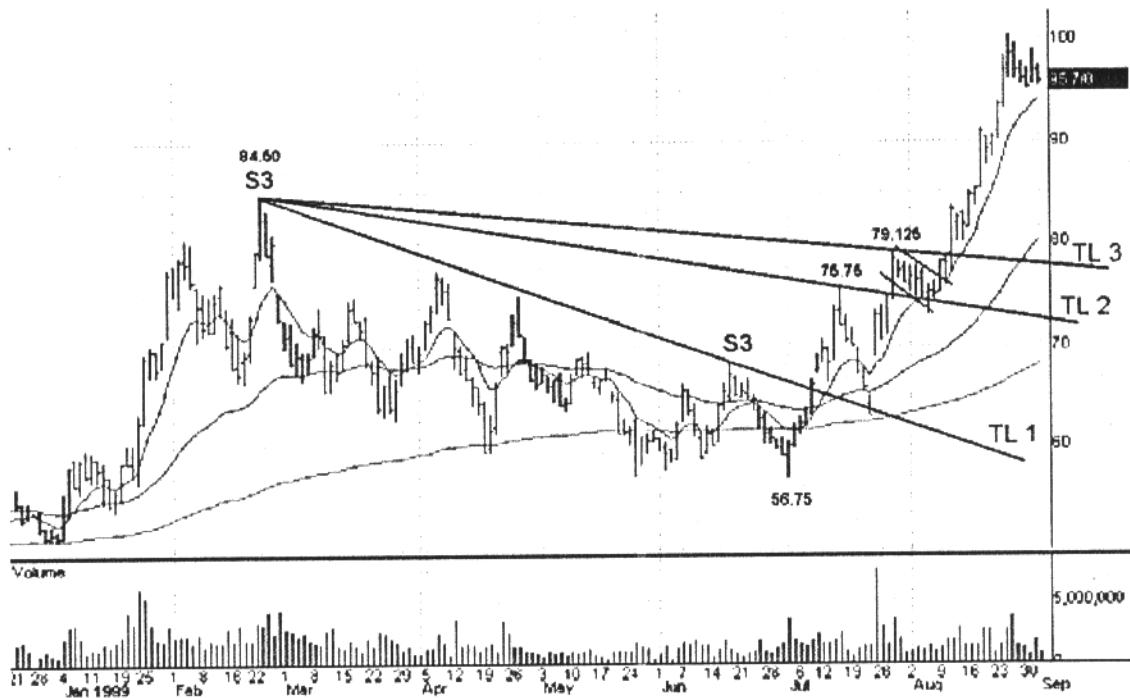
9,10,11 All good entry and trades as TQNT makes new high of 56 1/2.

15. TQNT pulls back 5 days (counted from 15 back to 11, double top at 56 1/2) and closes at 51 just above the 10 day EMA (again).

8/31 16. Good entry. Good trade. If they come for it again, get on board.

9/1 Good entry at 53 and TQNT trades to a high of 55 7/16 by 11:30 AM before any stop out.

Gateway Chart (GTW)



GTW - Swing Point TL From Common Point

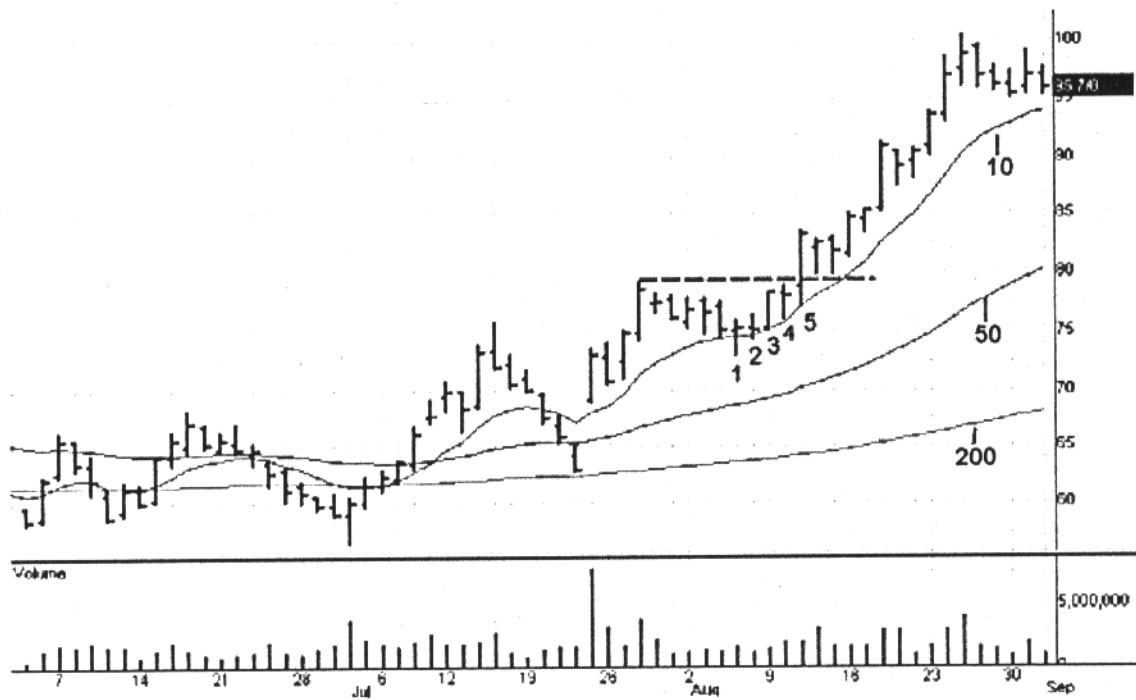
After making a record high, GTW corrects from 84.50 to 56.75. You draw your S3 TL from common point at 84.50 to last S3 (If none use an S2) before low. In this case its a four month trend line.

GTW breaks TL and runs to 75.75, which is a 68% RT of correction from 84.50 to 56.75. It also surpassed the second S3 swing point, and that was a strong signal for a change of direction. The stock also re-crossed and closed above its 50 and 200 EMA's. Momentum had been regained. It always seems to happen at and around the 200 day MA's.

GTW hit the wall at the 68% RT level and corrected back to 62 7/8 right at the 200 EMA. This was 68% of the 56.75 to 75.75 move. Funny how the Fibonacci numbers of .38, .50, .618, .70, and .786 keep showing up. I use them to alert me to possible reactions at those levels.

The rally from 62.875 starts with a big gap and WRB on news and the stock breaks through TL2 on WRB with good thrust and forms a FLAG at the 80% RT level. Once the TL2 was scaled, there was plenty of momentum, and a run at the old high was in the cards.

GTW Chart 2



GTW (Chart 2) Momentum

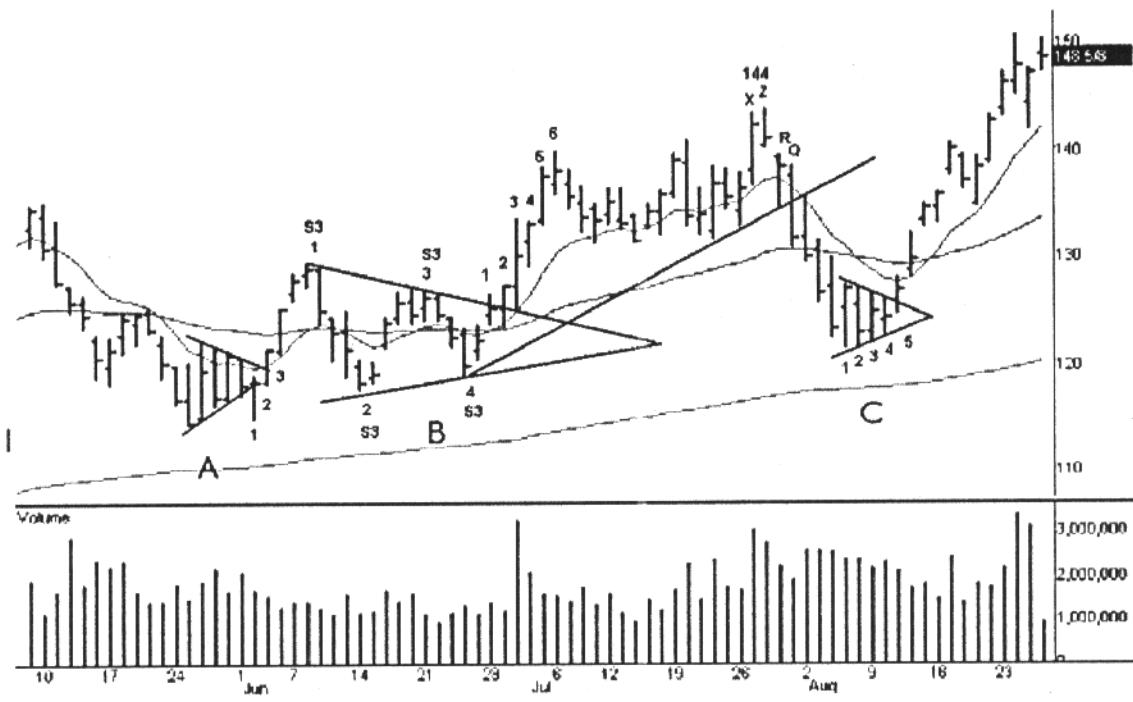
1. Seven Bar PB (pullback) to a rising 10-day MA which is also above a rising 50 and 200 EMA in the top of its range and above the TL2.
2. Good entry. Stopped out. Plan to enter on day 3, 1/8 above the day 2 high.
3. Good entry with multi-point move.
4. Entry stopped at loss.
5. WRB B/O (break out) of TL3 and above 79.125 swing point high. GTW took off, and they ran it directly to 100.375 high on 8/25. The low of 56.75 got tested, it broke the TL2 line, and then the momentum phase was in swing to the upside. This was on your master lists.

Narrow Range Consolidations

After strong thrust moves in either direction, stocks will consolidate as dynamite triangles, flags, symmetrical triangles, horizontal trading ranges etc., but it is all with shrinking volatility. This reduction in volatility usually precedes a strong move in the direction of the trend. (see AXP Chart)

The dynamite triangle or flag usually gives you the strongest moves in the highest RS stocks because they usually only pull back or consolidate for 3, 5, 7, 8, and 13 days. (Review Week 4)

AXP Chart

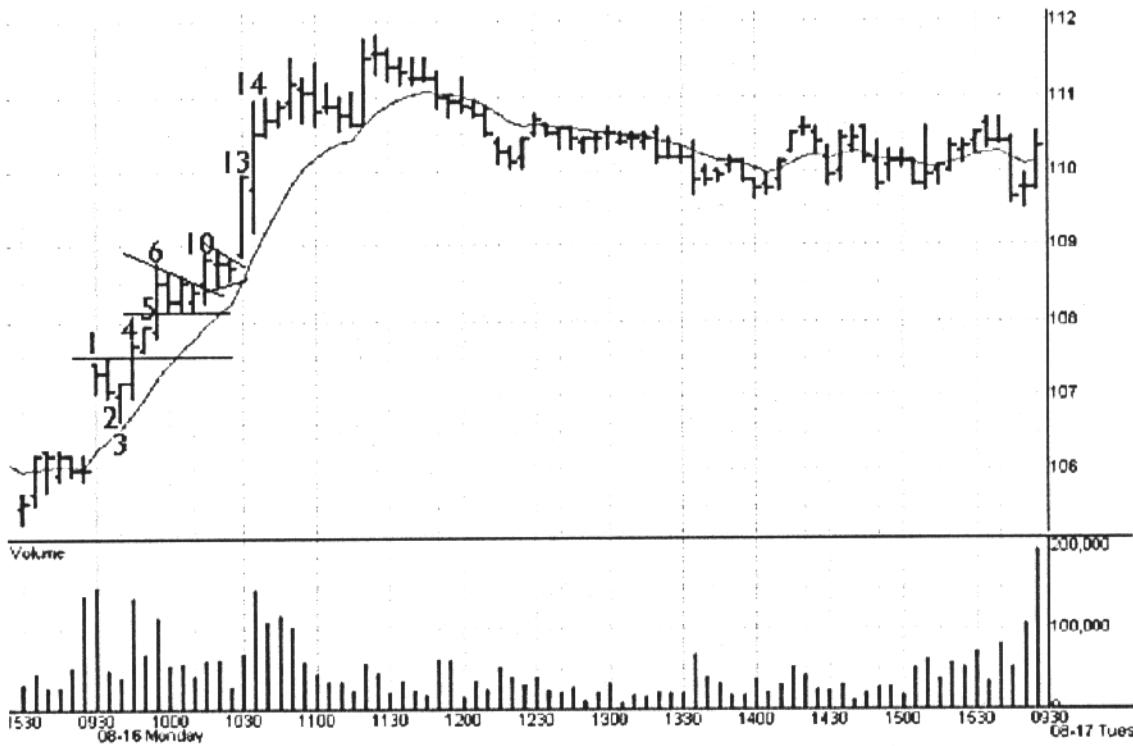


Intra-Day Patterns

When you are working off of your intra-day charts looking for trades, keep it simple and utilize several patterns that are easy to spot. You will do much better that way instead of using the gunslinger approach where you buy or sell a stock reacting to every increased bid or offer. When you react and trade emotionally, you will lose because of all the short-term noise.

The Opening Reversals (OR's) and Trap Doors are two very good strategies to play over-reaction on the openings due to excessive S&P futures action which always has a fast counter-trend reaction. OR's are, of course, easier to see for a new trader while Trap Doors require you to read a 3 to 5 bar reversal pattern and be able to recognize when the stock dynamics are changing. (Review Trap Doors Week 4)

HWP Chart (OR)



The stock gapped open 1 7/16 points to 107 7/16 from the prior close of 106 (BAR 1). It traded down to 106 11/16 (BAR 3) showing strong relative strength, as it didn't come close to filling the opening gap. The stock quickly reversed on volume and traded back above the opening price. It traded to 108 1/2 on a WRB (BAR 6), consolidated to a FLAG and broke out again at BAR 10, consolidated two bars then two big WRB thrusts to 111 1/2 before fading.

The discipline of the pattern and the dynamics put you in the trade. We got lucky that the momentum front runners took it so high. They got their lunch handed to them the next day as HWP closed down 5 3/4 points.

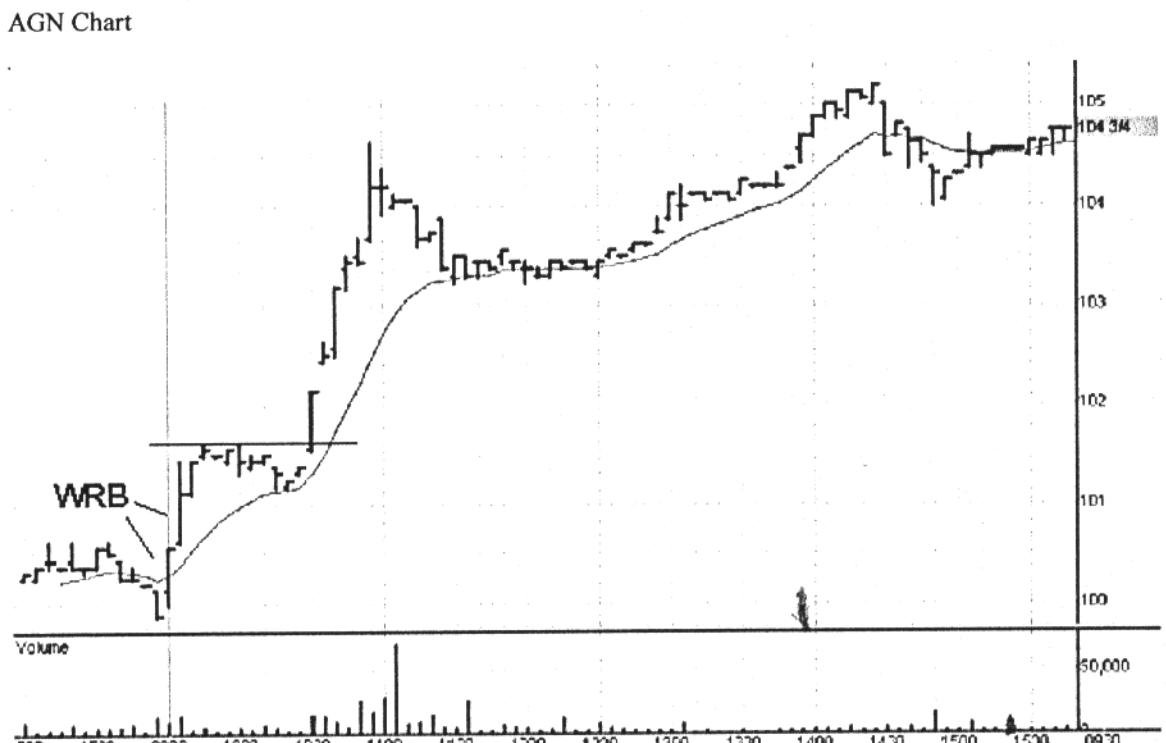
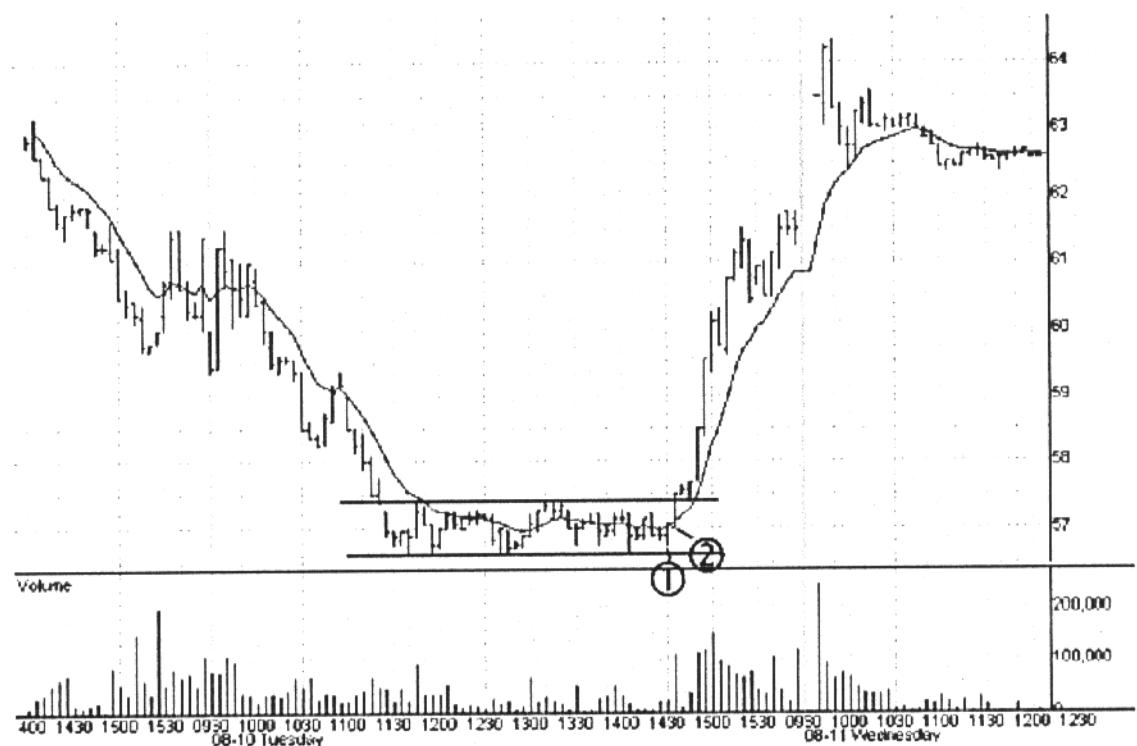
It is important to note that this HWP example is a stock that gapped up, traded down, remaining above prior close and reversed opening to the upside. Most of your OR's will be stocks that open below or trade below the prior close then reverse opening to the upside (sells reversed).

Slim Jims

These are simple easily recognized but explosive patterns that you find everyday on your intra day charts (5 min). They are tight narrow range consolidation patterns where you play the breakout to new intra day highs or lows and also the counter trend moves from over sold or over bought conditions. They are simple trend continuation patterns just as you utilize on your daily charts.

Slim Jims are most often long tight horizontal trading ranges. The longer and tighter the consolidation, the more powerful the breakout. The following chart of BBY is an example of an over sold Slim Jim that exploded to the upside.

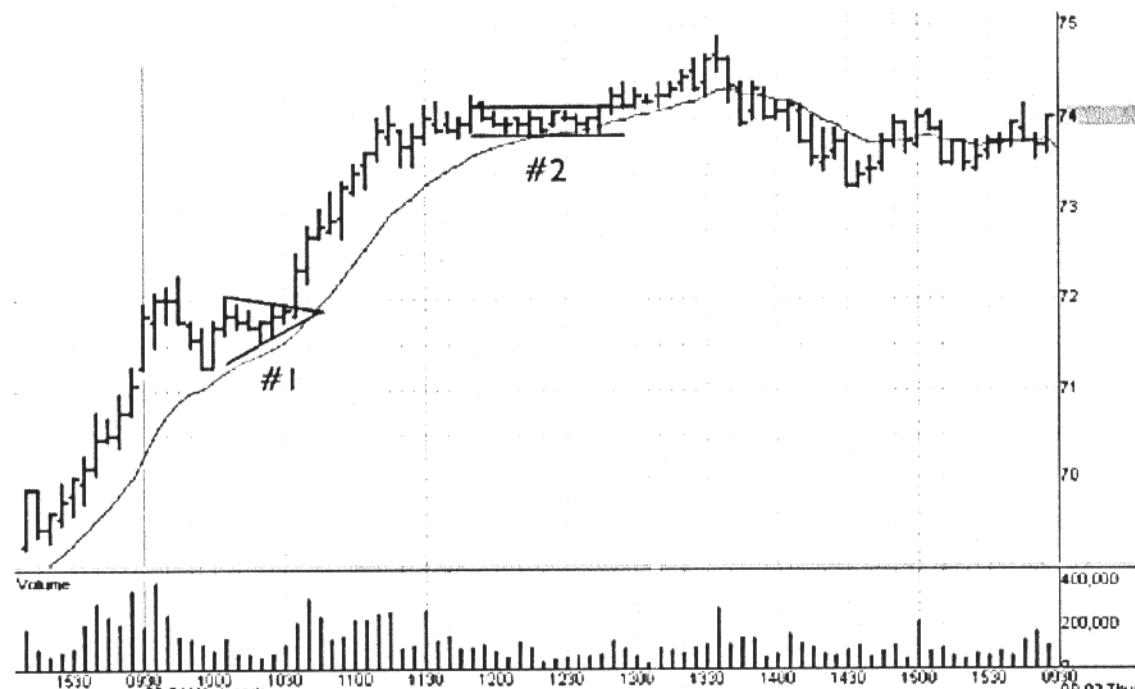
BBY Chart



AGN (5 MIN)

AGN is a breakout to new intra day highs from the first consolidation after a 2 WRB thrust up. The related stocks in the same group were also strong.

AMAT Chart



AMAT (5 MIN)

AMAT is an example of a stock where we entered the trade at 71 3/8 right after the opening (8/31 Outside Bar Entry). Entry point was 1/8 above previous close. The stock consolidated in a slim triangle after it had traded up to 72 14. I call them Dynamite Triangles. You could also draw the larger triangle you see, but it's not art school, so start from right to left because that gives you the earliest entry.

If you were fast enough, you got in between 72 - 72 1/4. After it made new intra day high above 72 1/4, it ran fast. If you had enough courage, you bought the break out of the next Slim Jim #2.

Key Points

1. When you enter a trade from a Slim Jim, it can give you a head fake as it trades back into the consolidation, and you might get stopped out. Don't be afraid to take the second entry as it trades through your original entry point.

As a new trader, you probably should make second entry a rule. It will miss some trades, but it will give you a higher percentage of profitable trades, especially in OTC stocks where large market makers can influence the stock.

2. It seems that many traders are reluctant to take the trade as it goes to new levels. Believe it and take it. When that high RS stock gets rolling, it is usually because the Generals have to reach for it.

3. Regardless of what pattern(s) you utilize to trade, it all comes down to what the stock and market dynamics are at the time of entry. As a day trader, you must manage a trade in a much different manner than a longer term player or even a 2 to 5 day position trader.

The profit opportunity during the day can be explosive, but you must be nimble as the dynamics are always changing. It is now the exception when you get the pure trending days. This is because of the excessive S&P futures related trading.

Closing Remarks

For the past five weeks, I have attempted to provide you with the necessary information to get started in the day trading business. It is too short a time to cover every facet of trading, so I tried to highlight the key ingredients.

- Financial commitment to start the business.
- Knowledge of Stock and Market Dynamics
- Good stock selection process
- Understanding the trading and margin risks.
- Adequate capital to support positions.
- Utilization of simple but effective trend continuation strategies to enter trades.
- Proper communications necessary to trade on a direct access basis.
- "Traders Equation" must be managed.
- Day trading can in no way be successful if you don't keep your losses small, small, small!

Review the 5 Weeks, paper trade, see how you do, then please feel free to e-mail me with any questions.

Keep It Simple, start small, and enter your stop or stop limit orders to exit trades so that your emotions or bad judgement are eliminated. You will take un-needed pressure off yourself as a new trader if you adhere to this discipline.

I wish you all the very best in your trading endeavors, but don't expect it to happen right away. It takes hard work and focus to succeed.

It will be very rewarding for me if you take just one thing from this course that helps you become successful.

You will if you want to.

Kevin Haggerty