The Richard D. Wyckoff Method of Trading in Stocks

Division 2

A COURSE OF INSTRUCTION

IN

TAPE READING AND ACTIVE TRADING

RICHARD D. WYCKOFF, ONE WALL STREET

New York.

TABLE OF CONTENTS

SUMMARY OF THE RICHARD D. WYCKOFF
COURSE OF INSTRUCTION IN TAPE READING AND ACTIVE TRADING.

<u>Introduction.</u> Section 1.	General principles involved in trading to take advantage of the minor fluctuations. Basing judgment on impartial analysis of <u>available facts</u> instead of ill advised <u>impulses.</u> How to <u>interpret tape action</u> and learn to <u>make your own independent decisions</u> with a high degree of accuracy.
<u>Judging the Immediate Trend</u>. Section 2.	How to <u>construct and interpret</u> a Wave Chart. The selection of stocks that reflect <u>leadership</u> and have <u>barometric quality.</u> How to detect the minor price surges and estimate their significance. How to recognize the symptoms of a <u>reversal of the trend.</u>
<u>Using the Wave Chart.</u> Section 3.	How to employ the barometric quality of the Wave Chart in judging the trend of the individual stock wherein you are trading. How to operate in harmony with the Law of Supply and Demand.
<u>Trading Areas.</u> Section 4.	The general significance of a trading area and the exceptional trading opportunities it may offer. How to judge whether a stock in a trading area becomes <u>bullish or bearish.</u> How to decide when to trade close to the danger line with relatively small risk.
<u>Tape Reading Charts.</u> Section 5.	Correlation of <u>price movement,</u> <u>volume and time.</u> How to interpret the fractional price changes and the variations in volume during minor fluctuations. The logical <u>limitations of risk</u> and readjustment of <u>stop orders.</u> How to recognize conditions whereunder the <u>risk may be limited to a small fraction.</u>

<u>Buying and Selling Points.</u>
Section 6.

How to <u>spot the buying and selling levels</u> within a small fraction.

How the market is <u>continually giving information</u> to those who can <u>read the signals.</u>

How to <u>avoid overstaying</u> the market.

How to <u>make up your mind</u> what to do at the turning points.

<u>Judging Strength or Weakness.</u>
Section 7.

Recognizing the evidences of technical strength or weakness.

What constitutes a normal rally or reaction, and why.

How you may <u>develop your judgment</u> so that accumulating symptoms of strength or weakness become records of subconscious memory and resulting <u>decisions are virtually intuitive.</u>

<u>Keep the Risk in Your Favor.</u>
Section 8.

How to <u>limit</u>, <u>reduce</u> and <u>eliminate</u> the risk.

How to <u>insure your profits.</u>

How to develop a trading policy wherein risks are consistent with probable profits.

<u>Trading on Initial Activity.</u>
Section 9.

The general significance of <u>increased activity.</u>

How to interpret changes in the degree of activity.

The <u>importance of volume surges</u> in trading zones and following the formation of an apex.

<u>Tests and Responses.</u>
Section 10.

How the operator tests the technical condition of the market.

How the individual trader may secure, without expense, the benefit of the large operator's tests of the market's strength.

<u>Lines of resistance</u>; <u>how to recognize them</u> and profit accordingly.

How to observe when the market is in an <u>overbought or oversold condition.</u>

How to recognize <u>evidence of manipulation.</u>

The significance of the market's response to news items having the element of surprise.

<u>Best Stocks For Active Trading.</u>
Section 11.

How to select the best stocks for active trading.

Recognition of changing leadership.

The importance of average price range and its relation to floating supply.

The advantage of familiarity with the chief characteristics of leading, active issues.

<u>Use of Stop Orders</u>. Section 12.

<u>How and when</u> to use stop orders.

The <u>scientific location and readjustment</u> of stop orders.

Substitutes for stop orders.

<u>Miscellaneous Vital Points</u>. Section 12.

Judging your efficiency.

Consistent trading policies.

Interpretation of the averages.

Testing your trading ability without monetary risk.

Market orders vs. limited orders.

Limiting the duration of a trade.

How to avoid the dangers of ill-advised advice and tips.

Dangerous pitfalls and how to avoid them.

How to select your broker and judge his efficiency.

<u>Chart Studies</u>.

Tape reading charts of leading active stocks and their interpretation.

Typical trading maneuvers illustrated, with comments, suggestions and explanations.

How to recognize the termination of a reaction, and the subsequent buying signals.

How to recognize the termination of a rally, and the usual indication of impending reaction.

How to use the combination trading chart and wave chart of barometric leaders.

TAPE READING AND ACTIVE TRADING

For the three to five-point moves
with risk limited to
one-half to one-point

The majority of those who follow our Method devote an hour day, more or less, to studying and planning their campaigns. But we have learned that an increasing number wish to trade in the market continuously, either in their brokers' offices or in private offices of their own, equipped with a ticker and other facilities. From these traders we have received many requests for further detailed information on Tape Reading; and as the technique of active trading from the tape is different from that outlined in the first part of our Course, we have prepared the following to meet the requirements mentioned.

This Division of our Course of Instruction, like the First Division, is based on judgment of the technical position: Supply and demand -- support and pressure.

No news, earnings or other corporate or fundamental statistics are considered; we use only those which relate to the factors: Price Movement, Volume and Time.

The active trader who is a Tape Reader is concerned only with the immediate trend of the small moves in the market. This trend can be detected by this Method soon after the opening of the Stock Exchange at ten o'clock daily. It may change from bullish to bearish, or vice versa, and reverse itself from one to three times during each day's session.

We instruct such traders how to follow these trends, changing or reversing their positions as often as the market affords trading opportunities.

In most instances trades are closed out the same day they are made, but if there are strong reasons for carrying any stock overnight, this may be done.

Detailed instructions are given as to the best stocks to choose and the exact time to make commitments, based on methods formulated and successfully employed for over twenty years of trading and advisory work.

Stop orders are placed on every trade, from one-half to one point away from the buying or selling price. These stops must be constantly watched and moved as quickly as the market permits in order to reduce risk, then protect profits.

This form of trading disregards the long trend of the market, as well as the intermediate trends. It takes instant advantage of the technical rallies and reactions that promise to yield a profit in the same stock market session, on either the long or the short side of the market.

* * *

Tape Reading is the art of determining the immediate course or trend of prices from the action of the market as it appears on the tape of the stock ticker. It aims to detect the moves that are likely to occur in the next few minutes or hours; getting in when they begin and getting out when they culminate.

It requires activity and flexibility of mind; readiness to change or reverse one's opinion quickly; also nerve, poise, decision, promptness, courage and absolute independence of judgment.

Its purpose is to derive an average profit from a series of trades. By keeping the risk down to a minimum and constantly striving to reduce it; by clever manipulation of stop orders, a net profit over commissions, taxes and losses can be realized.

All commitments are temporary -- their duration is usually limited to hours. They are intended to take advantage of the small, immediate fluctuations.

With this Method you, as a trader, search for your opportunities and work for your profit <u>here and now</u> -- <u>today</u>. In most cases you will prefer to go home with a clean sheet -- with no commitments on either side of the market. Thus when you start trading next morning your mind is clear for new impressions; your judgment is unbiased by reason of your neutral position.

At each morning's opening you make a swift analysis of the market; sense the trend; decide on the best stock, and if conditions are favorable, you make your commitment. Then you watch the market for a confirmation or contradiction of the correctness of your position. Also for the psychological moment for moving stops, closing trades or crowding stops so close to the market price that you leave the way open for a further profit, or you are closed out on stop at a small fraction from the extreme high or low.

Trading thus, you are afforded several times as many opportunities in these small swings as you would have if you waited for the more important swings of ten to thirty points.

If a trade does not make good at once, you close it out, whether it stands even or at a small loss. You will never trade without a stop, for your risk must be kept down to a minimum. You will never take a big loss. You will never be tied up. You can clean house in an instant. And you can stay away from the ticker as often and as long as you wish.

This form of trading is entirely distinct and different from that described in the other Division of our Method, which aims to secure profits from the ten, twenty and thirty point swings. It meets the requirements of those who wish to trade more or less constantly.

Included in this Division of the Course is a plan for charting the detailed transactions in certain stocks as they appear on the tape, by which you can sense the immediate trend; figure the exact points for placing your stop orders and where to move them to reduce risk when the market goes in your favor. It shows you how to close your trades the same day at the most advantageous moments by watching these Tape Reading Chart indications and getting out near the extreme points in the advances and declines.

Under this Method you might take new positions from one to three times a day, depending upon the activity of the market. It is the nearest approach yet devised, so far as I know, to trading on the floor of the Stock Exchange.

But the most important advantage of a combination of Tape Reading and trading for the longer swings is that it will aid you in increasing your profits in this way: Sections 11 and 12 of the First Division of our Course show how to determine which stocks should move three to five points in a certain direction. You apply the Tape Reading Method in making your trade at the most favorable moment, and the position you then take with a small risk of one-half to one point may later develop into Position 2 on the long side, or Position 4 on the short side, and indicate a run of ten, twenty or thirty points in your favor. By thus trading with a fraction or a point original risk and letting your profit run into the many points indicated in your forecast of the probable distance in points, you will greatly widen your margin of profit. For this reason, these Tape Reading instructions, combined with our longer-swing plan will materially enhance the profit possibilities in both Divisions of the Course.

JUDGING THE IMMEDIATE TREND.

For this purpose we use a Wave Chart, made up of the price of five of the most active leading stocks. The prices of these are added together, and plotted on a sheet of cross section paper, with the time scale at the bottom of the vertical lines, and the price scale at the left, corresponding with the horizontal lines. Specimen sheet follows.

All movements in the market are made up of alternating buying and selling waves. We judge the strength or weakness of the market by the distance in points and fractions recorded by these waves; we combine this distance with the length of time each wave takes to run its course.

In studying the distance and duration of each wave, if the buying waves are longer in duration and travel farther than the selling waves, we get an indication that the immediate trend is upward. If the selling waves exceed the buying waves in time and distance, the immediate trend is downward. Whenever the buying and selling waves seem to offset each other and no material strength or weakness is indicated, the immediate trend is in doubt. Our position should then be neutral.

Select the five leading stocks. At the opening of the market add the prices of their first sales, including the fractions, which should be added in eighths. Put a mark at the price representing their total at the proper place on the price scale and on the 10 o'clock vertical line. Next watch for either an upward or downward swing to exhaust itself. When it seems to stop, put a dot on the chart at the proper time and price level. If the market then reverses its direction this proves that the position of the dot is correct. If it goes on in the same direction, change the dot until the movement again hesitates and shows signs of a reversal.

Then watch the new wave until it seems to come to an end. Place the dot. The market will confirm or contradict your estimate of that turning point. And so on until you are thoroughly familiar with judging and recording the start, duration and finish of each successive wave.

The immediate trend is indicated as soon as one buying and one selling wave have been completed. You then know on which side is the most power -- the buying or the selling side. And all you have to do is to go with that side.

But you must always be on the lookout for a change in this immediate trend. It is likely to change its direction from one to three times in a single session. This is how you detect the change: In an up trend, when the selling waves begin to increase in time and distance, or the buying waves shorten. Either or both will be an indication of a change in the immediate trend. Apply the same reasoning to a down trend. Watch closely for these changes for they tell you when to buy and sell; when to get long or short; when to close your present trade and reverse your position. Further details are on the chart, Page 4-A.

Remember you have nothing to do with the other trends of the market -- either the long trend or the intermediate swings of 10 to 30 points. The latter swings are the basis of the First Division of this Course in Stock Market Science and Technique. Trading for such swings is an entirely different proposition, requiring less time and attention, but having as its objective larger profits - - 10, 20 or 30 points - - and using 2 or 3 point stops. More detailed instructions regarding the above Wave Chart will be found in that Division of this Course.

Although the buying or the selling waves may be sufficient on certain days to carry the market in a certain direction until the close, this does not mean that it will continue to do so the next day. And it does not mean that you should carry any trades overnight for this reason. Tomorrow's trend will define itself in the same way. And it is best not to go into tomorrow's session with any stocks on hand unless there is some extraordinary reason in the action of the market. Such a reason would be, for example, a strong development of power near the beginning of what looks like an important bull or bear swing, indicated by increasing activity and volume in a given direction; with scarcely any points of hesitation, or rally, or reaction, as the case may be. In such instances, a long position, for example, might be allowed to run with a frequent raising of stops so that a trade originally made with a half to one point stop might run into several or many points and thus increase the net average of profit on all your trades for the month. Full advantage of such a situation may be taken by those who understand our Method of trading for the larger swings and can forecast the probable number of points certain stocks should move. Once a trade is made on the strength of directions herein, and its price gets well away from the starting point, and indicates, according to the other Division of our Method, that it will probably develop a move of 10 to 30 points, the trader allows his profit to run according to instructions, and large profits should result.

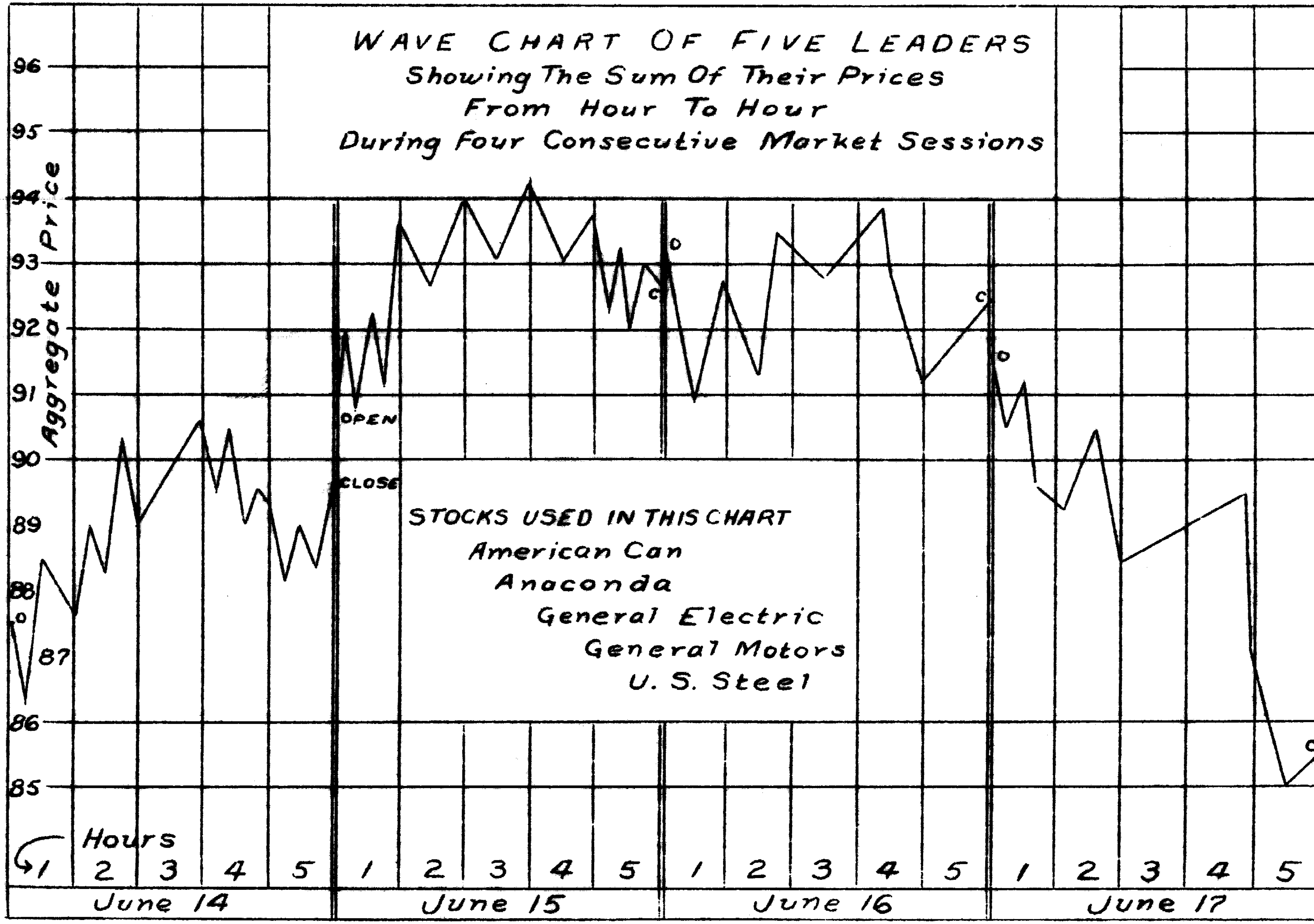
The Wave Chart teaches Tape Reading. After you have used it for a while, you may not need it. Your eye and brain will see and record these happenings that you now are required to plot on the Wave Chart. After you have gone from the first step to the second, you will after a long time begin to develop intuition, by which you will know in an instant when a change in the immediate trend is coming, just as a champion knows how to hit a golf ball without thinking of all the different motions necessary in doing it correctly. But do not abandon the Wave Chart too quickly and do not expect intuition to come until you have had long experience and much practice.

* * *

The five leaders should always be representative of the market. At times when a leading rail has considerable effect it should be included. At other times a utility, like Consolidated Gas, might come to the front; it should take the place of some other leader so long as this condition lasts. Selection of these leaders may be likened to observing the pulling power of a group of five horses: If you were driving such a group and you noticed one horse lagging in the traces and another always tugging ahead of the rest, you would at once decide that the former should be replaced and that the latter is the real leader. Apply this reasoning in keeping your five leaders among the most representative of all the stocks in the market in their ability to influence the rest of the list. Keep weighing these from day to day. Weed out poor ones, which means those that have lost their influence, or have become too inactive to be included.

* * *

The Wave Chart of the previous day should be before you when the market opens so that you get the relation of today's market to that of yesterday.


WAVE CHART OF FIVE LEADERS
Showing The Sum Of Their Prices
From Hour To Hour
During Four Consecutive Market Sessions
Aggregate Price
96
95
94
93
92
91
90
89
88
87
86
85
OPEN
CLOSE
O
C
STOCKS USED IN THIS CHART
American Can
Anaconda
General Electric
General Motors
U. S. Steel
Hours
1 2 3 4 5 1 2 3 4 5 1 2 3 4 5 1 2 3 4 5
June 14
June 15
June 16
June 17

BUYING AND SELLING WAVES

(The Wave Chart-Part II)

In the First Division of our Course of Instruction, Section 4, we presented Part I on the use of the Wave Chart. The material in Part I discusses in somewhat greater detail the instructions set forth in TR Section 2 of the Second Division; therefore, it may be substituted for this last-named Section. Or, if you prefer, you may remove Parts I and II from their present binders and place them in a separate loose-leaf folder. You will then have a complete text book on the theory of the Wave Chart as I have developed and expanded it.

On pages 7 to 9 of Part I, I showed you how to interpret the Wave Chart from the standpoint of price movement, duration of each buying and selling wave, and comparative support or pressure. The following illustration will show in more detail how to apply the additional factors of volume and activity to your analysis of the small waves.

In this illustration (Figure 1), it will be seen that volume and activity both shrink to very small proportions on the little buying and selling waves from 10 o'clock to 1:40 P.M. The day starts with a small rally which is promptly followed by a small dip. Bulls and bears are evidently well matched at this point. After the first dip (Period 2), the bulls try to put prices up, but they fail to attract a following, as shown by the failure of activity to increase. Demand peters out around the 11:00 A.M. top. A small dip in the fourth period brings out very little stock on the downside, however, and this encourages the bulls to try again. Once more they fail to attract a following. Note how the rally in period 5 dies out around the two previous tops. So now, the bears endeavor to break the deadlock by offering stocks down (Period 6) until 1 o'clock. This maneuver meets no better success. Activity fails to increase on the downside, however, and a tentatively bullish signal is given by the evidence of support around the morning low.

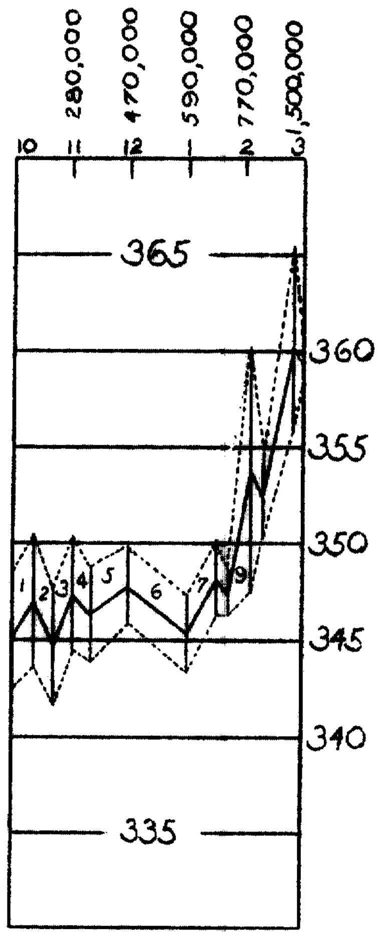


FIG.1

At this point the market has come to a complete standstill. Everything now depends on the ability of one side or the other to rouse a following, either by breaking down the support level or by pushing prices up through the forenoon tops. When the bears fail at 1 o'clock, it is the bulls' turn to try their strength again. This time, demand is a little stronger. Prices rise a little bit above the previous highs and activity increases a trifle as they advance.

If we are trading for the short swings, this is our cue to prepare for action. If activity falls off on the next selling wave, we may expect the bulls to become aggressive. We do not have long to wait. Prices sag a bit in the next fifteen minutes but the activity dies out completely on the dip. This is the cue we have been waiting for. It tells us that the supply which held the bulls back on previous rallies has been absorbed on the small earlier reactions. Therefore, we step in with confidence and buy. We are promptly rewarded by a sharp rise in Period 9.

Any question as to the validity of this upward move is settled by the sharp increase in activity as prices rise through the previous tops. Shortly after 2 o'clock, the bulls rest momentarily because, at this point, the average has risen to a level where stocks encountered supply on the preceding Friday and Saturday. (Not shown.) Evidently this supply has also been disposed of, because activity promptly shrinks on another temporary sell-off. Since there is obviously no pressure yet and few offerings to be taken at this level, we stay long and wait for the bulls to push on again as they try for a higher objective. This they attain just before the close.

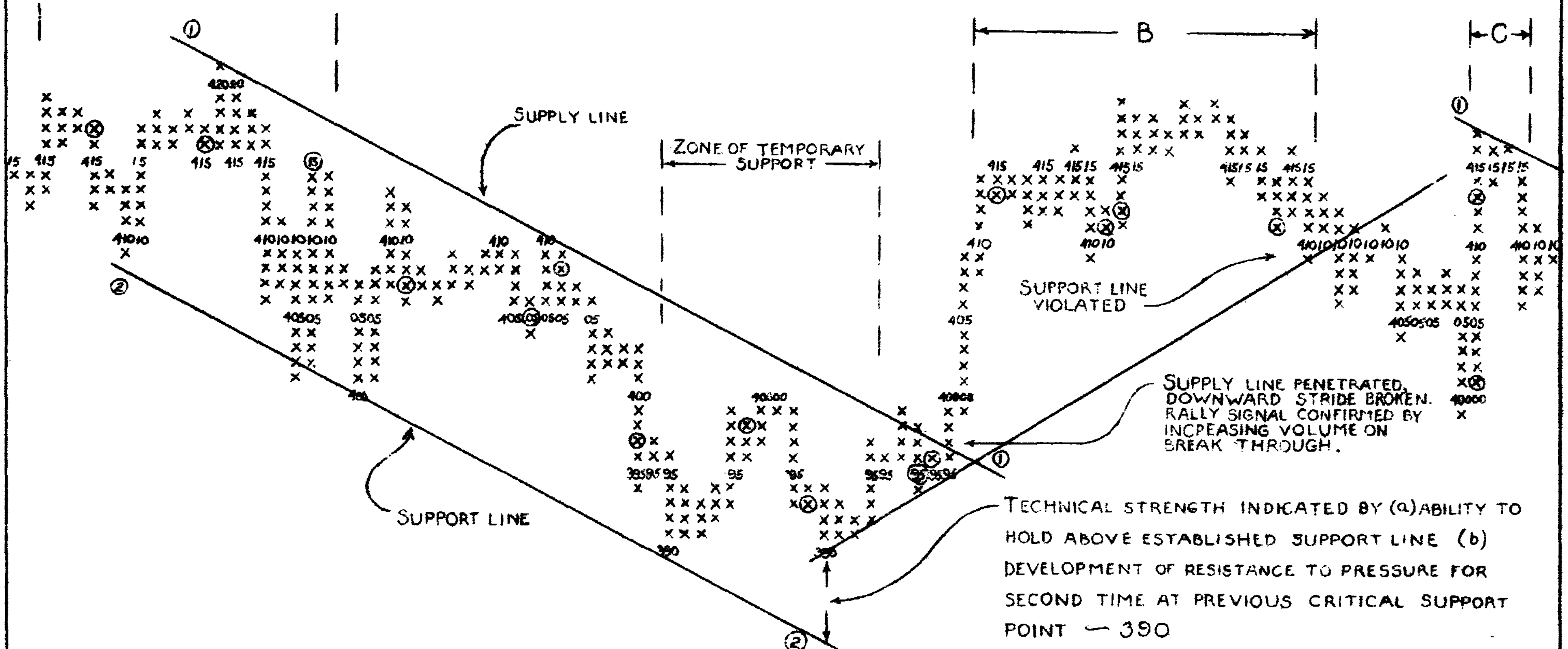
In this and the example on page 7, Part I, we have considered the Wave Chart's usefulness primarily from the standpoint of short-swing trading operations. For your analysis of the intermediate and longer term movements, you will find it helpful to construct a one-point figure chart from the Tape Readings.

This will permit you to bring all of the principles set forth in Sections 10-12-14-16 and 17 of the Main Division of our Course to bear upon your analyses of the Wave Chart. The charts, pages 5 to 8, with explanatory notes, make clear how this is done.

The additional illustrations on pages 9 and 10 show how to mount the daily Wave Charts to form a continuous record so you may compare the action day by day with significant indications developing on the one-point figure chart.

ONE POINT FIGURE CHART OF FIVE SENSITIVE LEADERS

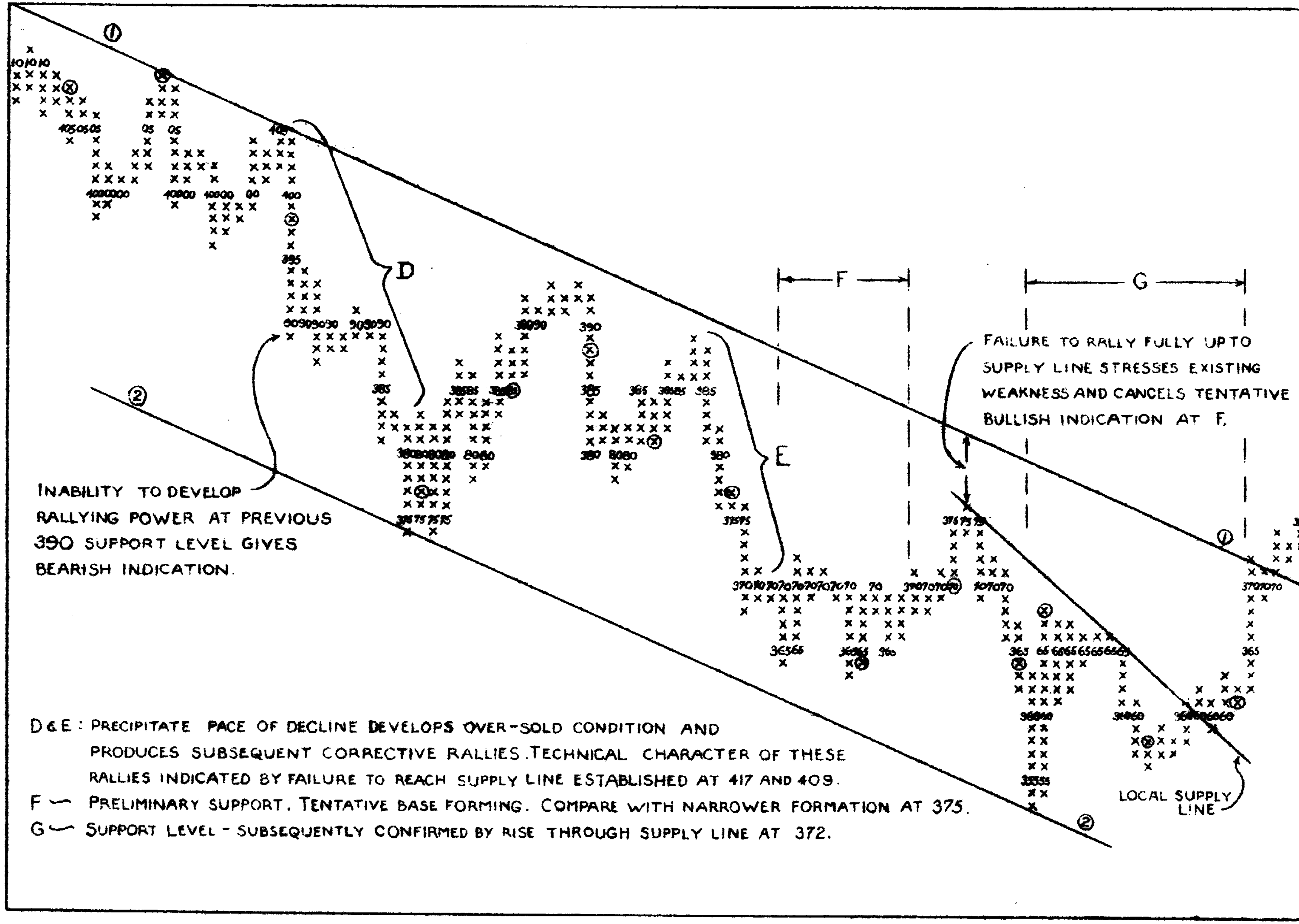
(AUGUST 28 to NOVEMBER 9, 1933)

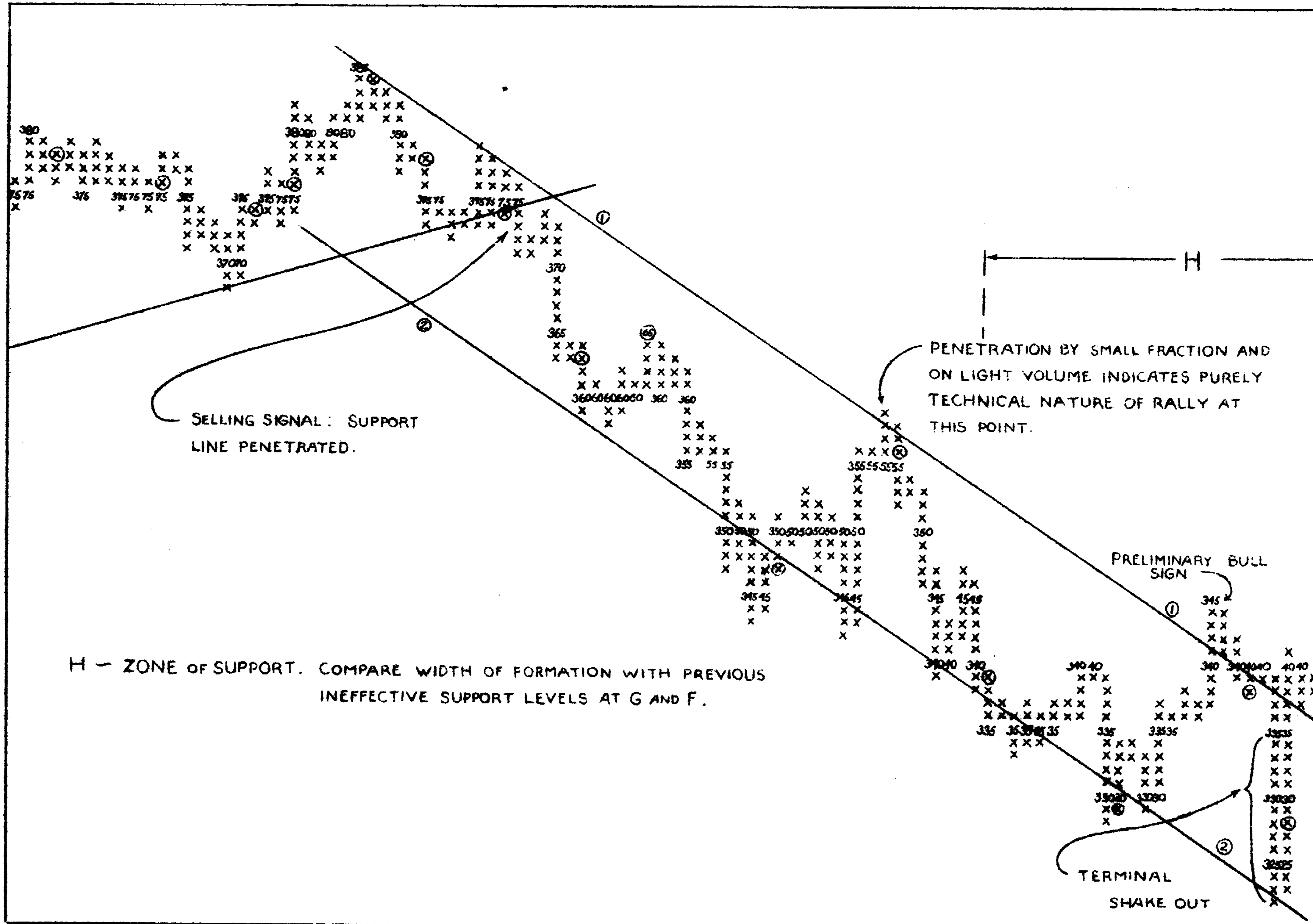


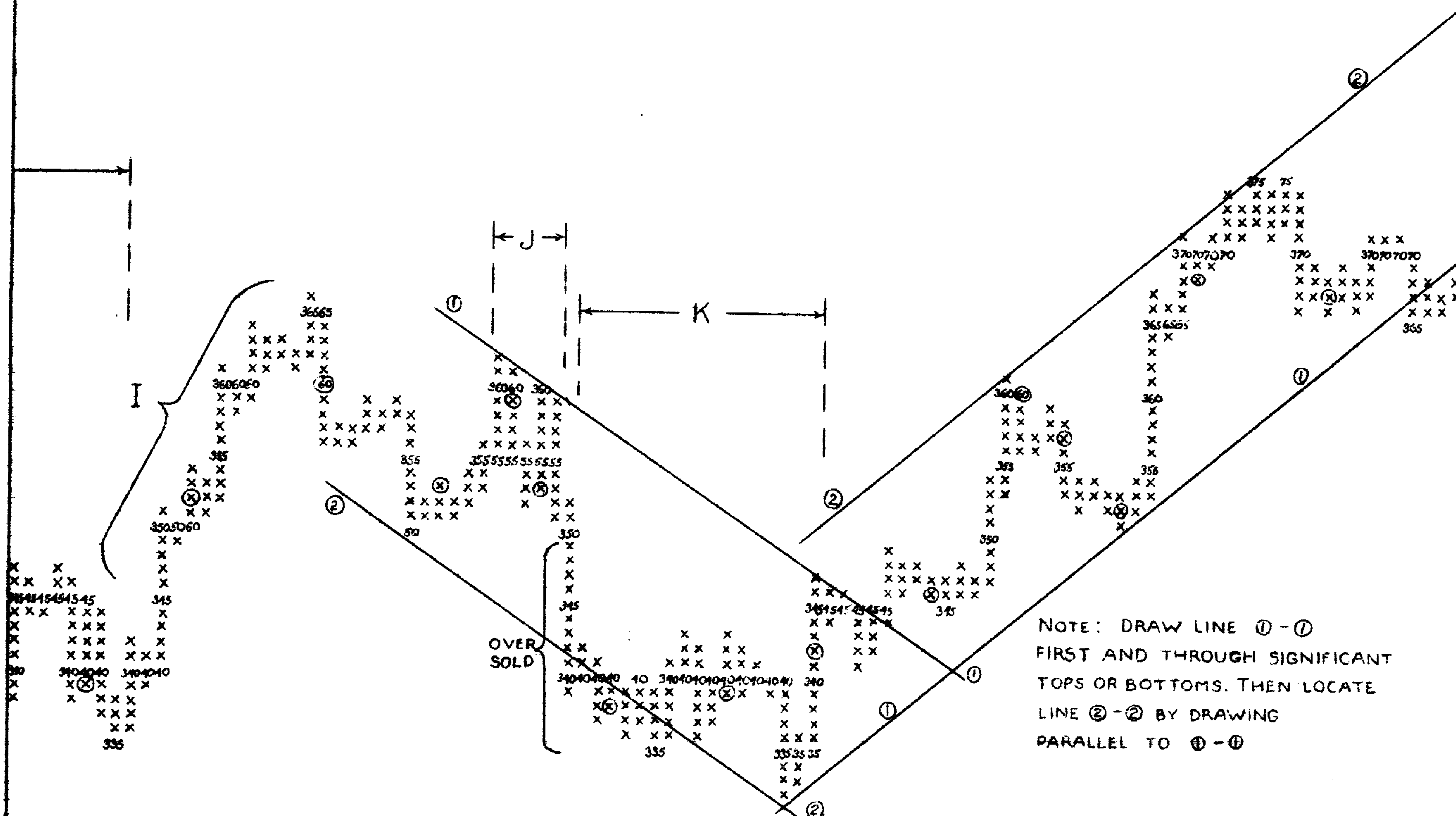
A - ZONE OF SUPPLY: WEAKNESS INDICATED BY INABILITY TO ABSORB OFFERINGS JUST UNDER RANGE OF JULY TOPS; FAILURE TO MAKE PROGRESS ON HEAVY VOLUME; DIMINISHING ACTIVITY ON SUCCESSIVE BUYING WAVES.
(SEE CONTINUOUS LINE CHART ON PAGE 9 FOR DETAIL)

B - ZONE OF SUPPLY: SELLING SIGNALS SET BY INABILITY TO ABSORB OFFERINGS AT PREVIOUS CRITICAL SUPPLY LEVEL.

C - QUICK UPWARD THRUST TO CATCH SHORTS. BRIEF DURATION OF RALLY TO THIRD LOWER TOP EMPHASIZES INCREASING WEAKNESS OF MARKET'S WHOLE POSITION AFTER DISTRIBUTION AT A AND B


D
E
F
G
FAILURE TO RALLY FULLY UP TO SUPPLY LINE STRESSES EXISTING WEAKNESS AND CANCELS TENTATIVE BULLISH INDICATION AT F.
INABILITY TO DEVELOP RALLYING POWER AT PREVIOUS 390 SUPPORT LEVEL GIVES BEARISH INDICATION.
LOCAL SUPPLY LINE
D & E: PRECIPITATE PACE OF DECLINE DEVELOPS OVER-SOLD CONDITION AND PRODUCES SUBSEQUENT CORRECTIVE RALLIES. TECHNICAL CHARACTER OF THESE RALLIES INDICATED BY FAILURE TO REACH SUPPLY LINE ESTABLISHED AT 417 AND 409.
F — PRELIMINARY SUPPORT. TENTATIVE BASE FORMING. COMPARE WITH NARROWER FORMATION AT 375.
G — SUPPORT LEVEL - SUBSEQUENTLY CONFIRMED BY RISE THROUGH SUPPLY LINE AT 372.


SELLING SIGNAL: SUPPORT LINE PENETRATED.
PENETRATION BY SMALL FRACTION AND ON LIGHT VOLUME INDICATES PURELY TECHNICAL NATURE OF RALLY AT THIS POINT.
H
PRELIMINARY BULL SIGN
TERMINAL SHAKE OUT
H — ZONE OF SUPPORT. COMPARE WIDTH OF FORMATION WITH PREVIOUS INEFFECTIVE SUPPORT LEVELS AT G AND F.

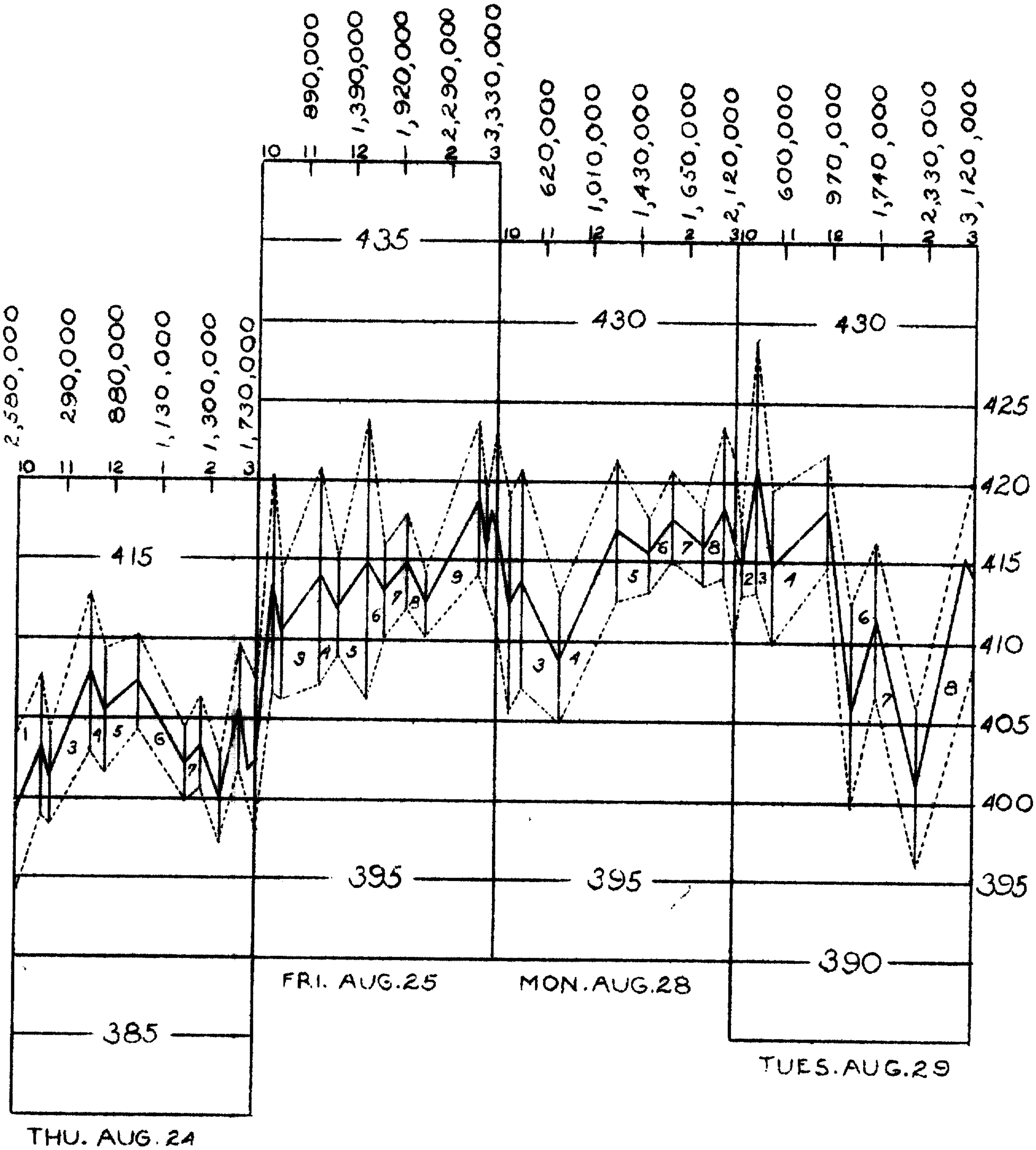


I — STEEP PITCH OF RISE CREATES OVER-BOUGHT CONDITION, INDUCING 50% (NORMAL) TECHNICAL REACTION 365 TO 350

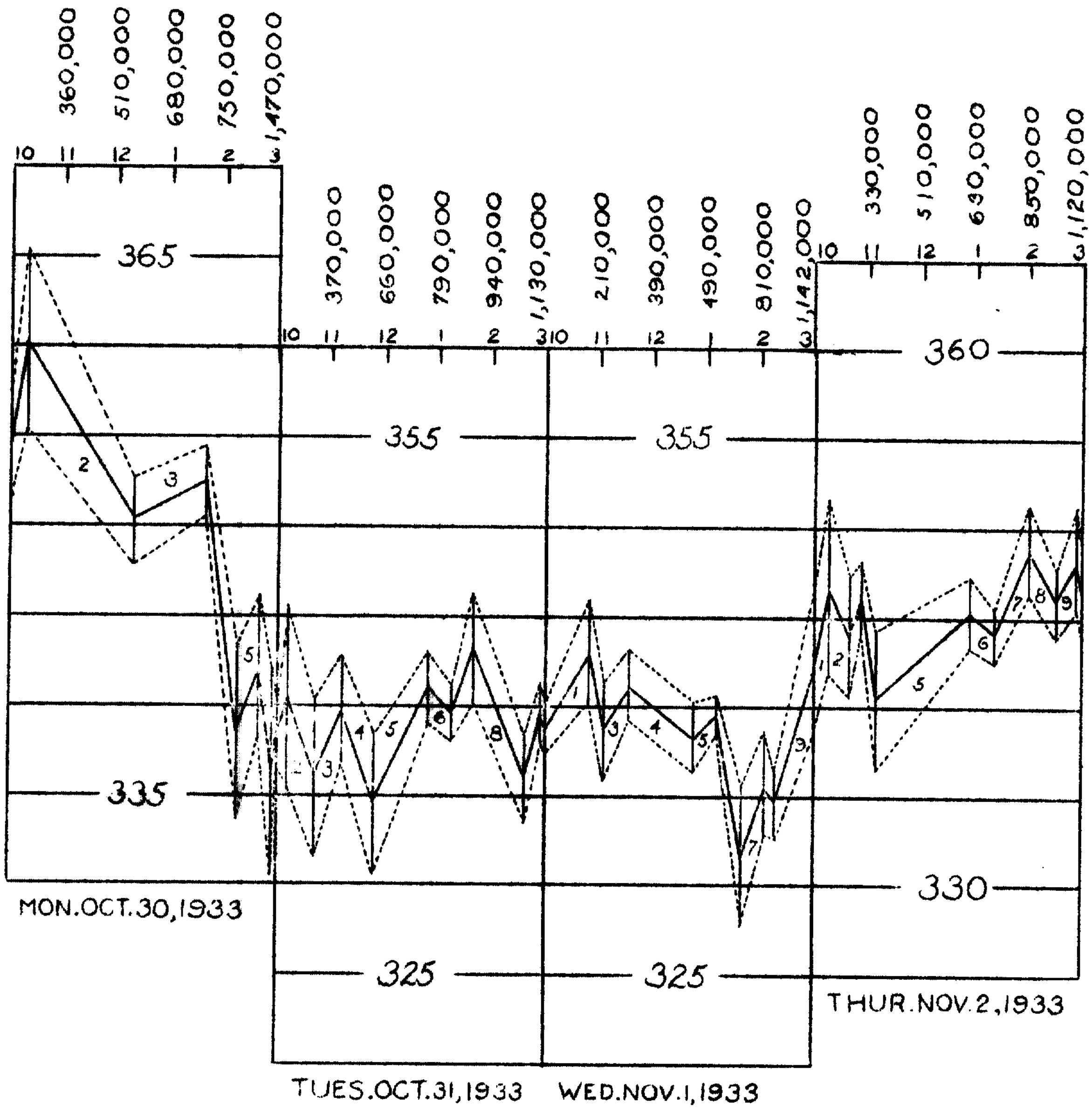
J — INABILITY TO RESUME ADVANCE AFTER NORMAL CORRECTIVE REACTION INDICATES WEAKNESS.

K — SUPPORT APPEARING ABOVE PREVIOUS 330-335 BASE CONSTITUTES BULLISH SIGNAL AND SPREADS ORIGINAL BASE.

(SEE PAGE 10 FOR CONTINUOUS LINE CHART OF ACTION AT THIS POINT.)



Illustrating zone of distribution: inability to absorb supply and development of weakness. (Compare with one point figure chart at A, page 5).



Illustrating zone of support, ability to absorb offerings and development of strength. (Compare with one point figure chart at K, page 8).

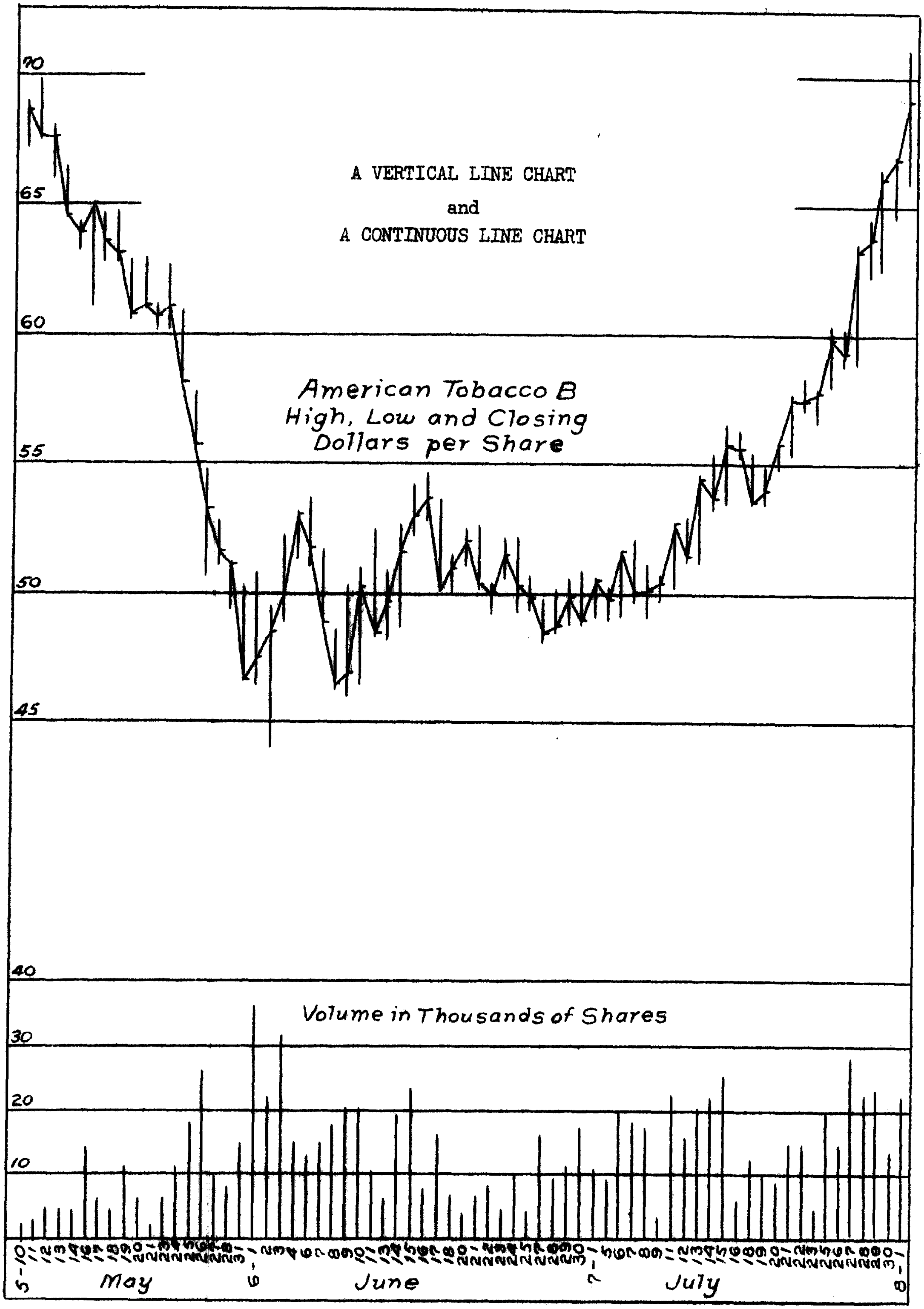
HOW TO LINK THE WAVE CHART WITH THE

STOCK IN WHICH YOU ARE TRADING.

The Wave Chart being based on the action of the five leading active stocks is complete in itself if you wish to trade in all five at once and whenever a turn is indicated. But in the beginning it is best to trade in only one stock.

Observe which of these five leaders appears to follow most closely the swings on the Wave Chart; or perhaps there may be some other stock not included in your five leaders which, by observation and experiment, you find is better for this purpose. This will depend upon the kind of stocks that make up your five leaders. You might, for example, include Auburn, which would give the group a different aspect than if it were not included; or a rail like Union Pacific would again change the texture of your averages.

When you find a stock suited to your purpose, study closely its behavior under all conditions; watch the character of its manipulation. During the study period make different kinds of charts of it, such as a vertical line chart, a continuous line chart, (see Page 1-A) and a combination of figure and volume chart, which will be described in another section. Any and all of these will aid you in becoming acquainted with the peculiar action of that stock so that you can trade in it to better advantage.


A VERTICAL LINE CHART
and
A CONTINUOUS LINE CHART
American Tobacco B
High, Low and Closing
Dollars per Share
70
65
60
55
50
45
40
Volume in Thousands of Shares
30
20
10
May
June
July

Whether for study or actual practice, plot its moves on the Wave Chart. The price scale of this stock should be entered on the right side of the sheet; on the left the price scale of the five leaders.

Now study the action of your one stock in combination with the changes in the immediate trend as shown on the Wave Chart.

You may find that it is changing its trend exactly when the averages change. If this continues, you will know just when to buy and sell it. But you may find it is working exactly the opposite: when the Wave Chart turns upward your stock may begin to get weak. Trade accordingly. Or you may observe that your stock reaches its turning points before or after the five stocks in the averages. You do not care what it does so long as you learn its habits and turn them into profits.

Now that you have the idea, it depends on the amount of study and practice you put into it. What you see on the Wave Chart is the working out of the law of Supply and Demand. That Chart is a moving picture of a cross section of the market, designed by me for this very purpose -- to help you get profits out of trading from the tape. Make the most of your opportunities.

TRADING AREAS AND HOW TO PROFIT BY THEM.

From observation you know how often stocks get into periods of narrow ranges of 3 to 5 points. These are times of discouragement for most people who are on the wrong side, or who are looking for big profits when the market affords only small profits. There are many short swings to one long one. Let us see how we can derive profits from the 3 to 5 point moves.

Keep a vertical line chart showing the daily movements of any of the well-known averages, such as Dow-Jones, Standard Statistics, New York Times, New York Herald-Tribune -- whichever is published in your local daily newspaper. Use these to indicate when the market is in a trading area or whether it is moving to another level, upward or downward. You do not care which way it goes, or when; but you need these averages for a broad picture of the market -- as an indication of the various currents and eddies. The currents are the small, intermediate or long trends. The eddies are the trading areas. In streams these are the whirls or the quiet water between rapids.

Your vertical line chart of these averages should also show the volume of the day's trading -- the total sales for the day. This is very important because it aids in forming your judgment of the prevailing trend. Your individual stock chart should also show the volume of the day's trading in that stock, so that you may observe whether this volume increases or decreases on the advances and declines. Increases serve to emphasize the bullishness or bearishness. Decreases warn you of a probable reversal in direction. I could elaborate on this -- write a book, in fact; but there it is in a nutshell. Do not let its brevity disguise its value.

When you see the averages working back and forth over a trading area, you will generally find your individual stock doing the same. Not always, however. All stocks do not move alike, as you know. Your averages may be in a trading zone and other stocks may have small, medium or wide swings without affecting these. Your stock may not be included in the averages; whether it is or not, remember you are trading in <u>your stock</u> and not in the averages.

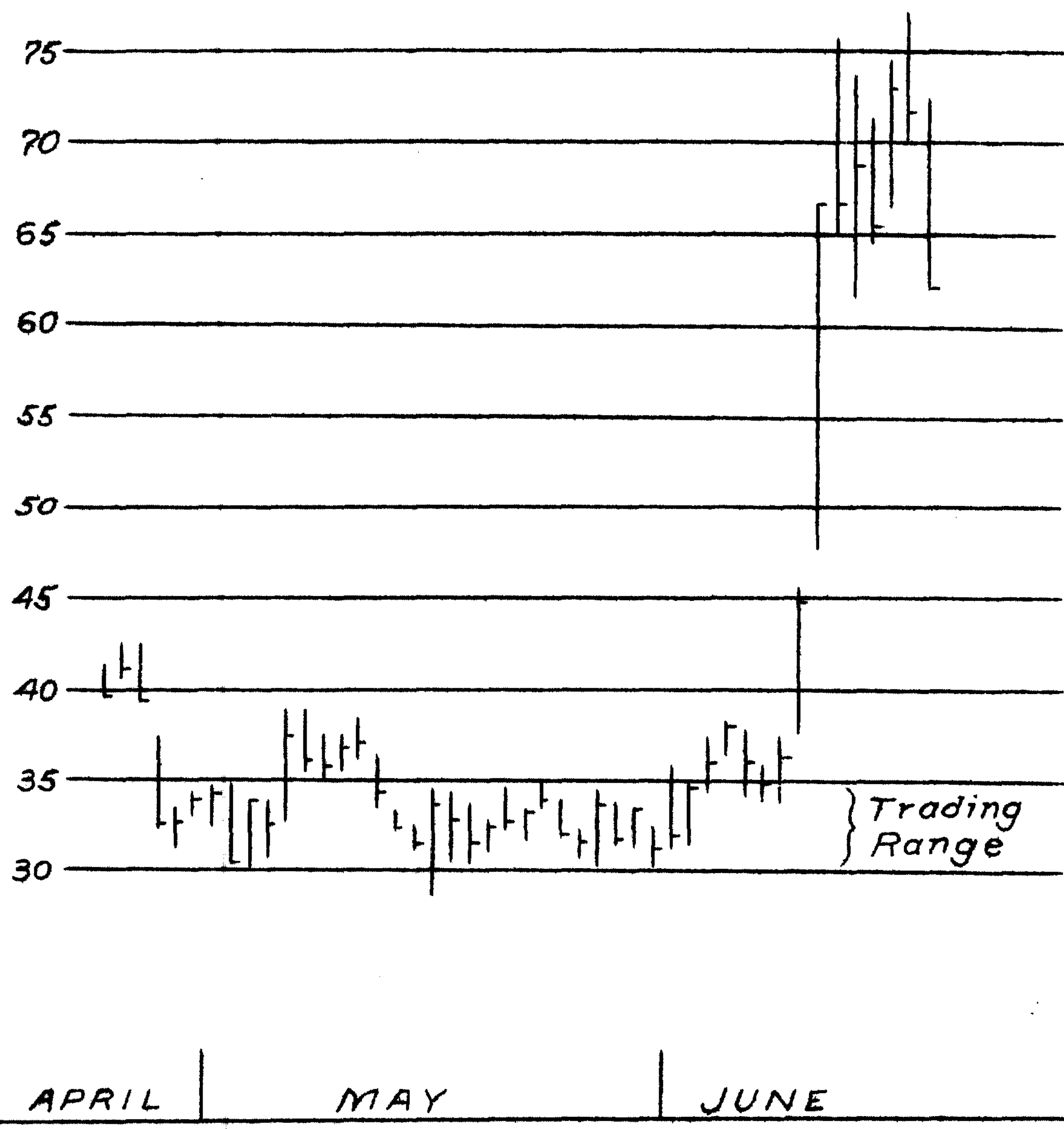
The upper and lower boundaries of these trading swings represent the points (at the tops) where supply overcomes demand and (at the bottoms) where demand exceeds supply. Unless the action of your stock indicates (by methods we shall explain) that it is going out of its present trading range, your purchases should be made around the bottoms of these short swings and your sales, long or short, around the tops. This seems a simple thing, but very few people can do it. That is because they have not had the proper instruction, or they have not studied and practiced it. We will show you how to do this according to our Tape Reading Chart -- the most perfect method that, so far as we know, has ever been devised for those who trade from the tape, in an office, or on the floor of the Stock Exchange. If one is a member of the Exchange and can trade from the tape on the floor, this will be found all the more valuable. It is explained in Section 5 of this Division of the Course.

Meantime consider the position of a single stock with its movements plotted on the Wave Chart, and in connection with its location in its trading area. If it is swinging between 30 and 35 you should give increasing attention to its buying opportunities as it approaches 30, and its selling as it nears 35. This does not mean that you are to buy or sell at or near those points, but that you are to watch out for chances for profit indicated by the action of your stock on the Wave Chart, and on the Tape Reading Chart referred to above. You never know, when a stock approaches the upper or lower levels of a trading range whether, this time, it will go on through; so you do not take a position until you have all the facts assembled, i.e., transferred from the tape to your Wave Chart and your Tape Reading Chart.

Any top or bottom is a small turning point, and even a small one may develop into one that is important.

TRADING AREA
OF AUBURN MOTORS
DURING MAY AND EARLY JUNE, 1932
ILLUSTRATED IN LINE CHART FORM
SHOWING ACCUMULATION
IN PREPARATION FOR AN ADVANCE.

CONFIRMATION OF TREND
IS INDICATED BY THE CORRESPONDING
TAPE READING CHART



THE TAPE READING CHART.

It is twenty-five years since I first began to forecast the coming movements of the market from its own action as it appeared on the tape of the stock ticker. Many memoranda were necessary at the beginning, but as I developed efficiency in this art, I gradually reduced my notes and charts to a minimum, whenever I found simplification possible.

It is one thing to learn to read the tape and to develop therefrom one's judgment and intuition, and another to teach other people how to do it, making everything perfectly clear and practical. I have decided that the easiest way for me to teach and for you to learn Tape Reading is by means of the Tape Reading Chart which is described below.

This Chart combines the three vital factors: Price Movement, Volume and Time in such a way that a trader can see at a glance just what a certain stock is doing; how it acts on the rallies and reactions; the volume of each trade; the progress of the advances and declines; the proportion of the rallies and reactions to previous swings; the lines of supply and demand; the best location for stop orders; the means of deciding when to move stops and how far, etc. This Chart, in fact, combines, on one page, most of the indications required by the Tape Reader.

It can be kept on a sheet of cross section paper. If this be oblong in shape, the two Wave Charts -- of the five leaders and of a single stock -- can be kept on the same sheet, so that a complete picture of the market may be had in combination with the Tape Reading Chart. If several individual stocks are charted on separate sheets in this form, the Wave Chart can be recorded on a sheet of transparent paper, half this size, so that it can be laid over any individual stock chart in order to see how that stock is acting in comparison with the five leaders.

Let us study the construction of this Tape Reading Chart from the specimen sheet which follows. This should be taken out of the binder and laid beside this text in order fully to understand the explanations. The Chart has a price scale at the left. The full figures are in one column and the fractions in the next. The figures recorded in the chart are the total number of shares dealt in at each fractional price. When the price changes, the volume at the new price is filled in at the proper level on the chart. When a price is skipped a cipher is entered at the fraction where there were no sales. Now watch this point very carefully because on it depends your getting the right start in making this kind of a chart; it is simple enough, but if you do not get it clearly into your mind your chart will not be correct. After a sale at a certain price, you enter the next sale in the <u>same column if</u> there is blank space at the proper level, above or below, in that same column. But if that space, above or below, be filled, you make the entry at the next vacant space <u>to the right</u>. This will be perfectly clear when you go over the following detailed explanation.

Your Chart, recording the movements of J. I. Case begins at 10 A. M. with total sales of 900 shares at 40. This 900 might have been made up of several lots; so long as sales continued at that price they were added together and recorded all at once <u>when the price changed.</u> Not until then do you know that there will be no more sales at that price for the moment.

The next sale is 100 at 40-1/4. As there were no sales at 40-1/8, a cipher is entered at the 40-1/8 level, and the figure 1 is entered on the 40-1/4 line. Now you have three figures in the first column -- 9 on the 40 level; 0 on the 1/8 level and 1 on the 1/4 level.

The next sale is 40-1/8, only 100 shares; next 200 at 40. These two figures must go in the second column as the first column is filled on those two levels; next sale 40-1/8 (100); then 200 at 40-3/8 (0 on the 40-1/4 level); then 100 at 1/2; no sales at 5/8; a total of 2100 at 40-3/4; none at 40-7/8; 200 at 41; none at 41-1/8; 200 at 41-1/4; 200 at 41-3/8. All these items were recorded in the third column because the advance continued straight up to 41-3/8 without a single fractional reaction.

The next transaction is 100 at 41, so in the fourth column we must enter 0 on the 41-1/4 and 41-1/8 levels. Next sale 100 at 41-1/8. As the space above the previous sale is already occupied by a cipher we must enter this in the next column, and when the following sale takes place at 41 it goes just below the previous sale -- in the same column. With that explanation as to how to start keeping a chart of this kind, which is really a 1/8-point figure chart, combining volume and price movement, I will proceed with the instructions as to how this chart should be used in actual trading and forecasting.

On January 19, 1932, Case opens at 40. Our position is neutral. We wish to make a trade on either the long or the short side as soon as the stock shows a tendency. Let us assume that the indications on the Wave Chart soon after this opening were bullish, but that we wish to wait until the stock itself has given some sign of a definite tendency. There may be an opening bulge but this may not be its true direction, so we shall wait until the indications are definite enough to promise a worth while swing. We allow 1/2 a point for commission and taxes, so it is best not to go into a trade that does not promise three to five points. If we had the background of the previous day's trading, we would know better just where this stock stands; but starting from scratch, we must wait until the stock tells us what it is probably going to do before we make a commitment.

In learning to read these charts, it is best to cover with a sheet of paper most of the chart, exposing one column at a time by drawing the sheet to the right. In this way there is less tendency to form judgments on the basis of what already appears on the chart. This Method may be followed in a study of all forms of charts, care being taken not to see the general formation in detail before study is begun.

After the opening -- 900 shares at 40 -- the tape shows 100 at 40-1/4; 100 at 1/8; 200 at 40; 100 at 40-1/8; 200 at 40-3/8; 100 at 40-1/2; and a total of 2,100 at 40-3/4. Then 200 at 41; 200 at 41-1/4; 200 at 41-3/8 -- a rise of 1-3/8 from the opening. The reaction recorded by 100 shares selling at 41 marks for the present the boundary line of that trading range of 1-3/8 for the day so far. We do not wish to take a position until the stock clearly indicates that it is going out of that range. To trade within it might not give us enough room to turn around in, and pay 1/2-point for overhead.

Next the tape records 100 at 41-1/8; 100 at 41; 300 at 41-1/8; 300 at 41; 300 at 41-1/8; 100 at 41-1/4; 200 at 41-1/8; 100 at 41-1/4. The trading range has narrowed to 1/4 of a point; we are still in doubt. Next sale is 1000 at 40-3/4 -- a sign of weakness, because there were no sales between 41-1/4 and 40-3/4; this indicates a thin market. Next 900 at 40-5/8; 800 at 40-1/2; 500 at 40-3/8; 300 at 40-1/4. These sales total 3500 shares, all taken within the range of 40-3/4 down to 40-1/4. Here is some strength, but it may mean only temporary support. The chart must tell us what the insiders are trying to do with their stock. Are they supporting it because they want to sell at higher prices, or do they really want to acquire a lot of the stock? They take 900 at 40-1/2, making 4400 around that level; then 300 at 40-5/8; 300 at 40-7/8; and 1000 at 41. That is 6,000 shares on the way down to 40-1/4 and up to 41. That does not look like buying for the sake of accumulation. If they really wanted this stock they would not have bid up for it; they would have put it down. So here is our indication that the pool is trying to sell and not to buy. We form a tentatively bearish attitude and wait for the market to confirm, cancel or reverse it.

The bidding up proceeds: 400 at 41-1/8; 600 at 41-1/4; 1400 at 41-1/2. Now the price stands at a new high for the day which has the appearance of an artificial bulge made by the pool in order to attract outside buying. It required 8400 shares to be taken in order to advance the stock 1-1/4 points. This is not bullish because of the way they did it; therefore, bearish. Unless this stock goes on upward and its volume increases as it advances, we are looking for a chance to go short.

The tape next records 700 at 41-3/8 and 400 at 41-1/2; then

400 at 41-3/8. So far the rise is checked. The pool or someone is trying to sell, for the tape says 800 at 41-1/4; then 100 at 41 and 400 at 40-7/8. This is a half-way reaction following the bulge from 40-1/4 to 41-1/2. This reaction confirms the checking of the rise and narrows the trading range to 5/8 -- between 40-7/8 and 41-1/2. We should go with the stock when it goes out of that range; that is, we should sell it short on a bulge, endeavoring to get as high a price as possible so as to keep our risk down to a minimum. Remember that we are trading now with a 1/2 to 1 point stop and it would be better to lose opportunities, because there are plenty of them, than to be so eager to trade that we take on a risk larger than the above.

There is a rally of 3/8 on a single 100 shares at 41-1/4. It looks like a mark-up by the specialist, or an odd lot house buying to even up. Another 100 at 41-1/8, then 600 at 41. The stock is heavy. We look for a rally on which to sell. This is confirmed by the next sale 700 at 40-3/4, which is 1/8 under the previous low; then 1000 at 40-7/8; 200 at 41; 100 at 41-1/8 -- decreasing volume on the rally. Here we give an order to sell and we get 41 for it. We put a 1-point stop at 42 (indicated by an S) in the 42 space. 300 shares more are sold at that price, making it 400, followed by 100 at 40-7/8 and 800 at 40-3/4.

The chart now has a slab-sided downward formation, made by several lowering tops. A rally to 41-1/4 occurs on light volume, confirming the previous bearish indication. Someone else tries to sell 300 and gets 41 for it, followed by 100 at 40-7/8. The 1/4 point rally which follows at 41-1/8 is the weakest yet. Then comes 300 at 41; 200 at 40-3/4; 100 at 40-5/8 -- a new fractional low on the down swing since it made 41-1/2. Little demand at the low level. Suddenly the stock is bid up 5/8 and

1300 shares change hands at 41-1/4. It looks artificial, particularly when a quick slump to 40-5/8 follows. Now observe 1/8 point rally to 40-3/4; a return to the 40-5/8 low on 100; another weak rally up to 41 (a lower top); then the real slump begins.

When the stock reaches 40-1/2 we reduce our stop to 41-1/2 -- our risk is only 1/2 of a point now, for overhead.

There is only one rally of 1/8 on 100 shares at 40-3/8. Then a new low at 39-3/4; another rally of 1/8 on 400 shares to 39-7/8; then a new low at 39-1/2. Note that the volume increased on the down side. There were only small lots sold in the upper 40s. More substantial lots were sold around 40 and under. Add the sales at 39-3/4 across the page horizontally and you find they are 4400 shares. But these takings are not sufficient to absorb the supply, as proven by a dip to a new low -- 1100 at 39-3/8. When this occurs we reduce our stop to 40-1/8.

The decline continues another 3/4 point with a total of 2300 at 39, and a low level of 38-5/8, then 200 at 38-3/4; 200 at 38-7/8; 100 at 38-3/4; 600 at 38-5/8; then a 1/4 point rally to 38-7/8. Note that offerings are getting very thin here; that is, the volume around this level is light. When the stock again dips to 38-5/8, we bring our stop down to 39, because we do not want it to rally even 1/8 above the 38-7/8 level without taking our profit. It is getting toward 3 o'clock and we must not let that profit get away from us if we want to go home with a clean sheet. There is a rally to 38-7/8 on 100 shares; then 100 at 38-3/4; 400 at 38-7/8 and 500 at 39. This catches our stop and we have our profit for the day.

Our initial risk was 1 point, or 1-1/2 allowing for overhead.

We were able to reduce that risk to 1/2 point, then reduce it to nothing -- the flat price (meaning the price at which it was sold); then to 40-1/8 which assured a 7/8 gross profit; then to 39, which was 3/8 from the day's low, at which price the trade was closed with a net profit of 1-1/2 points.

There is a little stock for sale on the closing rally but we get no cue from it for the next day's session; in fact, we would rather not carry any impressions home with us as we prefer to have an unbiased opinion when the market opens in the morning.

* * *

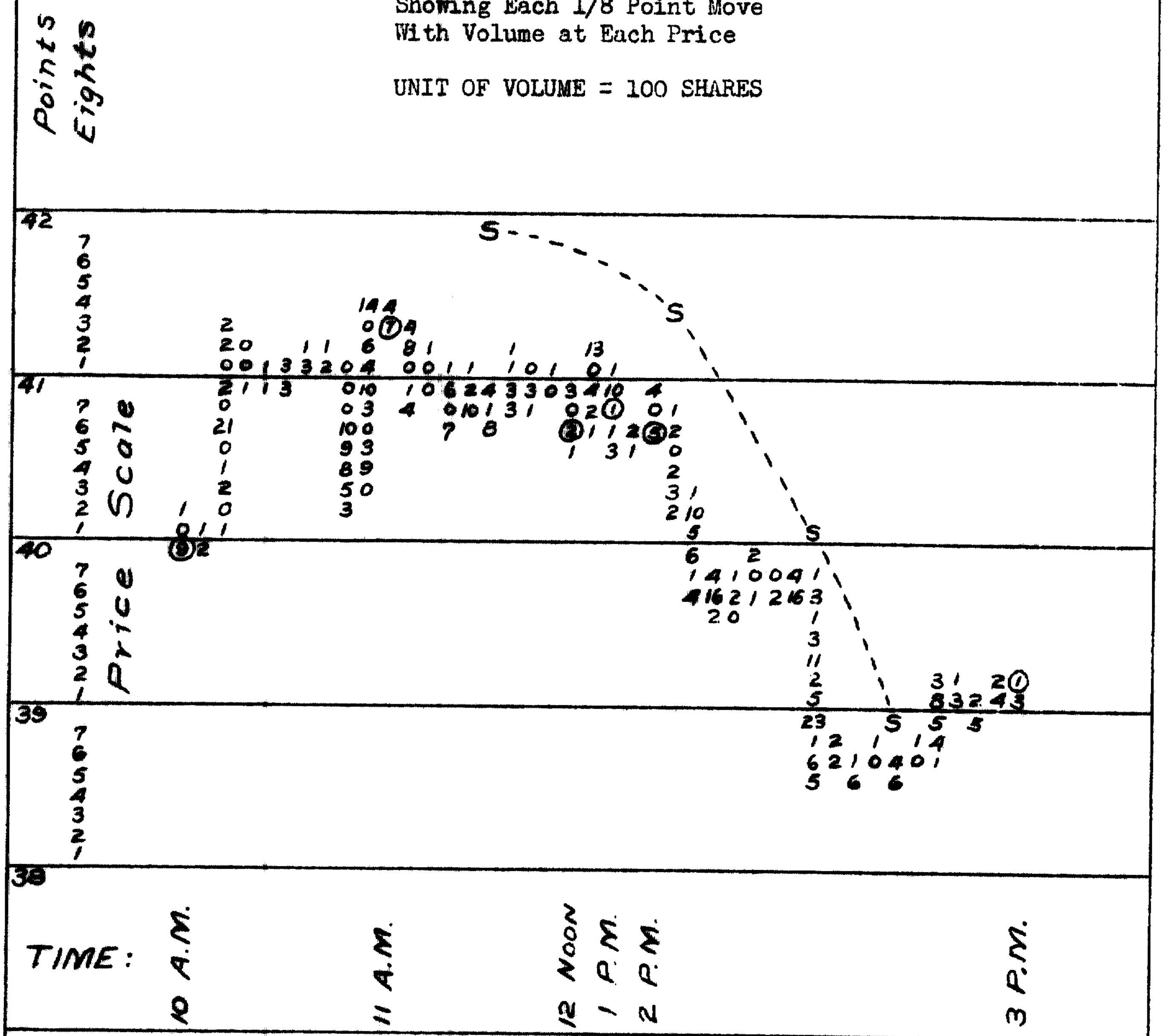
Note: A number of other charts and interpretations of this kind will be found in the Chart Studies, following Section 12. Additional studies will be added later on. Many detailed instructions in Chart Reading are included in Division 1 of this Course.

TAPE READING CHART

OF J. I. CASE JAN. 19, 1932

In Figure Chart Form
Showing Each 1/8 Point Move
With Volume at Each Price

UNIT OF VOLUME = 100 SHARES



S = Level of Stop Order
O = Price at Time Indicated

HOW TO SPOT THE BUYING AND SELLING POINTS WITHIN A SMALL FRACTION.

Numerous examples as to how this should be done are found in the explanations of the Tape Reading Charts. But there are some fine points which may be made a little more clear. One of these is this: We must learn to anticipate the high and low spots in the day's moves by assembling in our minds, and from the chart, all the factors that point to a certain conclusion, and if this conclusion is justified at what we believe to be the right moment, it becomes a command to trade. Thus it will be seen that there are two important steps: making the diagnosis and acting upon it.

The market is continually giving information as to its technical position. It does this through the Wave Chart, which forms your background, and forecasts the immediate trend. It gives further information as to the particular stock in which you are trading if you will plot a Wave Chart of that stock on the same sheet with the Wave Chart of the five leading stocks. In addition to the above, you get all the little details if you will keep the Tape Reading Chart of that stock on the same sheet as the two Wave Charts. With these three and your eye on the tape you are well equipped.

Thus fortified there will be no reason to buy on bulges and sell on weak spots; for, in this form of trading, these are not opportunities to make profits but to make losses. If you sell on weakness with a short stop you increase your chances of having that stop caught.

But if you form a bearish conclusion and wait for a bulge on which to take your position, the chances favor a profit. All such technique must be taken into consideration. You must endeavor in every way to increase the percentage in your favor.

One of the most important ways of doing this is to learn to do your buying on what I call the drive down; that is, during a selling wave and at just about a minute before this wave ends -- while the pressure is on; not when you see it hesitate, but a minute before that, because it takes a minute for your order to get into the crowd and be executed. (If it takes more than that on the average, your broker is slow or he has too much business on hand to give you the right executions.)

Selling on the drive up is just as important. Most of the bulges in a stock are made by pools, specialists, manipulators and floor traders to induce outsiders to buy. If you learn to spot these plays, you have all these interests working for instead of against you.

Take advantage of the public's tendency to buy on bulges and sell on weakness by doing the reverse of this. It is better to get out too soon than to overstay. The public usually overstays.

Watch the Wave Chart for your cue. If you expect to buy, and the five leaders are showing an up trend for the time being, wait for the selling wave. Look back and see how long the previous down wave lasted; judge by that and the action on the tape about how far this down wave will go. Watch the Wave Chart of the individual stock you are trading in, also the Tape Reading Chart for volumes, comparative strength or weakness, and all the other technical points mentioned in chart interpretation. Learn to combine all these various indications into a sound conclusion, and when you have made it, time your stroke; that is, the moment when you give the order, just as you time your stroke in order to hit a golf ball correctly.

Watch for the pauses that mark the end of the buying and selling waves. They indicate that the forces that produced the wave have exhausted themselves. For a moment or two, even in a fairly active market, the ticker is quiet. These are like periods at the end of paragraphs; a new phase of the tape's story usually follows.

When a stock hesitates it notifies you that it has lost its momentum in the direction in which it has been travelling. You should then quickly make up your mind whether it is advisable to buy or sell or move your stop order. Any halt may be the final turning point in that move. If you have studied the First Division of this Course and know how to judge the distance which a stock should move, you are well fortified; you can more easily distinguish the halting places from the probable turning points. There are more halting places than turning points. The periods of hesitation usually indicate a reversal of temporary trend. They also often mark the beginning of a new trading area.

Every move starts at the end of a previous move. If there are indications that the coming move will be important, take advantage of it. If there are no such indications, let it pass.

Always be expecting a change. Be constantly on your guard and ready to close your trade at the first sign of danger. (See illustrations in the Tape Reading Charts.)

Even when you have moved your stop close to the market price for your stock, try to do better by selling on a strong spot or buying on weakness if you really desire to close your trade.

When an upward or downward move is losing some of its force it will be indicated by a shortening of the upward or downward thrusts as shown on the Tape Reading Chart.

Never reach for a stock except in some cases where you are pyramiding and have a substantial profit on paper. Even at such times there is frequently an opportunity to buy on a reaction after a break through on the up side, or a rally following a break through on the down side.

JUDGING STRENGTH OR WEAKNESS BY THE HALF WAY POINTS.

We do not subscribe to the theory that action and reaction are equal in the stock market because we have rarely found it to work out in a practical way. Even if it were true in the stock market, we do not see how one could make any money thereby. But there is advantage to be gained by watching the half-way points on rallies and reactions as a basis for judging strength or weakness.

When a stock advances two points and then reacts one point, it may be called a normal reaction; but if it reacts less than a point, it gives us an indication of strength. If it reacts more than a point, there is an indication of weakness. Used in this way, with the half-way point as a sort of measuring stick, we can really derive an advantage. This is proven by the numerous examples explained in the text accompanying our Tape Reading Charts.

Other signs which may be included under this head are those extreme cases where, after a movement of say three points in a certain direction, a reverse movement takes place to the extent of all or nearly all of the preceding move. A stock advances because the buying power is greater than the selling power; but if it does not hold this advance: if it immediately reverses and loses all or most of what it has gained, this tells us that someone at once took advantage of the strength and sold the stock back to its starting point by offering more shares than the buyers were willing to accept.

The same illustration may be applied to a raid or drive down of say three points more or less, followed by a recovery of practically the same amount. This is a sign of strength because the rebound showed that there was more strength than weakness. This sign is more bullish than bearish because the sellers, having spent their force, are met and overcome by the buyers, who, at the moment of completion of the recovery, are in a comparatively strong position. They have taken all offerings on the way down and whatever stood in their way on the advance. The floating supply is thus reduced; unless further offerings appear higher up that they are not willing to take, the way is then open for a still further advance.

Study and learn all these technical points. Consider everything that appears on the tape as an evidence of support and lifting power, or pressure and selling power. Continually compare the strength of these forces. Use all the judgment and reasoning power at your command. Endeavor to improve your judgment by constant study and practice. Strive to lift your judgment from commonplace to good; from good to better; from better to excellent.

When your judgment has become excellent through your own efforts remember that you can carry it to a higher point by training your intuition; so that after a while you will get the pulse of the market and the psychological moment for trading down to such a fine point that you can form conclusions without conscious reasoning. You can learn to act on these intuitive conclusions and then go back and check up your reasons in order to find out how good your intuition is becoming.

HOW TO KEEP A PERCENTAGE IN YOUR FAVOR.

This is accomplished chiefly through the limitation, reduction and elimination of risk. That means: (1) You must immediately place a stop order as soon as each new trade is executed. (2) You must move this stop to reduce your risk as soon as the market will permit without endangering the life of your trade. (3) You must further move the stop so as to cover the price at which the trade was made, and (4) you must move your stop still further whenever you have a chance to insure thereby a part or most of your profit. These four steps are vital to this form of trading. Unless you carry them out cold-bloodedly -- without hope or fear -- and persistently and with determination, you will greatly reduce your chances for success.

Based on your intention of trading for the swings of 3 to 5 points that occur in a day's session, or perhaps two or three days in succession, your risk is kept down to a small percentage of your prospective profit by placing stop orders 1/2 to 1 point away; but if you should fail to use these stops in the way indicated, you are positively increasing the percentage of your risk.

At 1/2 point risk and 1/2 point for commissions and other overhead, you can be wrong twice out of three times if you realize on the third trade a profit of three points. Your two losses would be 1 point each, or a total of 2 points, including overhead; the third trade would carry an overhead of 1/2 point, making 2-1/2. Hence your net profit would be 1/2 point on the three trades.

On a theoretical 1 point risk with a 5 point objective, if you are wrong twice for 1 point each time, that would be 2 points lost. If your profit on the third trade were 5 points, you would have to deduct the two losses (2 points) and the overhead on three trades, which would total 1-1/2 points, making 3-1/2 points debit and 5 points credit; a net of 1-1/2 points on the three trades; or an average of 1/2-point on each trade.

We do not claim that you can make cut and dried transactions like this, but we emphasize the point that you must keep your losses plus overhead in such proportion to your profits that you will have a margin to the good. This whole plan for active trading involves buying right and selling right, and letting trades run in your favor until you observe technical indications that they have gone as far as you can reasonably expect on the strength of your diagnosis. Thus many a trade which you start with anticipation of a point or two profit may run into several points and help your average profit for the week or month.

On the other hand, your risk is strictly limited from the start; it is <u>never</u> increased. It is frequently decreased. Many times you can plug a profit with a stop order so that it cannot get away from you. Therein lies your expectation for success. You aim at a larger profit than loss in every trade. You keep a percentage in your favor.

Remember that we have by this method eliminated all guessing; all trading on tips, hopes, hunches, hearsay, news, information, statistics; and that we are trading on the basis of stock market technique which has its roots in the law of supply and demand, the only real fundamental on which a sound method may be based.

TRADING ON INITIAL ACTIVITY.

Deciding upon the stock in which to trade may sometimes be done to advantage by letting the market itself tell you that here is an opportunity.

You watch the tape. You have no commitments. Your Wave Chart of the five leaders is before you, on a sheet of chart paper. You make mental note of the prices that are flowing across the Tape or Translux. You wait for impressions.

Suddenly you notice a certain stock getting active on the up or down side. If it is moving in harmony with the trend of the five leaders, you immediately take a position in it, long or short, with a stop 1/2, 3/4 or 1 point away. Then you go back over the tape and make a Tape Reading Chart of it from the opening or from some reasonable distance back. If the high and low prices are on the quotation board before you, you can mark these on the left side of your chart as a guide to the day's range; then if you have a vertical line chart of that stock in your collection you can see where it stands; whether it is in a narrow trading range, or moving out of it on the up or the down side, heading toward a new level.

Your incentive to trade is due to the fact that this stock which has been idling along in a very narrow range and with small volume, is now becoming active. This activity means that somebody is getting busy in it and you infer that he may be in possession of information likely to influence supply or demand or that its technical position is such that they believe they can move it to another level and realize a profit. You, therefore, hop on that stock and ride along with whoever is engineering the move. Thus you have him working for you. You are taking a ride, so to speak, on a special train chartered and paid for by someone else.

Your Tape Reading Chart will give you all the details. You can judge not only by what he does but by what he does not do, for it must be your first precaution to see that he is not making a false move in the opposite direction toward which he intends to make his play. That is, he may be planning a down swing, so he first bids the stock up a point or two in order to attract a following of buyers to whom he can sell a larger quantity -- either on the way up or beginning at the top and selling it back. If he intends to bull the stock he may drive it down first so as to clean out the stop orders below and secure all the stock he can find around the low level. Hence you must be on your guard with your stop order for it is your only protection against a sudden reversal and a big loss.

If, however, the operator is really bulling the stock (or bearing it, as the case may be) and really goes on with the deal the way he started it, your stop order is safe, so long as you do not get it up too close to the price of the stock so that you are kicked out on a small reaction. Keep your stop at a safe distance — on the bull side below the bottom of the last dip, and on the bear side above the top of the last rally, until the time approaches for closing the trade.

Watch your Tape Reading Chart, and watch the trend of the five leaders to make sure they are not indicating a turning point in the day's trend. If, for example, you are long and the Wave Chart says a reaction is coming, it would be prudent to close out and buy back again when the Wave Chart shows the leaders are exhausting themselves on the down side and that a recovery is in preparation.

Your reason for this is that the operator will probably not continue to buy in face of indications that the market is about to sell off. On the contrary, he will probably do just what I am telling you to do; that is, if he sees the leaders begin to weaken, he will probably give his stock a sudden spurt; then sell out all he can so as to reduce his line and thus provide purchasing power around the low point of the coming dip. You follow his moves closely and when your Tape Reading Chart says he is buying them back, buy yours back.

These points in trading are based on standard practice among expert floor traders, pool managers and other important operators who know the game. If you expect to make money, you must not trade the way the public does; you must not merely buy, sit and hope. You must get in and out at the right moments, trading the way market technicians do.

It must be your constant aim to refine and polish your judgment so that you will be able to keep your mind clear and unbiased and your decisions firm yet flexible. Never become prejudiced in favor of either side of the market, for if you do you will be like a ship that goes too close to shore on high tide and is stranded there.

A good way to prepare for trading opportunities on initial activity is to have at your command a large number of vertical line charts with volumes. This does not mean that you will have to make the daily entries on a large number yourself or through your assistant, for you can subscribe to the Graphic Chart Service* which supplies these at a

*11 Stone Street, New York.

small cost, entered up to date, daily. If you have the assistance, you can keep these up to the minute as they come out on the ticker tape, so that you can instantly look up the position of a stock when it begins to show new activity.

JUDGING THE MARKET BY TESTS AND RESPONSES.

Manipulators are constantly testing the market to see whether it is most responsive on the bull or the bear side. They want to know whether they can get a following in the industrial, rail or utilities group, or in any other group or stock representing a certain industry.

Imagine, if you can, that the whole market is controlled by what we may call the Composite Operator, and that every move is either the result of his operations or of those influenced by him. Suppose this Composite Operator has a long position in most of the leading active stocks; this makes him desirous of advancing prices whenever he can, in order to help his whole position. He is like a general advancing into the enemy's territory. His allies are all the bulls. His enemies are all kinds of bears. His object is to defeat the bears. This he does in varying degree whenever he advances a stock.

Now suppose, at the opening of the market today, this C. O. wants to know whether the temper of the public is bullish or bearish: First he tests out the rails by advancing Union Pacific one or two points. He observes how much response is given, as indicated by advances in other rails. If none of these follows his lead upward; if the other leading rails drag themselves up a fraction and nobody operating in the rails takes the cue from the C. O. and advances others in that group, he decides that he cannot get a following in that group for the time being.

Next he tests out Steel, Telephone or Can in the same way. He gets some following in Can, a little in Telephone and nothing much in Steel. Then he tries out the utility group and gets a little more encouragement on the bull side.

From this series of tests he now knows that he can best advance the market by bulling Can. He feels out the other stocks that sometimes respond to the leadership of Can so as to get help or at least support from other sections of the market. He finds a little more response in other industrials and when he has these sized up he goes ahead and bulls the ones that show the best response -- that seem most to influence the rest of the list.

Observe that he follows the line of least resistance. He avoids bulling the rails because he would there have to play a lone hand. He does not want to take big blocks of stocks which stand in his way; someone else can do that. He advances the ones that are easiest to put up while requiring the smallest purchases on his part. After a while the small bulges which he has produced in his testing operations, followed by the more active bidding up of a larger number of stocks, encourage floor traders and the public to get in on the bull side. An increasing number of stocks advance on expanding volume and a bull swing of substantial proportions is under way.

The C. O. further encourages this bullishness by helping along wherever he can. If he sees certain stocks or groups lagging, he will send a broker into those crowds to bid them up. If weakness breaks out anywhere, he will give support. As a good general he is always endeavoring to hold his lines against attack and to advance his front lines (tops) as far as he can.

Suppose the bull swing has now been running for several days and after sizing up the situation by a series of tests, he finds that the buying power has temporarily become somewhat exhausted; that is, most of the people who could be influenced to go in and buy have done so; they cannot spend that same money twice and there is a scarcity of other buyers to take their places. Demand has shrunk.

He now supplies whatever the market will take; he sells all he can around the top of the swing and on the way down. If the rise in the averages has amounted to 10 points, he may keep on selling until it has declined 6 points; then he may begin to buy back what he has sold -- not by bidding up these stocks but taking them as they are offered. Out of 1,000 shares offered at a certain price he may take 600 or 700 leaving 300 still offered and the market unchanged. His reaccumulation is not apparent. The market is still heavy although he is buying back on the reaction.

After a while he absorbs most of the floating supply at a level about half way back from the top. The selling power is now lessening; in fact, he is unable to buy back all he wants; so he drives several stocks downward to weaken the market so he can complete his purchases on the reaction. These drives are also his tests. While these stocks are weak, others advance a little as a result of his raising buying limits. Thus the averages are scarcely altered. People who are bearish point to the few weak stocks and decide that the market is going much lower. They make some ventures on the short side. These help the C. O. to buy more. He takes their offerings.

With the bears making no progress and no more stock pressing for sale, the market is now in a position technically known as "sold out" for the time being. All the offerings of those who sold on the way back from the top are now absorbed; hence, for the next five points up -- on the averages -- there is little opposition to an advance. The C. O. therefore adds to his lines, buying as carefully as he can, so as not to advance prices.

After the averages have recovered about 3 points out of the 5 they lost, he has replaced about all the stock he wants and begins a rapid bidding up of prices all around the room. The market advances to the level of the previous top. Here a lot of those who bought at that time and who held through the reaction place selling orders so they can get out even or at a small profit. This makes a lot of activity and narrow swings around the old top and chart observers say: Here is a double top; we should sell short on this. But the C. O. finds that the long selling combined with the short selling is not sufficient to stop the advance of the market. There is a latent buying power that appears to increase on advances. He bids certain stocks up to new highs in order to encourage this outside buying power.

The strength spreads to other issues and the market goes on through the old high for the averages; bears, finding they are wrong, begin to cover; their stops are caught in many cases. Bulls who have been holding back come in and buy. The bull procession widens and deepens -- more buyers, a greater number of stocks dealt in, a larger volume of trading all through the list.

And so the C. O. continues his operations on the bull side -- with the characteristics of the market in its various phases much like one another in principle but differing in detail -- until the bull wave has lasted so long and extended to so many stocks and brought in so many buyers that the C. O. is able not only to unload every last share of his long stocks; but, as his unloading such a large supply overcomes the remaining demand, he also begins to put out a line of shorts all through the list. He keeps on selling until all of the demand at the high level is satisfied. The market is now saturated with stocks and there is no buying power left to lift that tremendous load which would have to be moved in order to advance prices to a new high level.

The C. O. sees this situation and knows that the time is ripe for a break. He bids up several leading high-priced stocks to new high levels, which causes the public to say: The averages are up into a new high. We should buy more.

Meanwhile he has been selling so many other stocks that their prices are sagging under the weight. He keeps on selling, getting out of the ones he bid up, and getting short of them also. Now he is adding every hour to the supply of stocks. The reaction has brought the public through the successive stages of hesitation to caution and then into a state of fear. That is, they fear the market is going down but they hope it will recover enough to let them out. This emotional conflict on the part of the public causes people to hang on and do nothing.

The market goes lower and lower because there are few buyers except occasional shorts covering. Prices are falling of their own weight. Supply is vastly heavier than demand. The C. O. has only to wait to realize a big profit on his shorts, to be added to the great profit he has already gathered on his longs. And with this vast sum at his command he knows that he can buy a tremendous number of stocks at the bottom of the decline, paying greatly reduced prices compared with those at which he sold.

Now I have explained all this so that you will get a clear idea of what is going on under the surface in the stock market. There is no Composite Operator, but the effect of the combined operations of bankers, pools, large operators, floor traders and the public is, when boiled down on the tape, of the same effect as if it were produced by one man's operations. It is important that you observe the market from this standpoint, and that your trading operations are based, not on what you formerly regarded as the market's characteristics but on the fundamental law of supply and demand, which is at the bottom of every move that is made in every stock in the market at all times. This law is working and will continue to work always and forever. There can be no getting away from it. It does not matter whether the buying and the selling, or both, are genuine or artificial; that is, manipulative; designed for a purpose.

Study and apply this law in the way outlined here, by means of the Wave Chart which shows the comparative strength of the Supply and the Demand; by the Tape Reading Charts which are a microscopic reproduction of the same law's operations; and from the action of the market as it appears on the tape of the Stock Ticker. All these can be turned to your advantage if you will follow the method explained in this Course, constantly studying and practicing it so that you will become highly efficient in due time.

* * *

The market is also continually being tested by the various news items and developments affecting single stocks, groups representing industries, the financial or business situation, etc. A test of the strength or weakness of any stock, or any kind of a market, is frequently afforded by these. For example, there were rumors in June, 1932, that both Allied Chemical and American Can would pass their dividends. Both stocks were heavy. Allied Chemical made a low of 43-5/8 an hour or so before the dividend was announced, and when the report came that the regular dividend had been declared, there was a half-hearted rally to 47, a good part of which was quickly lost. This afforded a test of the temper of the market, which was bearish. Bullish news had only a momentary effect on this stock and little or none on the rest of the list. The tape reader's cue would have been to sell either this stock, or others that responded poorly while the strength still appeared in Allied Chemical.

One more word about these tests: No matter who makes them -- the Composite Man, a pool manager, large operator, or a big floor trader, the result of the tests show immediately on the tape. You, sitting at the ticker, can observe at once whether these tests bring a bullish or bearish response; and you are just as free to act upon them as if you had made them yourself. Therefore, never fail to observe these and other details in Tape Reading. You can never tell what they may lead to, or signify. I have derived some large profits from tape indications which most people overlooked. You can do the same when you learn to be highly observant.

THE BEST STOCKS FOR ACTIVE TRADING.

For this purpose there are two chief requirements: (1) Wide daily swings; (2) A close market -- that enables a trader to get in and out close to the last sale. A third and less important advantage is in a large volume of shares listed in a stock; this is sort of a guarantee that when activity begins a large number of investors and traders will participate in the campaign and thus aid in maintaining a close market.

Wide daily swings are vital, for without them there is little chance to buy and sell, pay overhead and realize a profit. A stock with a daily average swing of only a point would be of no use for our purpose, for in order to realize a half point net profit we would have to buy at the bottom eighth, sell at the top eighth and deduct a half point for commissions, etc. Such stocks should, therefore, be avoided. As the daily swings widen, a stock becomes more attractive as a trading medium.

A close market in a stock is greatly aided by its activity because this attracts a large number of traders in the offices and on the floor; competition is keen; floor traders try to get their bids and offers ahead of the rest of the crowd so as to benefit by fractional moves. All this keeps the market very close to the last sale. By "market" I mean the combined bid and asked price at the moment. The last sale is not the market; that is market history.

Most of the principal daily papers throughout the country carry in their Monday editions a complete list of transactions for the previous week. Such a table shows quickly which stock had the widest swings and the greatest volume of trading: These were the leaders for the previous week. This sheet can be preserved as your weekly record and the five or ten leaders marked with a black or colored pencil.

Leadership is constantly changing. Past records are no guarantee for the future. It is best to take off a list of the leaders each week in order to have them before you for the coming week but this is only your background. The tape will constantly tell you which stocks are affording the best trading opportunities. Of course there are many stocks outside the leaders which have close markets. Watch for these.

Below is a tabulation of the average daily range (difference between high and low) of five leading active stocks having close markets during four months in 1932:

	Am. Tel.	Al. Chem.	Am. Can	Con. Gas	Steel
March	3	2-5/8	2	1-3/4	1-3/4
April	2-3/4	3	2-3/8	2	1-1/2
May	2-1/4	2-3/8	1-7/8	1-7/8	1-3/8
June	2-7/8	2-5/8	2-1/8	2-1/8	1-5/8
4 Mos. Average	2-3/4	2-5/8	2-1/8	1-7/8	1-1/2

The daily range of these stocks sometimes amounted to from 4 to 7 points, which made trading operations on those days more profitable if a trader were on the right side. The above average should not be considered an indication of the future, but just a comparison.

During this period there were many days on which the most active of these, Telephone, quieted down to a point and a small fraction. The same is true of the other stocks; some at times were down to less than a point between high and low for the day. But on the average these five gave plenty of activity -- enough to enable traders to get in and out, often more than once on the same day, with a profit above overhead.

Auburn has not been included in this group because it is in a class by itself. At times it has a fairly close market -- in its periods of preparation for important moves, or in its resting spells. But one never can tell when the next sale is going to be 1/2, 1, 2, 3 or 5 points away from the last sale. It has the reputation of being a dangerous stock to trade in. I consider it no more dangerous than any other if you understand its peculiarities and regulate your trading to fit them. The stock merely requires a different technique from the other leaders. Everyone is not qualified to trade in it. We cannot advise anyone to do so without much practice on paper. He will thus become accustomed to the erratic changes in this stock. These are due to its small capitaliation and extremely limited floating supply. Those who are manipulating it "snap the market whip" frequently -- greatly to the consternation of those who are endeavoring to grab profits out of its gyrations.

* * *

The following table indicates that 66% of the total uninterrupted swings were 1 and 2 points only. The swings of 3, 4 and 5 points amounted to 28% of the total -- a very fair proportion; nearly one-third, in fact. This percentage may seem somewhat increased by reason of the wide swings in Auburn, but, without the latter, it is 27%. Nearly one swing out of three in those running from 1 to 10 points consecutively afforded an opportunity to trade with the assurance that it would go far enough to yield a profit even though this were not accomplished in a single session. In a word, the percentage of 3 to 5 point swings is worth while. After the trader takes a position, if he estimates that any swing should go farther he has only to move his stop and let his profit run.

Number of swings of from 1 to 10 consecutive points, on the full figures, without a 1 point reversal, for about eight weeks in May and June, 1932.

	Number of Points										
Stock	One	Two	Three	Four	Five	Six	Seven	Eight	Nine	Ten	Total Swings
Auburn	169	111	72	43	25	14	11	8	6	4	463
Al. Chem.	66	42	29	12	3	1	1	-	-	-	154
Am. Can	59	25	14	9	4	-	-	-	-	-	111
Am. Tel.	58	36	22	12	5	5	3	2	-	-	143
Con. Gas	47	26	14	9	5	3	1	-	-	-	105
U. S. Steel	25	13	8	6	1	1	-	-	-	-	54
Totals	424	253	159	91	43	24	16	10	6	4	1030
Approx. % of 1 to 10 pt. swings	41	25	15	9	4	2.4	1.6	1	.6	.4	100%

With the exception of Auburn, most of the moves in the five leaders are interrupted after they have run five or six points. This may be only a 1 or 2 point reverse move, and a tabulation of the swings with one such interruption might make another interesting picture.

For those who like to trade in a fast mover Auburn is now (June, 1932) attractive; that is, if their trading faculties are on a hair-trigger, and they can operate without fear of having stops caught from 1 to 5 points away from their stop prices. The table shows that in the

1 to 10 point moves Auburn travelled about nine times as many points as U. S. Steel; four and a half times as many as Can and Con. Gas and three times as many as Telephone and Allied Chemical during the period mentioned. This cannot always be expected, for May and June marked one of its characteristically wide swings.

STOP ORDERS AND OTHER VITAL POINTS.

The use of stop orders: Stop orders should be regarded as insurance against large losses. They should be placed immediately after a trade is made.

We cannot emphasize too strongly the absolute necessity of a stop order in every case, for this whole method of active trading depends more on the limitation of risk and the control of losses than on any other one factor.

Stops can be: (1) placed on the floor; (2) left with the order clerk, or (3) kept in your own hands.

A stop on the floor means that it will be executed the instant a transaction is made by another buyer and seller at your stop price; your stop then becomes a market order.

If you leave a stop with the order clerk in your broker's office, you instruct him to execute it at the market, as soon as he sees a transaction on the ticker at your stop price. This form of stop is a little slower, but, in some cases, may work out more satisfactorily. Try it and see.

If you keep the stop in your own hands it is called a mental stop; that is, you decide you will give the order to the order clerk when the price on the ticker reaches a certain figure. You must determine to carry out your decision without hesitating for a moment; for if you do the chances are you will either hesitate too long or you will move your mental stop farther away from the price at which you made the trade. That is a fundamental error in this form of trading, the whole purpose of which is to limit and reduce the risk. If you make this error you will not be limiting your risk, and you will be increasing it.

At the first sign of danger, your stop should always be brought close or the trade closed out at the market. If the danger passes and you are kicked out, you can always get in again.

Stops should leave room for normal rallies and reactions, so that the trade is open for further possible profits. But if a rally or reaction is more than normal, you should revise your forecast and act accordingly.

Never carry a trade overnight without a stop. You may be delayed or be taken ill the next morning and an adverse market might cause a loss of several points.

An automatic stop is one in which you instruct your broker to move it continually within a certain fraction or number of points from the highest or lowest market price recorded.

Instruct your broker in writing and get his acknowledgment that all of your stops are to be considered good till countermanded.

Under all conditions play safe. Do not see what chances you can take without getting caught, but with what small risk you can trade.

* * *

Judging your efficiency. The objective in this form of trading is to make a long series of trades in uniform number of shares from which we derive profits in excess of losses. We never know when we make a trade how it is going to turn out; we can but use our best judgment and continually try to improve our judgment so that the percentage of net profit increases steadily.

The measuring stick by which good results or bad may be judged is the percentage of profit out of each $100 worth of <u>profits plus losses.</u> That means this: If you make two trades, one with a net loss of $25 and the other with a net profit of $75, your percentage of profit is 75. You add the profit to the loss, making $100, and three-quarters of your total is on the profit side. By this means you judge how you are progressing. Whenever you find your percentage of profit on closed trades running down, or running low, go back to paper trading and study your losses till your judgment improves.

* * *

<u>Trade in uniform lots.</u> All your commitments should be for the same number of shares in each trade, so that the percentage of profit and loss will not be disturbed by trades in larger or smaller amounts than your standard.

When you increase the size of your trades, the same uniformity should be preserved, for the same reason. Results are measured in points. Records will not be accurate unless the lots are the same in all cases.

* * *

<u>Dow-Jones Averages.</u> These are now being posted in many brokerage offices every half hour. The ebb and flow of prices may be recorded in form similar to the Wave Chart in case your attendance at the ticker

is interrupted. The half-hourly prices will not, of course, correspond with the length of the buying and selling waves. Therefore, these averages are not a substitute for the latter; but they have a certain advantage which it would be well to test.

* * *

<u>Trade on paper</u>. When you first begin trading on this Method, do not use real money. Trade on paper until you thoroughly understand it. When you decide to make a paper trade, write it down in your record just as if you were giving an order to your broker and allow a fair price, according to the tape, at which the order should be executed. Give yourself the worst of these transactions, in case of any doubt, so that your record will be conservative and you will not be fooling yourself. Remember it is not important that you make money at first; but it is very important to make a good beginning so that when you once learn how to trade and realize net profits, you can go on and increase the size of your trades without at any time jeopardizing your capital.

* * *

<u>Trade at the market</u>. In nearly every case your orders should be at the market. A limited order should rarely be used.

When it is time to take a position or close a trade, never stand on fractions; get in or out at the market.

* * *

<u>Put a time limit on your trades</u>. There is no reason why you

should stay in a trade which does not act right or goes stale. Your positions are taken on the strength of certain indications and you should give them but a limited time in which to work out. If they do not make good, you should either close them out at the market, or crowd your stops up close to the market price, thus leaving the way open for more profit.

You go long on a certain set of indications shown on the Wave Chart and your Tape Reading Chart; then you wait for these to make good. If the buying waves continue to lengthen and the selling waves shorten, well and good. But if they falter on the up side and your Tape Reading Chart shows supply overcoming demand, get out quickly. Do not sit there and hope. Obey the tape. If it tells you you should be short instead of long, get short on a bulge. This is trading scientifically.

You need no opinion when you are constantly being told what to do and why by the action of the market. And when the tape says the situation is doubtful, close out all trades and sit still in a neutral position. Do nothing until you get your orders from the tape. "When in doubt get out" is an old and a sound rule. It will keep you out of many a losing trade.

* * *

Qualifications. A successful speculator possesses self-reliance, sound judgment, courage, caution and mental flexibility.

You must do your own thinking; form your own conclusions, and so refine your judgment that self-reliance will develop as a natural consequence.

* * *

Never ask advice. The information you will derive from the tape and from your charts is far more valuable than any that you can get from any other source.

It is an old saying: The tape never lies.

Your judgment should be based on sound premises. You have all the facts before you; assemble these and make your diagnosis. Decide what the situation calls for; then use courage in acting upon your decision. Be courageous, and somewhat bold, but with a certain measure of prudence -- alertness and watchfulness combined with caution. Allow for the unforeseen and the incalculable.

Learn to think and act promptly. Your decision becomes a command to trade. Having placed your order, never fear to revise your opinion. You must have flexibility; the mere holding of a certain position is no reason for your holding it; never be bullish or bearish just because you are in a trade.

The market tells you what to do; it continually confirms or cancels its previous indications. It tells you: Get in. Get out. Move your stop. Close out. Stay neutral. Wait for a better chance. All these things the market is continually impressing upon you, and you must get into the frame of mind where you are in reality taking your orders from the action of the market itself -- from the tape.

Your judgment will become poorer from the very time when you decide that you know more about the market than the market is telling you. From that moment your results will be unsatisfactory, for in this trading business the tape is the boss. You must learn to obey its orders, doing exactly what it tells you. When you can accomplish this, you are on the high road to success in your stock trading.

Overhead. It is best to allow half a point for overhead on each trade. The commissions on both the purchase and the sale, the Government and the State tax, together with interest and the invisible eighth make this advisable. Your trading record will show after a while whether this average is fair. This will depend on whether you are carrying trades overnight, or for some days; also the class of stocks you trade in, some carrying lower commission rates than others.

When the price of a stock is in approximate equilibrium, your bid or offer at the market will have a tendency to raise or depress the price an eighth of a point or more. Hence, if your order is to sell, you will receive 1/8 point less than the price of the last trade; and if your order is to buy, you will pay 1/8 point more than the price of the last trade. This variation in price is called the "invisible eighth." When a stock is standing still, the price is, say, 53-1/8 bid, offered at 1/4. If you buy, you usually have to pay the offered price because there is someone ahead of you bidding 1/8. If you hold it say half an hour and the bid and asked are the same, you would have to sell it at 53-1/8. This combination of bid and asked price is the real market. Do not confuse this with the last sale; you cannot trade at the last sale but only on the bid and asked market price. For these reasons, it is best to allow a part of your overhead to cover the invisible 1/8.

* * *

Averaging. If a trade once goes against you, it proves your judgment was wrong when you made it. To average the trade means that you insist upon being more wrong than you were in the first place.

Your profit does not depend on any one trade, but on the net average of a long succession of trades. Never average.

* * *

Capital required. Unless you have a steady income from your business, profession or your investments, it is best to provide in advance and set aside your living expenses so that in trading you will not be concerned with this vital matter and your judgment thereby impaired. It is a mistake to attempt to make money because you need it, or have to have it for some special purpose, for in such cases your judgment is nearly always so biased by your necessity that you do the wrong thing.

It is better to trade on paper until you are in such financial condition that your mind is properly poised. It is better to test your judgment with 10 share lots of actual stocks rather than larger lots if you have to use money required elsewhere. Allow for the possibility of several consecutive losses.

When you find that you have made many paper trades and established a successful record, begin in a small way making actual trades, but, if you continue to make real money on these, do not be misled into increasing the size of your trades too soon. You are building for the future; therefore, make each step with caution, particularly in the matter of increasing the size of your trading.

When you make money, do not put all of your profits into your trading fund. Use only half of them; with the other half pay yourself back your original capital until your trading fund is all velvet. Follow this idea continually so that you will always have a reserve over the money you are using as margin.

* * *

How profits accumulate. If you can realize an average profit of $50 on 100 shares per day, the total will amount to $1,000 in 20 trading days. I mention this in order to show that when you are trading continuously, you do not need to secure very large profits in order to make your efforts pay. But there is no reason why you should come out with such a small average profit as 1/2 per day if you continue to study, practice, train your judgment and develop your intuition. This Method gets away from the big profit idea and teaches you to roll up small net profits until they aggregate a large sum.

The way to increase the average size of your profits will be found in that part of our Course of Instruction which explains how to trade for the 10, 20 and 30 point moves. With that included in your trading knowledge, you can use the present instructions in taking your positions, and, when indications favor, hold those positions for the important swings. Your original risk of 1/2 to 1 point taken on the basis of Tape Reading Chart indications may thus result in profits which are large in proportion to your risk.

When you are able to judge the approximate number of points that a stock should travel in a certain direction, it gives you the courage to go in, pyramid and hold on until that stock makes good, or warns you that it will not. And this one factor of knowing "how far" will do more to increase your average profit than any other.

That part of the Course also gives plans for pyramiding at certain levels and under certain conditions, by which you can derive more net profits out of some moves than the total number of points from high to low.

Where to trade. As soon as you can arrange it, have a little private office of your own where you can install a ticker and a private telephone to your broker's order clerk. It is best not to let your friends know where they can find you so they will not bother you during the day and you can concentrate on the tape in order to get the best results.

If you cannot devote all your time to the tape during market hours, perhaps you can have a young man or woman assistant keep your charts for you so that you can go in at convenient times during the day and find everything up to date. You will find this arrangement very helpful in getting the best results.

If the amount of your trading warrants it, your broker will probably be glad to provide you with a small private office, ticker and telephone. If not, you can make a start in his customers' room, and, as you build up your account you will undoubtedly find it profitable to get into a secluded place where you will not hear the board room gossip and will not be bothered by people who want to give you tips and so-called information. Of course, that sort of thing may not confuse you but it is a handicap to most people.

Keep as many charts as your time will permit, or your assistant can keep for you. The larger the number of charts, the greater the variety you have to select from, and the more opportunities you can take advantage of if you have the necessary working capital. This is particularly advisable when you are trading on paper. Ten charts will give you far more practice and experience than one chart, and one hundred charts ten times more than ten.

* * *

Choice of brokers. Your broker should be able to give you prompt and satisfactory execution of orders, within one or one and a half minutes from the time you place these orders. Executions taking longer than this sometimes result from congested condition of the floor, or on wires or telephones during very active markets when everyone who handles your orders is overcrowded with business. In ordinary markets, however, a minute or so is time enough unless you have sufficient confidence in your broker to let him use his judgment in waiting for fractionally better markets before he trades at the bid or asked price.

Advise your broker just how you are trading. Let him understand your requirements. You trade actively, pay many commissions and are, therefore, worth more to him than several clients who get in and out only occasionally. He should be willing to give you special attention. You can advise him when your orders come through by having the order clerk mention your name when he phones the order to the floor. All these little advantages will add much to your profits in the long run.

* 2 *   *

<u>Study your losses.</u> All of your trades should be based on a line of reasoning which is more or less settled in your mind -- a set of reasons which have been tested and tried by you, so you know as a rule which will work and which will not. When you find results not so good you should study and learn why; perhaps you are experimenting too much with new ideas. If so, go back to the ones which you have proven.

Control your losses and your profits will take care of themselves. Have a space in your Record of Results showing, in each case of losing trades, the cause of that loss.

You may, especially in the beginning, or even after you are well started, find yourself running into a series of losses. Do not let that discourage you. Go back to trading on paper.

Depend on the law of averages and your well-tried practices to yield a profit over losses.

Never be concerned about any one unsatisfactory trade. It is the net result that counts, and after a long series of trades. You will learn more from your losses than from your profits; these tell you what <u>not</u> to do.

* * *

<u>Practice persistently</u>. The more time you devote to stock trading, the more profits you should derive from it. If convenient, keep your charts in a pocket-size book and study them in spare moments. Ask your broker for the tape after it comes off the translux; take this home and study it. It will enable you to review the day's transactions, and to observe small details that you might have missed.

Practice on paper with other stocks than those in which you are trading. Dull markets give ample opportunity for this. Continually absorb all the information you can on this subject. Read all available books for valuable sidelights.

* * *

CHART STUDIES.

American Telephone & Telegraph
At Bottom of Reaction June 2, 1932.

Note: In these examples, we will illustrate what can be done with average judgment, also with excellent judgment. No one can tell just what we would have done, under the circumstances; but by demonstrating what might have been done, we can learn how, and through constant practice increase our efficiency.

This Tape Reading Chart begins about 2:30 P. M. on June 1st, with the stock at 86-3/8 on the downward swing from 91-3/8 on the previous day. The chart shows that there is little support for this stock. Let us assume that we have a short position and carry it overnight. At the close there is a rally of only 1/4 point at 85-1/8.

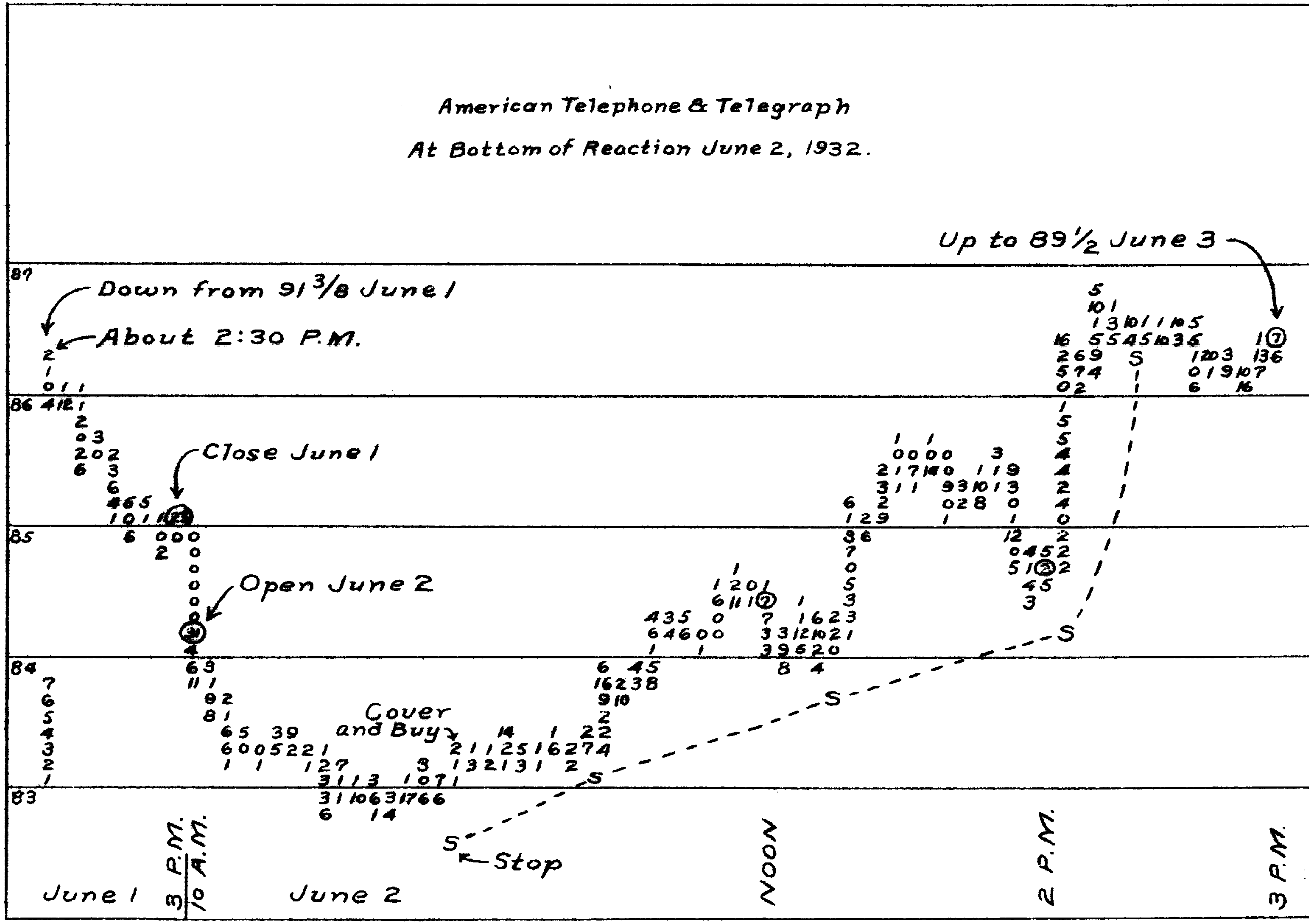
On June 2nd the stock opened with 3100 shares at 84-1/4 -- down 7/8 of a point overnight. There is not so much stock pressing but there still seems to be lack of support. Two rallies of 1/8 point each are the only ones until the price hits 83-1/4; then there are two of 1/4 each and a line indicating slight hesitation at 83-3/8.

Another decline to 82-7/8 and a 3/8 point rally occurs. The trading zone is now confined to the 3/8 between 82-7/8 and 83-1/4. The stock begins to get a little support there. 1000 is taken at 83, then 300.1/8. Two small dips on light volume and 1700.83 100.1/8 600.83 300.1/4 700.1/8 600.83 100.1/8. At and under 83 we find transactions have totalled 6300 shares. The stock has twice refused to go below 83, and the sale at 83-1/4 gave the up signal. Stop on our short stock (if any) should now be brought down to 83-3/8 and a long position taken if the price touches that figure. That means a double buying stop at 83-3/8. The price touches 83-3/8. This covers our short stock and puts us long at that price with a stop 1/4 under the low of 82-7/8; viz., 82-5/8.

Telephone now works in a 1/4 point range in small lots except 1400.83-1/2. The support line is now 83-1/4 and only small lots come in at that. Following 1200.83-1/2, the stock breaks through on the up side and makes 84. We raise our stop to 83-1/8. Sailing is clear to 84-3/4, then a little reaction to 84. Support just above 84 is much stronger than pressure. The selling dries up again and the stock pops up to 85-1/4. Meantime we have raised our stop to 83-3/4.

At 85-3/4 there is little demand and a reaction sets in; a 5/8 dip to 85-1/8, then a rally of 1/2 to a lower top, 85-5/8. This formation above 85 does not indicate any serious decline. A recovery of nearly 3 points calls for about 1-3/8 reaction, but it falls 1/8 short of this and the dip ends at 84-1/2. Pressure on the decline is neither light nor heavy; it is a normal reaction.

The reaction wears itself out. Demand overcomes supply. The stock soon sells above 85 and continues straight up to 86-1/2. This is new high ground; we raise our stop to 84-1/4 and await further developments. The 1600.86-1/2 brings a 3/8 dip to 200.1/8. On the next upward surge the stock only gains 3/4, with 500.86-7/8. The upward thrusts are shortened, indicating another reaction. So we push our stop up to 86-3/8. Adding the sales above that figure we find that 10,000 shares have come into the market here and as we are in the last hour of the trading, we may decide to sell at the market. If we do not, our stop is caught and we have the following result: Bought 83-3/8. Sold 86-3/8. Profit 3 points, less 1/2 point overhead; 2-1/2 points net for the day.


American Telephone & Telegraph
At Bottom of Reaction June 2, 1932.
Up to 89½ June 3
Down from 91 3/8 June 1
About 2:30 P.M.
Close June 1
Open June 2
Cover and Buy
Stop
87
86
85
84
83
June 1
3 P.M.
10 A.M.
June 2
NOON
2 P.M.
3 P.M.

American Telephone & Telegraph
At Top of Rally June 15-16, 1932.

This chart begins at 86-1/4 on the upward swing from 81 on June 9th. Our Wave Chart at the opening gave us an upswing. We do nothing until the clearly defined line of support under the light pressure at 86-5/8 and 3/4 tells us to go long with a stop 1/4 to 1/2 below the bottom of the dip to 86-5/8. If we put our order in when the stock is at or close to its low, we probably would pay 87 for it, and our stop should, therefore, be made 86-3/8 -- a risk of 5/8.

The stock works out of this range on the up side and on a reaction to 87-1/2 meets support amounting to 2500 shares. On the further 1/2 point bulge to 88, observe the increase in supply -- 1400.87-3/4 300.7/8 1700.88. The gain over the previous top at 87-3/4 is only 1/4 point, and the reaction to 87-5/8 is 3/8 with 1000.87-5/8 at the bottom of that dip. A rally of 3/8 to 88; another 1/4 point dip; higher support; then a snap up to 88-1/2 on very light volume with 500 at the top and an immediate recession of 5/8.

The trading zone is now 87-7/8 to 88-1/2. On the last dip 1100 came in at 88-1/4; there was no demand at 1/8 or 88. Weakness. We now push our stop up to 87-5/8 for we are suspicious of the long side, and we decide to sell on the next bulge, or raise our stop further. The next bulge is to 88-1/4. We raise our stop to 1/8 under the last low, which was 88, and when there is another bulge on light volume to 88-3/8, we raise the stop to 88-1/8 and double it; that is, we sell twice as much as we are long. This gives us a short position at 88-1/8. We immediately put a 1/2 point stop on our short which makes the stop 88-5/8. Net profit on long trade, 5/8.

The volume is now very light, and a technical reaction at least is indicated.

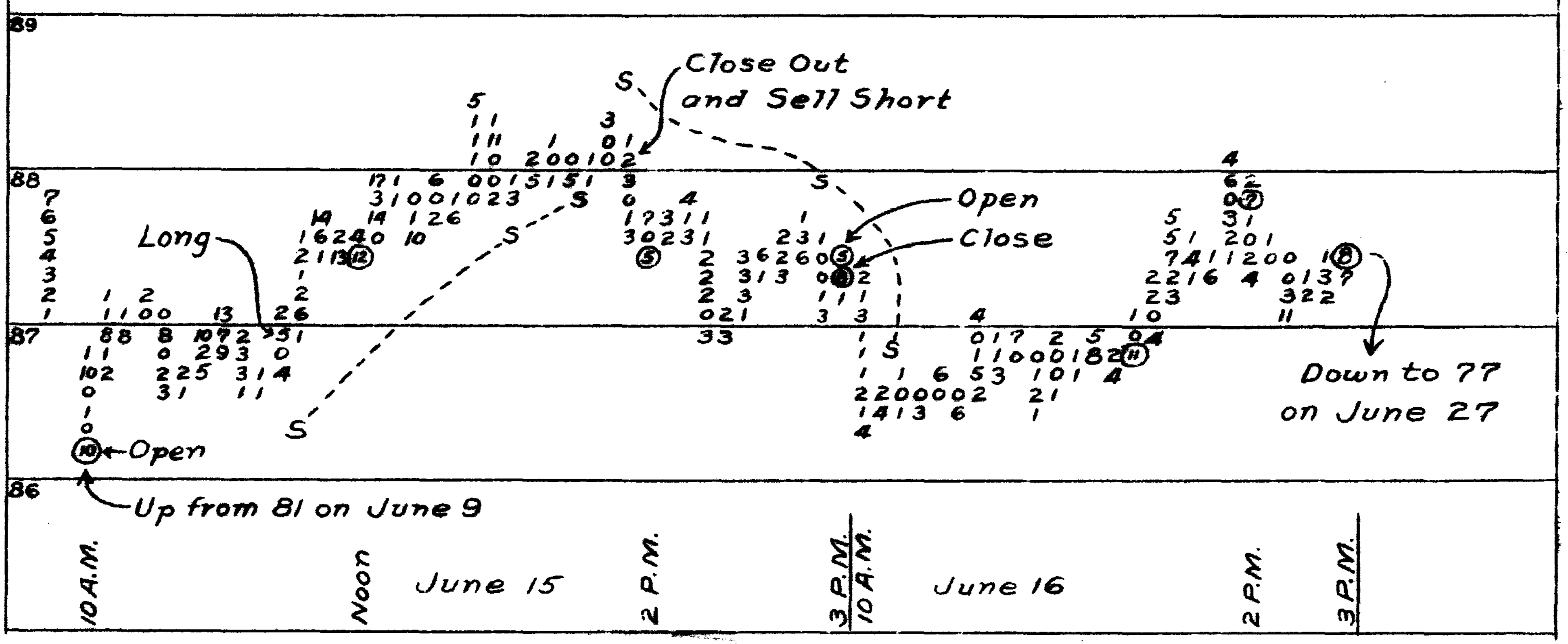
There is a dip to 87-1/2; another to 87. The rallies are fractional at first; then a 3/4 rally from 87 with volume petering out at the top. A 5/8 dip and a 1/4 rally leave the stock at 87-3/8 with 800 shares at the close, and as the indications are bearish, we lower our stop to 88 and carry the trade overnight.

Next day's opening, June 16th, is at 87-1/2 and the stock immediately resumes its decline. The very light volume makes us suspicious of a rally so we tell our broker to cover on a 1/2 point rally from any new low. At 86-1/4 a rally of 3/8 follows; then later extends to 3/4 and catches our stop.

All but 1/8 of this rally is soon lost, but higher support appears -- at first 1/8 above the previous low, then at 3/8 above. Volume is light. It looks like a further rally. We do not go long because the indications are bearish. We merely wish to sidestep more of a rally and perhaps get a new and higher selling point. We wish to see how the stock acts on the next bulge -- whether it has power to go through, well above 88, or if supply will overcome demand again above that figure. Our stop that was caught at 86-7/8 gave us 1-1/4 point gross profit.

Volume increases slightly on this further bulge: 600.88 400.1/8 200.88 700.87-7/8. But it is now 2 PM and with the trading quieting down, it seems unlikely that there will be activity enough to give us a good swing in the next hour. So we stand pat for the day, with 3/4 point net to our credit. We might have covered a little lower on that second morning dip from 87-1/8 to 86-1/2, or pushed our stop down further so as to gain an additional fraction.

American Telephone & Telegraph
At Top of Rally
June 15-16, 1932



Allied Chemical

At Bottom of Reaction June 2, 1932.

This stock has come down from 51, and at 2 P. M., June 1st, it stands at 48. It dips 3/8 below that, and jumps 7/8 point on one sale of 1200.48-1/2. Then some 1/4 point wriggles between 1/2 and 3/4, a dip to 600.48-1/8, and a rally on small lots to 48-7/8 where it closes.

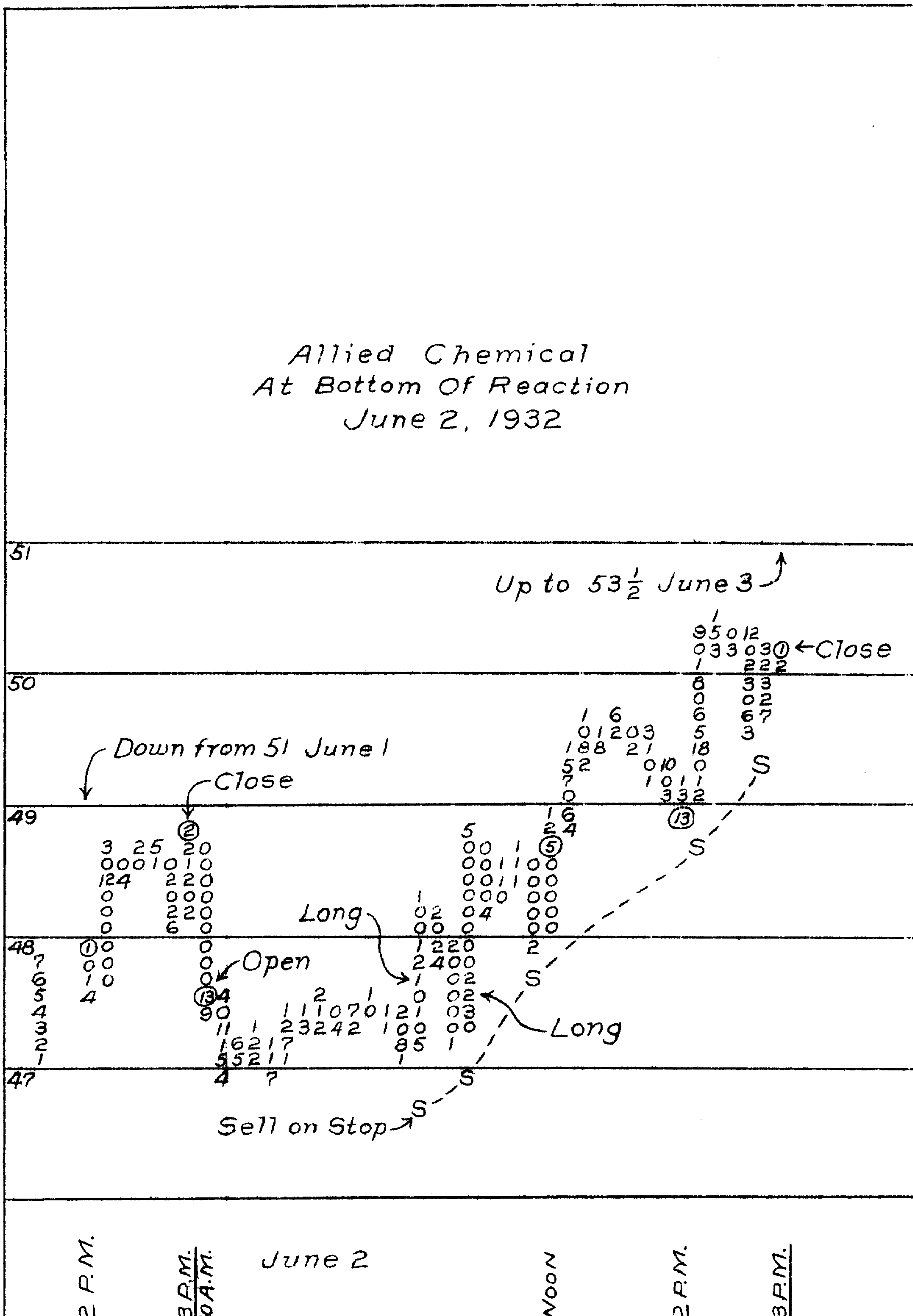
The opening, June 2nd, is 1-1/4 points down, with 1300 at 47-5/8; then 900.1/2 400.5/8 1100.3/8 100.1/4 500.1/8 400.47. A rally of 3/8 and a dip to 47 makes a 3/8 trading range. We watch to see which way the stock will go out of this range. The first signal is bullish -- 100.47-1/2, 1/8 higher. Next support at 47-3/8; another gain of 1/8; still bullish. 1/4 point range 3/8-5/8, then a 1/4 point dip below that to 47-1/8; higher support than the former low. If it does not go on through 47, this indication is bullish. 500.47-1/4 100.1/2 makes a gain of 3/8 after 1/2 point dip -- still bullish.

When the price recovers to 47-1/2, we have a forecast of a breaking out of this range and decide to go with it either way. We place orders to go long on stop at 47-3/4 or short at 46-3/4. Our long stop is executed; this cancels the selling stop. We immediately enter an order to sell 100 on stop at 1 point down, which happens to be also at 46-3/4. This is intended to limit our risk on our long trade to 1 point.

The break through on the up side makes 48-3/8. All but 1/8 of this recovery is lost, but another rally starts from 47-1/4. There have been frequent skips of 1/8 to 5/8; these coming at the bottom of the recent decline indicate a lightening pressure. This is bullish. From 47-3/4 the next sale is 500.48-7/8, then 400.1/4 100.1/2.

Now look back over the past few swings and note that the last bottom was made on 100 shares 3/4 point down from the previous sale and the following dip was 400 at 5/8 down. Then after 1/2 point rally on 100 share lots there is another dip of 200 shares at 3/4 down from the last sale. Someone is evidently trying to mark this stock down in order to bring out fresh selling. This means that they want the stock. Buying is better than the selling.

There is a bulge to 49-3/4 and a dip back to 49 where 1300 shares are taken. Then the price snaps straight up to 50-1/4, then 50-3/8. We raise our stop to 48-3/4 on both lots. Volume enough comes in to bring a reaction to 49-5/8 but the stock closes strong at 50-1/4 within 1/4 of its top. Increasing indications of strength have led us to carry the trade overnight. Our stop is raised to 49-3/8 assuring a profit of 1-5/8 if the stop is executed at that exact price. Of course, there is never any assurance of this, especially in a stock like Allied Chemical which, as the chart shows, has numerous skips, indicating a market that is not at all close. The activity of this stock, however, compensates for this additional factor of risk.



Allied Chemical
At Bottom Of Reaction
June 2, 1932
51
50
49
48
47
Up to 53½ June 3
Close
Down from 51 June 1
Close
Long
Open
Long
Sell on Stop
2 P.M.
3 P.M.
10 A.M.
June 2
Noon
2 P.M.
3 P.M.

Allied Chemical

At Top of Rally June 15-16, 1932.

On June 10th this stock made a low of 47, then rallied to 54-1/2 on June 11th, reacted to 50 on June 13th and closed at 53 on June 14th. It opens June 15th at 53-3/4. Our position is neutral. The first buying wave in this stock amounts to 5/8. The next down wave wipes this all out. Then an up wave of 3/4 and a normal half way dip of 3/8. The picture is bullish so far, because the stock has worked out of its 3/4 point range on the up side. We give an order to buy and get it at 54-1/4. Our stop is 53-1/2.

Next a rally to 54-5/8. The upward swing is not very vigorous. It is a drifting upward; little power under it. The gains are slight and the volume is small. Above 55, the formation becomes horizontal. A 1/2 point dip to 54-3/4 brings in a little support; it indicates another bulge, and the stock runs up to 55-1/2, with two 900 share lots at 1/4 and 1/2. On two sales 100.55-1/8 and 200.54-3/4 the stock loses all the rally -- a sign of weakness. We must get out on the next bulge. Then 1200.55 700.1/4 200.3/8. We give an order to reverse our position (i.e., close out our long commitment and sell short an equal quantity,) and get 55 for one and 55-1/8 for the other. We place a 5/8 stop at 55-3/4 on our short trade. The formation is now pointed like an arrowhead. The stock has come to a balance with 55-1/8 forming the point. It should pass out of that range on the down side, unless it contradicts its sign of weakness.

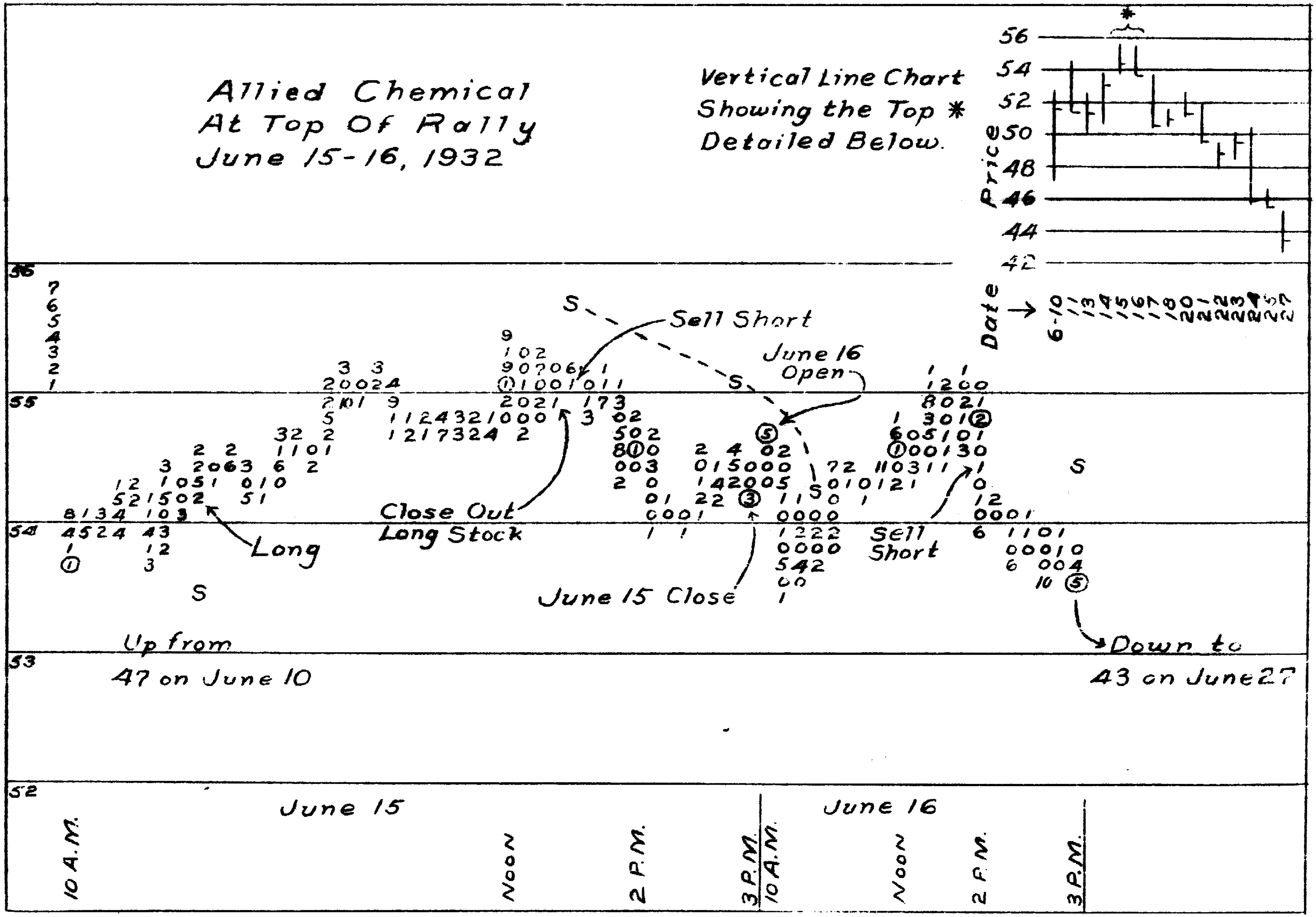
The trading range narrows when the stock dips to 54-7/8 and rallies to 55-1/4. Note the dip of 1/4 point below the critical 55-1/8 level and the rally of only 1/8 above that. This delicate scale shows that the balance of power is still on the down side.

A further dip to 54-3/8 and 1/2 point rally; then the stock sells at 54 on two sales. It rallies to 54-5/8; then makes a trading range 54-1/4--5/8. Here we bring our stop down to 55-1/8 (our selling price) and carry the trade overnight. Having rallied from 47 on June 10th -- 8-1/2 points, a reaction of a few points is in order.

Next day the first sale is 500.54-3/4; then a straight decline to 53-1/2. A rally of 3/4, a reaction of 1/2, and with the sale of 200.54 the formation becomes wedge-shaped, with the point around 54. We bring our stop down to 54-1/4 as protection against a rally and this stop is executed at 54-1/2 -- a net profit of 1/8. Now we are neutral, awaiting new indications.

The rally continues to build up and we watch to see whether the up swing has power enough to go into new high ground, above 55-1/2. Two rallies, the first to 54-7/8 and the second to 55-1/4, are immediately wiped out -- weakness again. Now we look for a chance to sell on a bulge. On the next upward surge it makes 55-1/4 again, then reacts quickly to 54-3/4. Supply is greater than the demand. We put in a short selling order and get 54-1/2 for it. Our stop is 55-1/2. The steady decline continues and the stock closes within 1/8 of the day's low, with 500.53-5/8. We bring our stop down to our selling price (54-1/2) and carry the short trade overnight.

The small section of the Vertical Line Chart indicates the subsequent action of the stock, which declined to 43 on June 27. The action on the two days described in the Tape Reading Chart was, therefore, a fair example of a turning point for a normal reaction which developed into a substantial down swing.


Allied Chemical
At Top Of Rally
June 15-16, 1932
Vertical Line Chart
Showing the Top *
Detailed Below.
Price
56
54
52
50
48
46
44
42
Date
6-10
Sell Short
June 16
Open
Close Out
Long Stock
Long
June 15 Close
Sell
Short
Up from
47 on June 10
Down to
43 on June 27
56
55
54
53
52
June 15
June 16
10 A.M.
Noon
2 P.M.
3 P.M.
10 A.M.
Noon
2 P.M.
3 P.M.

J. I. CASE

Reaction of March 14, 1932.

This stock opens at 37-1/2, declines to 37 and immediately recovers all but 1/8 of the decline. It then dips to 37-1/8 and the next sale is 37-1/2. All this is an indication of strength -- first, the ability to recover; next, the 1/4 point dip and a full recovery to the opening price. There is more strength than weakness.

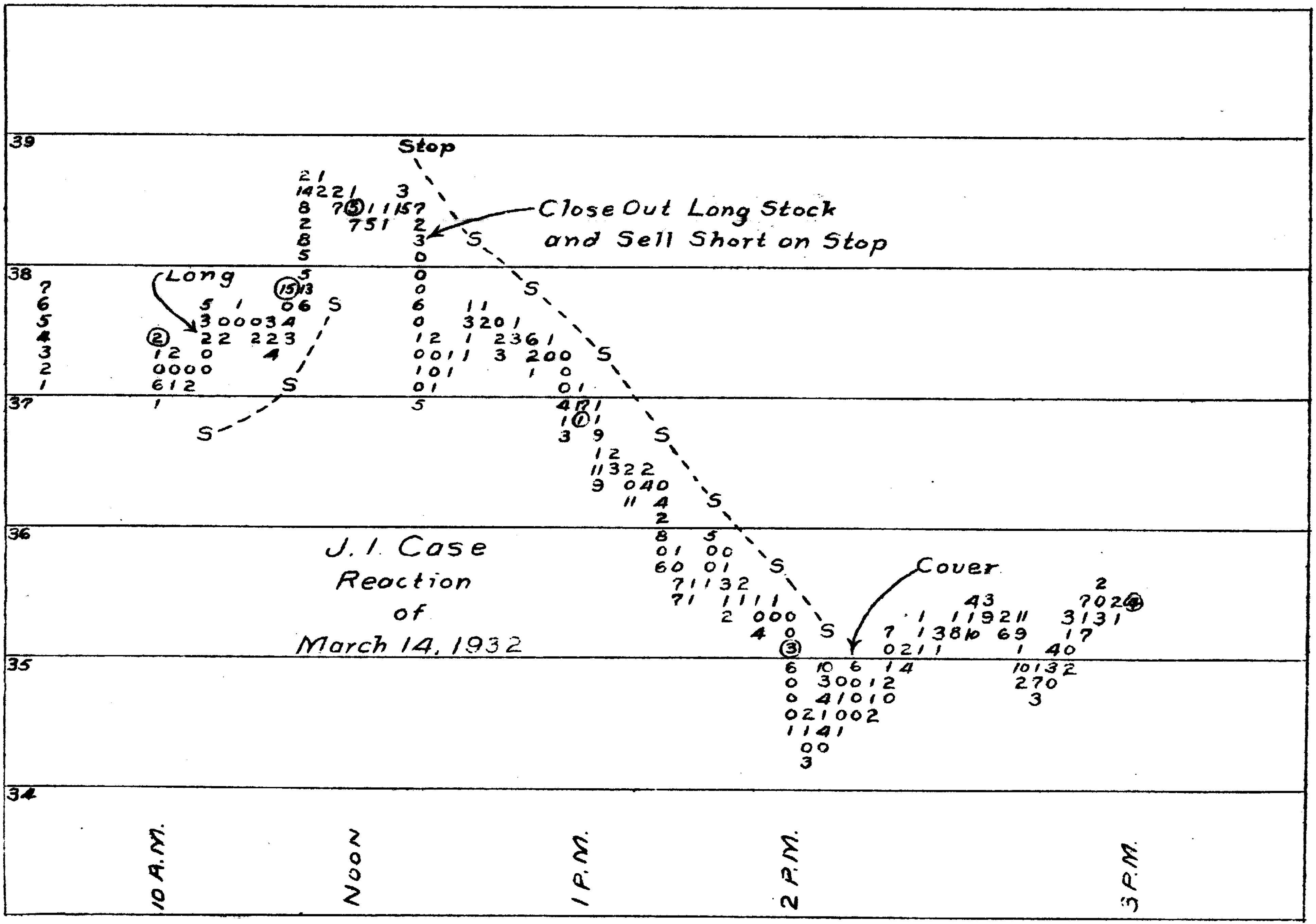
We go long at 37-1/2 with a stop at 36-3/4. A trading zone 37-1/2 to 3/4 is established, and after a dip of 1/8, the price moves up to 37-7/8, 1500 being taken there. Another 1/8 dip and 1300 more are taken at 37-7/8, followed by a straight run up on substantial volume to 38-3/4. A reaction of 1/8, then one of 1/4; 1/8 rally and another dip of 1/4, making a trading zone 38-3/8 to 3/4. Note the dullness between 11 A. M. and noon -- a bearish sign on a rally. As the trading strings out to the right on the chart, we find that a considerable volume is coming in on this bulge. Adding the transactions horizontally, we note that 8600 shares change hands at the 38-3/8 level and above.

On the first run up we have moved our stop up to 37-1/8, then to 37-3/4. We now change it to a double stop at 38-1/4, for if this 8600 shares is not followed up by further purchases, we expect the price to decline. And if it breaks even 1/8 below the 38-3/8 support, we want to get out of our long stock and go short.

The price touches 38-1/4, which gives us a net profit of 1/4 on our long stock and puts us short at that figure. Our stop on the short trade is 39.

In a few sales after that, the entire gain for the day is lost; the price touches 37, the low point of the opening dip. This is 1-3/4 down from the top and calls for a 7/8 rally; but the rally falls 1/8 short of half way. The volume is light -- bearish. Our stop is first moved down to 38-1/4, and when the rally begins to fade out, we make it 37-7/8. From that time on, there is a succession of new lows and weak rallies. We keep moving our stop down -- first to 37-3/8; then to 36-3/4; then 36-1/4; then 35-3/4 and finally to 35-1/4. Nothing that has happened so far has caused us any uneasiness on this short sale. After the 3/4 rally from 37, note that the subsequent rallies are as follows:1/4, 1/4, 3/8, 1/4, 1/4, 1/8, 1/8, 1/2, 1/4, 1/4, 1/8. Now the stock is 34-1/4, and at that price we are 4 points to the good on paper, with a stop at 35-1/4; so at least 3 points are assured.

We may be smart enough to cover on the decline around 2 P. M., or to shove our stop down within 1/4 of the bottom, because we can't expect it to go right on down without a rally. But the rally of 3/4 to 35 warns us that the stock is meeting more resistance below there and when it dips again to 34-1/2 we give an order to buy it at the market and cancel our stop. We have to pay 35, which gives us a gross profit of 3-1/4 points, or a net of 2-3/4. We stand pat for the rest of the day.


39
38
37
36
35
34
Stop
Close Out Long Stock
and Sell Short on Stop
Long
Cover
J. I. Case
Reaction
of
March 14, 1932
10 A.M.
NOON
1 P.M.
2 P.M.
3 P.M.

AMERICAN CAN

Combined with five leaders
June 14-15-16-17, 1932.

This Tape Reading Chart of American Can is combined with a Wave Chart of five leaders, of which Can is one; the other four are Anaconda, General Electric, General Motors and Steel. It is remarkable how closely Can follows the five leaders. Perhaps this is because it was at that time more dominant in its market movements than the others among the five; but this is just what we are looking for — a stock that can be plotted with a group in which the Wave Chart aids us in interpreting the Tape Reading Chart. Thus we can anticipate the moves and trade with profit in the one stock.

The opening of Can, June 14th, is 200.38-1/8. There is a quick decline of 1-1/8 points to 37; then a rally of 1-1/2 points, which shows that the greatest power in Can is on the bull side. The Wave Chart confirms this by advancing nearly twice as much as it declined from the opening. Following the straight upswing of 1-1/2 points we expect a decline of 3/4, but the dip is only 5/8 — a confirmation of strength.

On this dip we go long at 38, with a stop at 36-7/8. When the price goes to a new high, 38-5/8, we move our stop up to 37-5/8. When after a 1/4 point trading range, Can touches the high point again with 200 shares at 38-5/8, we raise the stop to 38-1/8.

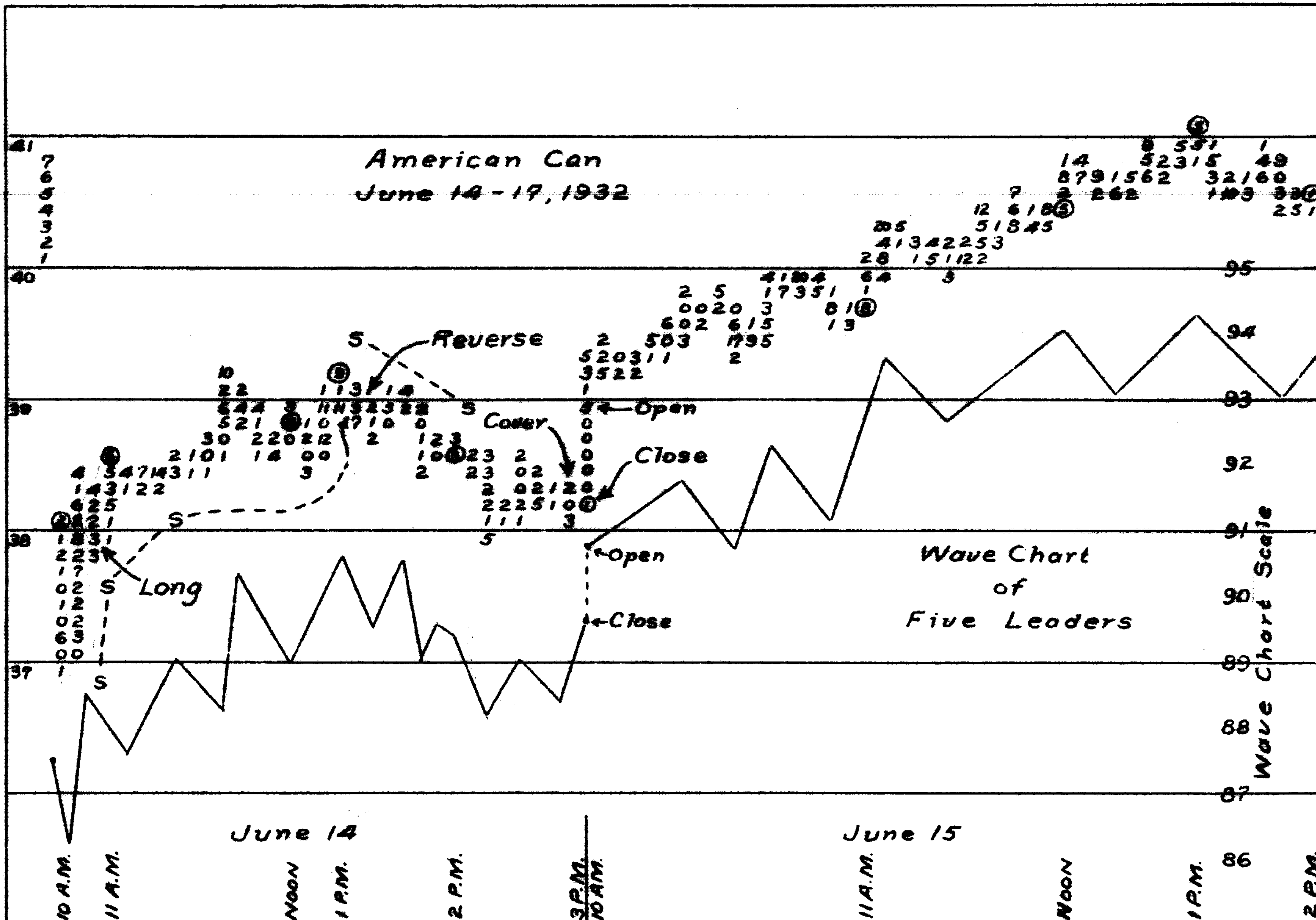
A further bulge and a new high is made -- 1000.39-1/4. The Wave Chart has heretofore confirmed the bullishness, but the down swing from that point, the fourth for the day, is a little longer than the third down swing, and we get ready to sell on the rally, unless Can goes on through to a new high with considerable volume.

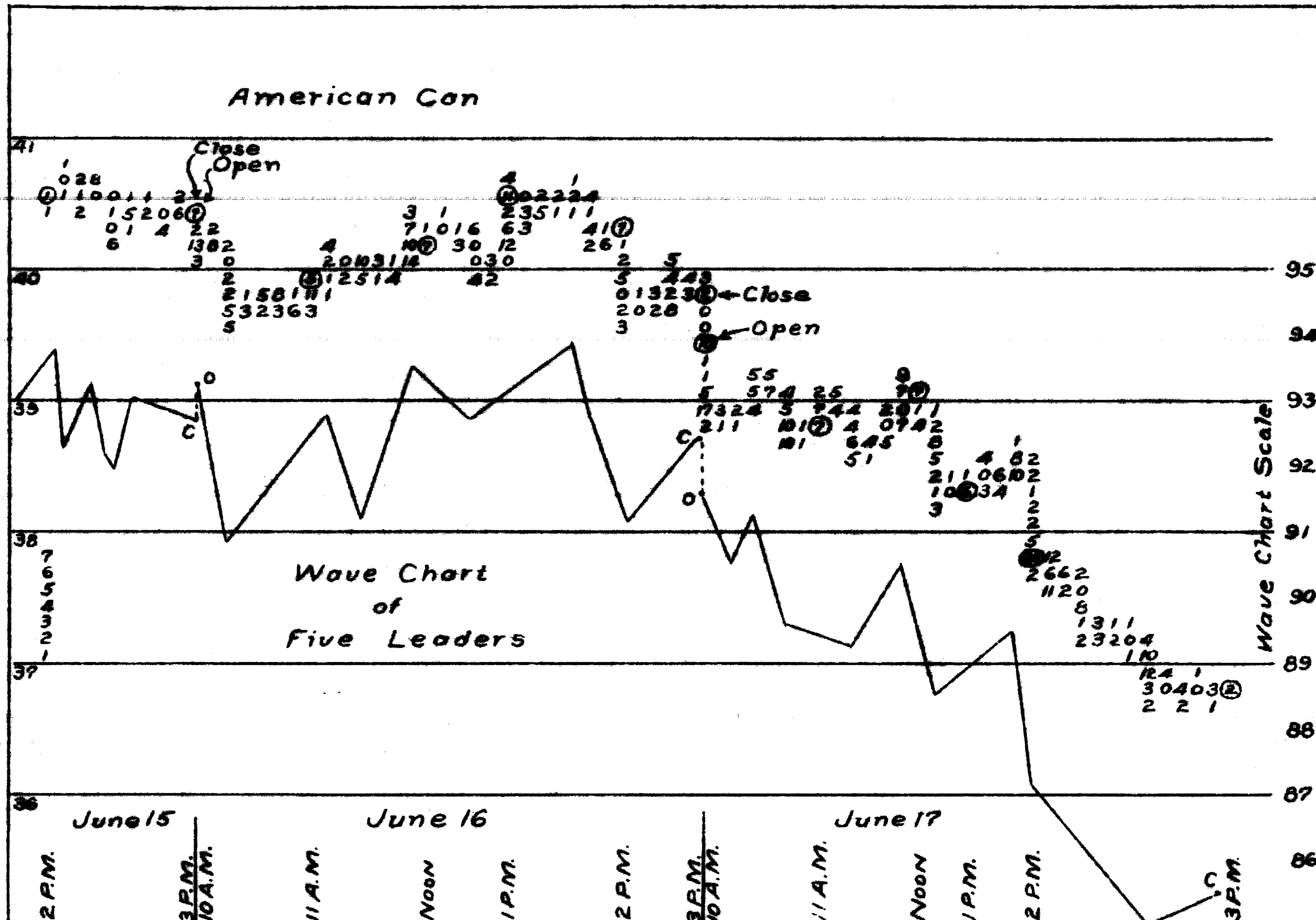
Can stops again with 900.39-1/4. We bring our stop right up under it to 39 and make it a double stop, so that when the price recedes again we are out of our long with a gross profit of 1 point and are short at 39 with a stop at 39-1/2.

After touching 38-7/8, there is a weak rally to 1/8 lower than the previous top, and the Wave Chart records a fractionally lower top, which is a confirmation that the short side is the right one.

Can declines to 38-1/2, rallies 1/4, then backs up to 38. Our stop is moved down to 39. The Wave Chart has been bearish, but the following rally in the Wave Chart is longer than the previous one, and the dip which follows is shorter than the previous one. This is our warning that a rally is coming. We cover our short at the market and get it at 38-3/8, which is 5/8 gross, or 1/8 net. Added to the previous profit of 1 point gross, or 1/2 net, makes 5/8 net profit for the day. The closing price is 38-1/4.

From now on, we suggest that students use this combination chart for working out correct trades based on instructions given in this and other Chart Studies contained in this Division of the Course. Also that the result of their paper trading be sent to us in writing so that we can go over and check progress and correct errors. This will give us both an opportunity to see whether these Tape Reading instructions and examples are being fully understood, and in case of any misconception or departure from proper procedure, we shall be able to make corrections.


American Can
June 14 - 17, 1932
Reverse
Cover
Open
Close
Long
Open
Close
Wave Chart
of
Five Leaders
Wave Chart Scale
June 14
June 15
10 A.M.
11 A.M.
NOON
1 P.M.
2 P.M.
3 P.M.
10 A.M.
11 A.M.
NOON
1 P.M.
2 P.M.


American Con
Close
Open
Close
Open
Wave Chart
of
Five Leaders
Wave Chart Scale
41
40
39
38
37
36
95
94
93
92
91
90
89
88
87
86
June 15
June 16
June 17
2 P.M.
3 P.M.
10 A.M.
11 A.M.
Noon
1 P.M.
2 P.M.
3 P.M.
10 A.M.
11 A.M.
Noon
1 P.M.
2 P.M.
3 P.M.