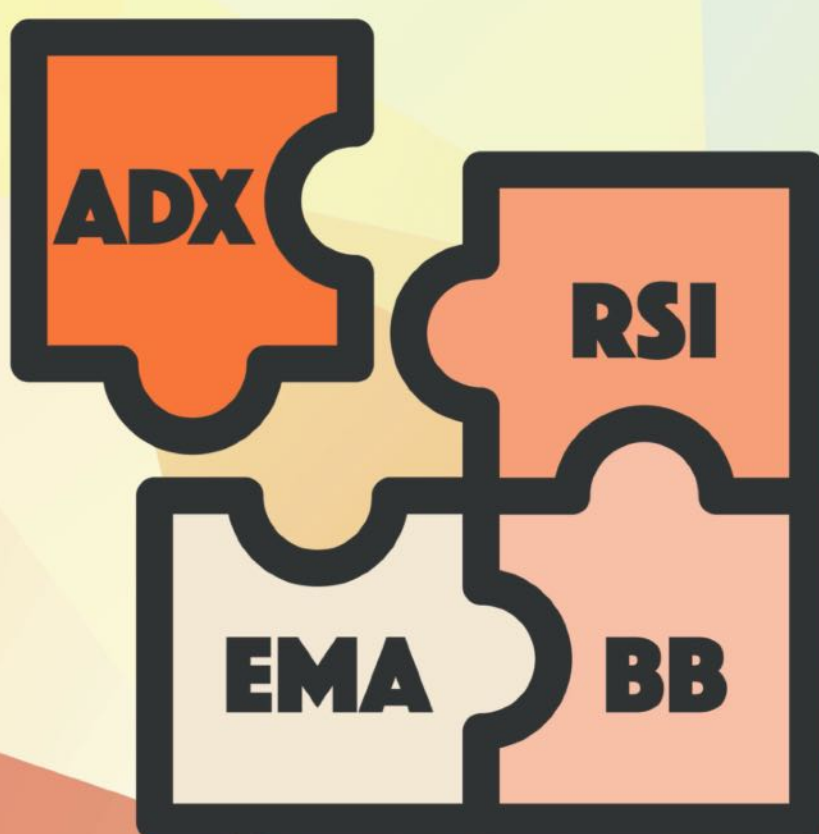


# **RDX**

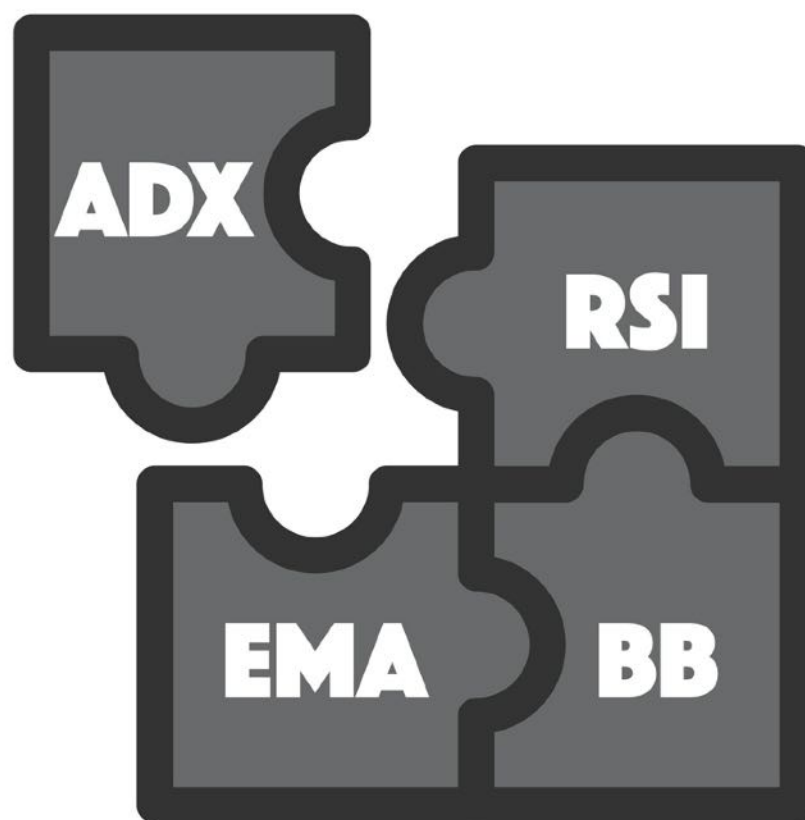
**A prescription for profitable trading**



**Dr. Jignesh Shah**

# RDX

**A prescription for profitable trading**



**Dr. Jignesh Shah**

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with thanks to admin team: Kunjan, Nathan & Nitin

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# INTRODUCTION

Application of technical analysis in trading falls into two major categories:

## 1. PREDICTING (“PREDICT AND PANIC”)

In first category, predicting and trading means one will buy at supports, at demand zones, at Fibonacci retracement levels. One will buy when markets looks oversold. One will buy at trendline supports etc. People who are following Elliot wave principles or neowave also fall in this category. I will consider all above examples as predict and trade category type.

These are few examples where one will do trading based on his ability to judge the future price reversals.

“Predict and Panic” is being mentioned here, as the outcome of the trades based on predicting the prices are most likely to cause anxiety and panic to the traders.

## 2. FOLLOWING (“FOLLOW AND FLOURISH”)

Another group of traders are formed by price followers. Here buy the strength & sell the weakness is the mantra.

Here you are not supposed to look at trend lines, Fibonacci levels, support levels, resistance levels, demand zones or supply zones... nothing like that..

Here the traders will Buy maximum in overbought zones and will Short maximum in oversold zones, supported by some confirming indicators.

I belong to this second category of traders.

“Follow and Flourish” is being mentioned here, as the outcome of the trades based on following the trend are most likely to turn in to profitable trades, offering better control in managing the trades for the trader.

Remember both methods are good. Both methods have their own advantages and limitations. You have to decide which trading method will suit to your personality. My whole trading ideas discussed here are based on this basic concept: Buy the strength & Sell the weakness.

I am following very simple trading plan based mainly on RSI and ADX.

# MOVING AVERAGES

In long term averages, **150 EMA** is smaller and **200 EMA** is larger average.

In short term averages, **13 EMA** is smaller and **21 EMA** is larger average.

Now to judge Buy/Sell decisions, we need Clear signal from the averages. All signals other than Clear signal are considered Neutral.

**Clear Buy** signal needs to fulfil the following criteria:

1. Closing Price should be above both the averages
2. Smaller average should be higher than the larger average

**Clear Sell** signal should have:

1. Closing Price below both the averages
2. Smaller average should be below the larger average

- **Reliable Buy signal** is identified when Clear Buy in both Short term averages and in Long term averages exists.
- Same way **Reliable Sell signal** is identified when Clear Sell signal in both Short term averages and in Long term averages exists.
- **No Reliable Buy or Sell signal** is identified in case there is conflict between Long & Short term moving average signals.

# BIAS (RSI)

Now whenever we want to initiate a trade then firstly, we have to decide the BIAS for direction. I always look only at RSI first to decide the direction, & for that I use the word “BIAS”.

BIAS based on RSI is as follows:

- **RSI Above 55: Long**
  - We can Sell Put or Buy Call, but only when RSI is above 55.
- **RSI below 45: Short**
  - We can Sell Call or Buy Put, but only when RSI is below 45.
- **RSI between 45-55: Neutral**
  - No directional trading zone when RSI value is between 45 and 55.

We just take overview from averages but our trading is based on RSI only.

**How to identify perfectly Bullish and Bearish stocks on the basis of RSI?**

**For Bullish Stocks**

- Daily RSI greater than Weekly RSI, and Weekly RSI greater than Monthly RSI, and all three RSI above 55

**For Bearish Stocks**

- Daily RSI lesser than Weekly RSI, and Weekly RSI lesser than Monthly RSI, and all three RSI below 45

# M O M E N T U M ( R S I )

Momentum study guides us for exposure in our Long or Short trade.

**Momentum based on RSI for Long trades** is as follows:

- RSI— 55-60~Mild Long (25%)
- RSI— 60-65~Moderate Long (50%)
- RSI— 65-70~Strong Long (75%)
- RSI Above 70~ Very Strong Long (100%)

**Momentum based on RSI for Short trades** is as follows:

- RSI— 45-40~Mild Short (25%),
- RSI— 40-35~Moderate Short (50%)
- RSI— 35-30~Strong Short (75%)
- RSI below 30~Very Strong Short (100%)

Please note, one need to check RSI at closing of the day for continuation of trade and exposure to the next day.



# TREND (ADX)

Now finally trend confirmation. ADX is very simple and effective tool to judge whether the underlying is trending or not.

Whenever ADX is rising it gives confirmation of trend formation and when ADX crosses 25, it suggests strong trend formation.

ADX gives first indication of converting sideways to trending move in the underlying when it starts rising with either +DMI or -DMI leading it.

- When ADX is rising and BIAS is on Long side, then it indicates UP Trend.
- Similarly rising ADX and Short BIAS gives confirmation of DOWN Trend.

For using ADX, don't consider the absolute value. Just develop the observation skill to watch ADX.

For using RSI, strictly consider absolute numerical value.

- When ADX is not rising then I prefer writing positions in both Calls and Puts (Non directional trade).
- When ADX starts rising then sometimes (strong momentum), I buy options also in the direction of trend (UP or DOWN).

**ADX should also be between the two DMI for Buying options.**

If ADX is below both DMIs, this suggests range bound structure, which is suitable for Non-directional trades.

I consider RSI and ADX as the Pulse and BP measurements of patients....

We doctors can easily manage the health of the patients with these two simple time tested parameters.

Same way we can easily manage our trades based on these two simple time parameters of RSI and ADX (along with DMIs).

Example:



# BOLLINGER BANDS

Bollinger bands have limited use. I do not use Bollinger Bands for making trading decisions, but they have their utility.

- Bollinger bands of one hour chart can be used to decide the strike price of options for writing. So, when we are having neutral positions, then to sell options, the strike price should be outside the band of 1 hour chart.
- Bollinger band narrowing suggests momentum-less trading
- When band is very narrow and ADX family meeting is going on, then it is better to reduce the option writing positions because some trending movement is coming

# WHEN TO BUY, WHEN TO SELL

For options Buying, Far expiry\* is always better than Near expiry. For Buying options, Monthly is better, as there is less price delay.

Reverse is true for Selling.

- **Buy:** Rising ADX with RSI showing strong momentum (above 65 or below 35) gives better results in options buying (or in futures trading).
- **Sell:** Option selling\*\* is more beneficial when ADX is falling.

In non-trending states, Sell Far OTM options

In trending states, Sell and Buy both can be done.

\*Far/Monthly expiry has less liquidity

\*\*Options Selling should always be with hedging

# WHAT TO BUY, WHAT TO SELL (CALLS OR PUTS)

- For all Bearish conditions (RSI < 45), we can Sell Calls
- Buying of Puts only when we have strong Bearish (RSI < 35) indication
- For all Bullish conditions (RSI > 55), we can Sell Puts
- Buying of Calls only when we have strong Bullish (RSI > 65) indication

ADX	RSI	Strategy
Rising	Above 65	Buy Call
Rising	Above 55	Sell Put
Falling	Between 45-55	Non-directional option selling
Rising	Below 45	Sell Call
Rising	Below 35	Buy Put

# WHERE TO BUY, WHERE TO SELL (STRIKE SELECTION)

- Always Sell OTM (Delta 0.2 or less preferred)
- Always Buy ITM or ATM options

My first focus on selecting strike price is always the last closing price plus or minus ATM straddle. The strike price where the distance between call and put is minimum is the ATM straddle (Jodi Bhav). The expected range based on ATM straddle gives us the Call and Put strikes to trade for a Short OTM Strangle.

Expected range based on ATM straddle (Jodi Bhav):

- Upper limit = closing plus straddle = Call strike selection for OTM strangle
- Lower limit = closing minus straddle = Put strike selection for OTM strangle

Generally these ranges are around 0.2 delta, so it becomes little easy for selecting strike. This, however, is the minimum range, it's always better to select strike as per delta (0.2 or less).



Adjust the strikes as per market move.

During UP move of the underlying, shift the Puts higher and increase position, & decrease Short position on Calls.

Similarly during DOWN move of the underlying, shift the Calls higher and increase position, decrease Short position on Puts.

# NEUTRAL ZONE

Ideal characteristics of neutral zone:

- Neutral range of RSI is 45-55. But it can extend up to 40-60 range. (“Traffic Jam”)
- Price is around both the short term averages.
- ADX is falling or flat with both DMI also in close contact with ADX (“Meeting of ADX family members”)
- (optional) Bollinger band narrowing

When we are in neutral zone, with ADX falling and RSI in neutral range, go for non directional options writing. The maximum one can hold in neutral strategy is between 40-60 RSI. Beyond this (i.e. below 40, or above 60), it's better to convert into directional strategy.



# ENTRY

When you are trading momentum, then start of momentum is your entry.

## LONG ENTRY

- RSI breaks the range, & crosses above 55
- Price gets out of range (Bollinger band)
- ADX starts rising

You need to initiate trade here. We can Sell Put (or Buy delivery, Buy Future) but only when RSI is above 55.

Then according to RSI breaking one by one levels you need to add positions as per our RSI criteria e.g. add another lot above 60, another above 65, & another above 70

When RSI goes above 65, then apart from Selling Puts, we can Buy Calls also.

## SHORT ENTRY

- RSI breaks the range, and goes below 45
- ADX starts rising

You need to initiate trade here. We can Sell Call (or Sell delivery, Sell Future) but only when RSI is below 45.

Then according to RSI breaking the levels one by one you need to add positions as per our RSI criteria e.g. add another lot below 40, another below 35, & another below 30.

When RSI goes below 35, then apart from Selling Calls, we can Buy Puts also.

# EXIT

I don't keep fixed stop loss (SL). It is always dynamic. Means I decrease my positions step by step. Suppose I have bullish positions then I decrease positions when RSI goes below 70, Then again decrease below 65.... like wise.

## LONG EXIT

(Long positions: Bought Calls or Sold Puts):

- If +DMI is above ADX, we can continue to hold our positions. DMI+ going below ADX suggests decreasing strength of uptrend.
- When +DMI goes below ADX line, decrease your positions (i.e. If +DMI crosses below ADX, one third of the position has to be closed).
- When RSI goes below 70, then 65, then 60 (e.g. If the RSI value moves (from above 70) to below 70, reduce long positions by one third)
- When the price goes below 13 EMA, decrease positions further or convert into neutral positions

## SHORT EXIT

(Short positions: Sold Calls or Bought Puts):

- If -DMI is above ADX, we can continue to hold our positions. DMI- going below ADX suggests decreasing strength of down trend.
- When -DMI comes below ADX line (i.e. If -DMI crosses below ADX, one third of the position has to be closed).
- When RSI goes above 30, then 35, then 40 (e.g. If the RSI value moves (from below 30) to above 30, reduce short positions by one third)
- When price goes above 13 EMA (i.e. If the Price moves above 13EMA, book one third position)

Also, when ADX is very high, it's normally difficult to sustain such high levels. So, it's better to reduce the positions. Similarly, if large number of candles have been already consumed by falling ADX, it may get strength and can rise. So we should be ready with options buying mindset. When ADX is falling and structure is bearish, then call writing gives better RR than put buying.

\*Any of these three may happen first. We have to follow the market and act accordingly.

We carry forward our positions only if Daily chart is fulfilling all 3 criteria. Otherwise, we exit all at end of day.

# TIMEFRAME

- For Weekly expiry, we should use 15 minutes (or 30 minutes) candles from market opening to 3 PM. But for carrying forward positions to next day, we must shift to Daily chart after 3PM.
- BANKNIFTY is high beta, so 15 minutes chart is preferred
- For low beta stocks and indices, 30 minutes chart is preferred
- Hourly is considered father of both. In case of any confusion, take guidance from father.
- For Monthly expiry and for Stock Futures, Hourly chart is preferred.
- For Positional trades, Weekly and Daily charts are to be used.

“Please note that in 15 minutes charts, we have 25 overs game for one day and overall 125 overs test match for the entire weekly expiry period”

Details:

In one day, we can get 7 candles of 1 hour each, or 25 candles of 15 minutes each.

In Weekly expiry, with 1D time frame, we get only 35 candles, which are too low to capture the movement of weekly expiry. With 15 minutes time frame, we get 125 candles in weekly expiry enabling us to spot the trading opportunities better.

In Monthly expiry, with Daily time frame, we get around 20 or 25 candles in a month which is too low to capture the movement. With Hourly time frame, we get around 140 candles in a month which can easily capture all movements worth trading in the month.

# AT WHAT TIME TO INITIATE TRADE

First trade depends on the Daily overall structure:

- Recognising ORB
  - The first 15 minutes of trade is known as opening range.
  - Write down High and Low of Opening Range.
  - Now whenever price trades above high or below low of Opening Range then it is known as Opening Range Breakout (ORB).
- If Daily is neutral then wait for ORB
- If Daily is clearly Bearish or clearly Bullish, then look at the first candle (15 minutes timeframe). Take decision to trade at 9.20AM after watching first 5 minutes formation of first 15 minutes candle. Here's how:
  - If first 15M candle after 5 minutes from market opening (i.e. around 9.20 AM) is also in the same direction of Daily, then start trading by 09:20 AM.
  - If first 15M candle after 5 minutes from market opening is in the opposite direction of Daily, then wait for candle to get completed (by 09:30 AM) and then wait till ORB happens.

# ROLE OF DERIVATIVES DATA

In trading 70% is technical and only 30% is derivatives.

## ATM STRADDLE (JODI BHAV)

As already detailed earlier, the ATM Straddle nearest to the last closing spot price helps us in selecting the OTM Strike price to trade.

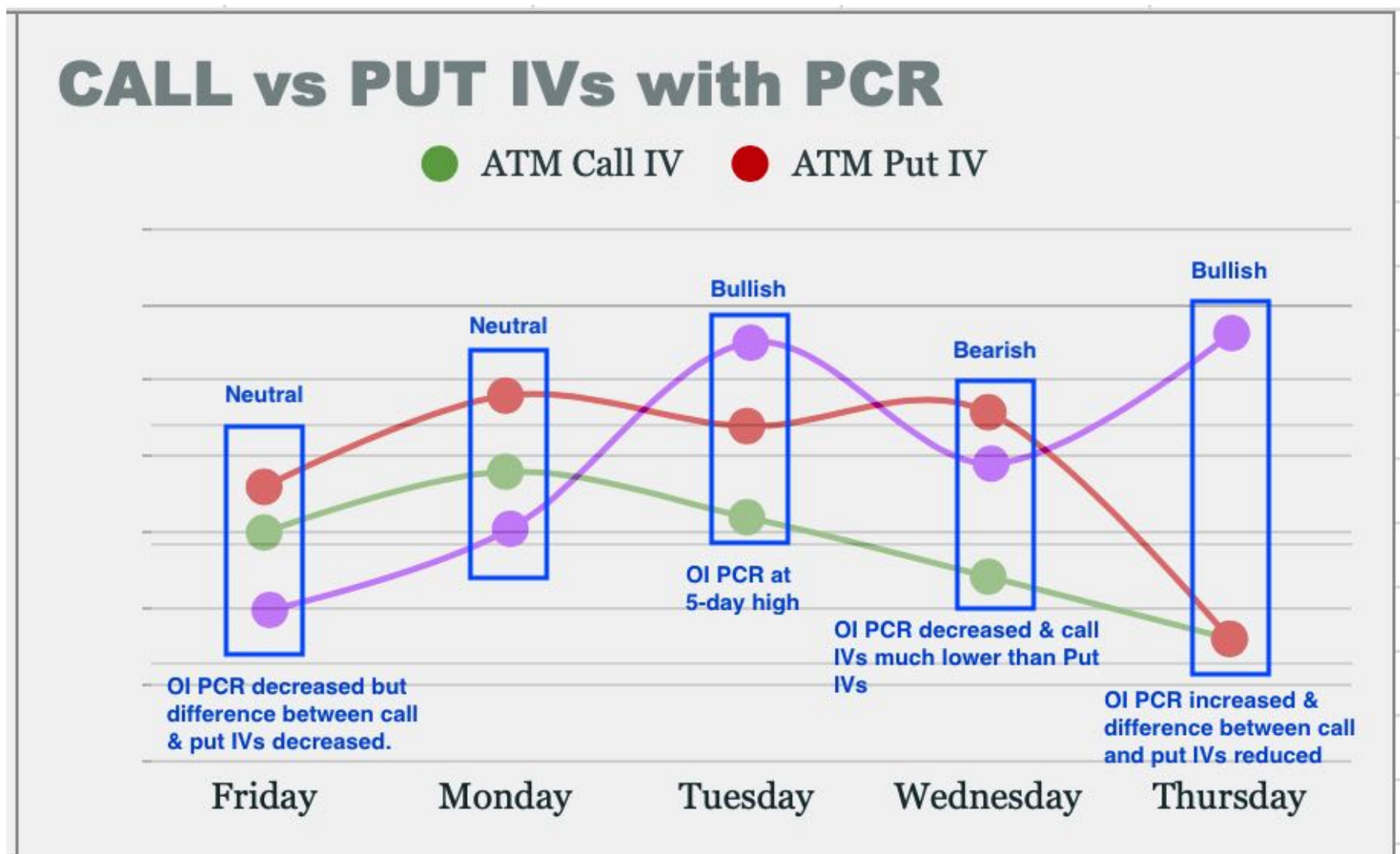
- Upper Strike = Closing Price plus ATM Straddle
- Lower Strike = Closing Price minus ATM Straddle

## PUT CALL RATIO (PCR)

- Increasing PCR with increased Call IVs is indication of Strongly Bullish condition
- Increasing PCR with increased Put IVs is indication of Bearish condition
- Decreasing PCR with increased Put IVs is indication of Strongly Bearish condition
- Decreasing PCR with increased call IVs is indication of Bullish condition

	↑ Call IV	↑ Put IV
↑ PCR	Strongly bullish	Bearish
↓ PCR	Bullish	Strongly Bearish

- In Bullish markets Call IVs will be higher than Put IVs
- In Bearish markets, Put IVs will be higher than Call IVs



I see IVs as reflection of demand and supply. If demand is more, then IVs will be higher and if supply is more, then IV will be lower. If demand is accompanied by increased open interest then it will reflect in PCR.

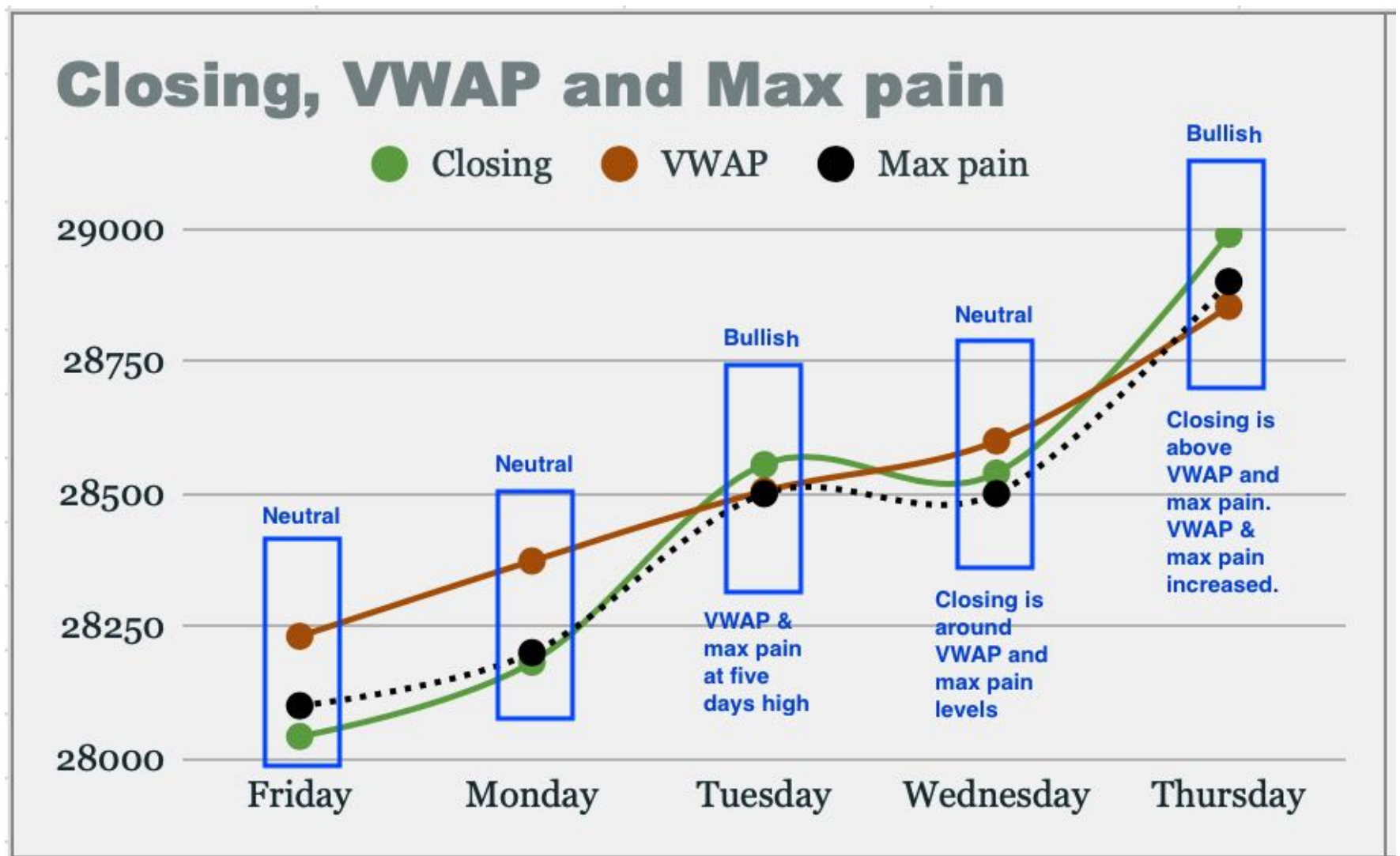
Practically we can focus on Call IVs minus Put IVs. If the difference between Call & Put IV is 8-10, the one with higher IV will indicate the direction of significant moves.



## MAX PAIN, VWAP & CLOSING PRICE

The price of an underlying stock tends to gravitate towards its "maximum pain strike price" - the price where the greatest number of options (in rupee value) will expire worthless.

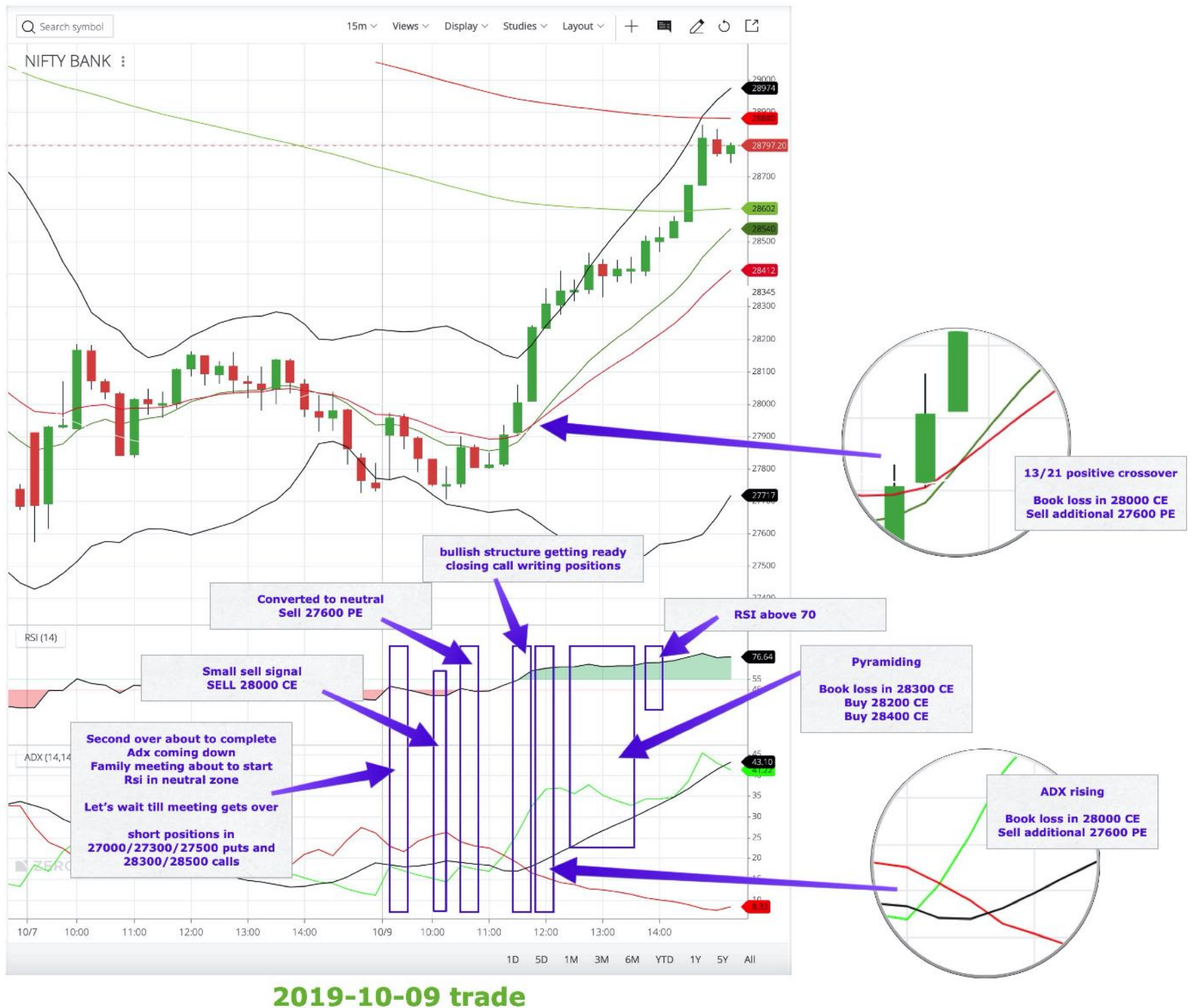
- Decreasing max pain level is Bearish
- Increasing max pain level is Bullish
- Similarly, increasing VWAP is bullish
- Closing above VWAP & Max pain level is bullish





# TRADE EXAMPLE

This trade was taken on 9th October 2019 using the RDX strategy as described in above pages.





I am Dr.Jignesh Shah, a practicing gynaecologist in Ahmedabad since 1997. I have my own nursing home in Nava Vadaj area of Ahmedabad in name of Jigisha Nursing Home. I was Hon. Secretary of Ahmedabad medical association in 2012-14. I also worked as Vice President of IMA Gujarat in 2016.

Stock market is my passion. I am trading and investing since 1992. I committed lots of mistakes in first 15 years of my trading, then I started trading in systematic way from 2009.

I used to trade in futures mainly but gradually turned into options selling. For past two years, I trade only in options writing & mainly in Bank Nifty options. And since two years my trading performance has been consistent. I get 3-5% returns monthly. I have won three times Zerodha sixty days challenge back to back.

I gave NISM exam in April 2019 and passed it with 95%, then I became sub broker with LKP securities. Now I look after around 30 trading accounts.

While planning to do some charity work in my medical field, I realised that if i do some work in financial field then may be I can help more families than what I can do in medical field. Then I started sharing my trading experience on twitter and on my telegram channel.

Wish you a happy trading journey!



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