
Ask Slim

By Steven Miller



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Dear Slim,

I have been trading online for just under a year. I started out trading 10-year Notes and have been trading e-Mini S&Ps for the last few months. I have not made any consistent money so far, but I keep thinking I'm ready to turn the corner. We had enough money saved up to live on for this period and my wife earns a good salary. But now savings are dwindling and we're getting nervous. Before I began trading I was a house painter. I did that for many years, but turned the small business over to my crew. My wife says I was a successful painter and I can make a living that way. But trading is in my blood and I feel bad about going back to painting. In fact, I don't even want to hear the suggestion. I want to keep trading. What do you recommend for a trader in my situation?

—Stewart M., San Diego, CA

Dear Stewart,

It sounds like you have put in a good year learning to trade. As I have mentioned in the past, turn-around time for new traders can be well over a year. You have appropriated funds to this learning period, which was a very good approach. I'll guess there are psychological aspects of your trading that are holding you back from consistent profitability.

There is one very telling comment you make in your letter. You express an ill feeling upon the prospect of going back to house painting. You are most likely describing a fear. This emotion may not be obvious at the surface. But I assure you, it affects your decision-making in trading.

A suggestion I often make to traders is to build a list of positive personal traits. Start out each day reviewing the list, whether in the morning shower, commuting to the office or in a meditation. Then when you're feeling threatened by the difficulties of trading, you will be less likely to be overtaken by fear because you have a stronger sense of self. The key is to disengage the link between trading and how you identify yourself.

The fact that you are a good house painter is a positive part of who you are. I encourage you to look at that and other aspects of yourself that you might be inappropriately labeling as a negative. In your case, until you can accept that you someday may again paint houses, it's likely the fear of it will keep you from succeeding in trading.

Dear Slim:

I have heard that a number of trading chat rooms exist for futures traders. What is your opinion on the benefits they might offer futures traders?

—Jason L., via e-mail

Dear Jason,

There are quite a number of financial-chat rooms on the Internet. In fact, you can pick the most obscure topic related to stocks, futures or options, and it is sure to have a forum, list serve or chat room. The most common chats seem to be those related to day trading stocks or index futures. However, there are a very limited number of live chats that are commodity specific.

I find the best chat rooms to be the ones offered on the websites of brokerage houses or trading firms. They usually have regularly scheduled guests that talk on specific topics. They also offer teleclasses. TFC Commodity Charts has a lively forum and a live chat. Also, some of the Internet portals, like Yahoo Finance and MSN, also have decent chats. But discussions in these rooms are more often about general financial topics, rather than about commodities.

The motivation to hosting a chat, of course, is to attract people to their sites in order to build lead lists and to sell their services. So once you've visited these sites, expect to start getting their advertisements. A lot of these companies must fold up quickly. I find it quite frustrating that a high percentage of links to chat rooms are dead links. Many of the chat rooms are attended by just a few people, mostly novices, and can be quite boring. Another downside is that some participants are just there to tout their positions. Finding a chat that matches your interests may take a bit of surfing. The effort will be probably be worth it, though, if you just make a few new online friends.

Dear Slim:

How important are trading volume indicators in technical analysis programs in determining market behavior? It has always been my belief that increased trading volume may indicate crowd mentality, which may not be the right time to pile into a trade. Do you agree with this premise?

—Carol B., Carol Stream, IL

Dear Carol,

It is true; an increase in trading volume does usually indicate "crowd mentality." However, that is not necessarily a bad thing. A volume spike might be signaling that it's exactly the right time to enter a trade.

I find the best times to enter a trade, based on an increase in volume, are when it accompanies another signal. Often when a chart breaks through the neckline of a head and shoulders pattern, a huge rush of volume confirms the move. Another pattern that consistently works well with an increase in volume is a "gap" or "break-away gap." Look for this pattern most often on a daily chart when a pre-opening news item causes a stock or commodity to break out of a trading range or reverse a trend.

Notice on the Broadcom Corp (BRCM) daily chart below, the two biggest volume days are in November and January. The November volume spike was at the end of a four-week rally. In this case traders/investors scrambled to buy the stock causing an "exhaustion" gap. Probably, many of the buyers were shorts that had to cover. The following day was the high of the move, meaning that buyers finally got their fill. In January, the volume spike came on a gap down day. As you can see, the stock has not been able to recover back to that level. So, going with the crowd on the November day would have been a big mistake. Going with the crowd in January would have been the right trade.



BRCM Daily Chart Courtesy of BigCharts.com

Another interesting tool, available on advanced charting services, is a "candle volume" chart. This is a unique candlestick chart in which the bars widen and narrow as volume increases and diminishes. Whatever tool you use, the most important aspect to consider when using volume in trading is when the volume has occurred. If you come to the party too late, you'll probably get in trouble.

Dear Slim:

Prior to getting interested in futures, I was a stock investor in earnest. The buy-and-hold belief that I held over the last several years has been a failure, not only for me but for millions of Americans. As a novice futures trader (trading currencies and the Dow mini-contract), I'm currently having a harder time pulling the trigger on trades, especially on entering a trade. What signals a good time to get into the market? I'm sure this is not unusual, but if you've had the same experience, can you tell me what you do to overcome it? —Bill E., via e-mail

Dear Bill,

One of the great challenges for traders is adapting to changes in the marketplace. Your earlier experience was that of a long-term holder. Now, as a trader, you are in an entirely different paradigm. So not only do you have to adjust to a huge change in the market, but you must adjust to an entirely different approach to the market. No wonder you are having trouble "pulling the trigger."

It will be helpful for you to look at your risk parameters and trade objectives. If you are trading too big or nervously maneuvering positions, it will be hard for you to discover your comfortable holding period and trading style. The length of your holding period will determine which signals you use to find trade entries. A five-minute stochastics won't be of much value to a trader that is comfortable holding a trade for several days. More likely you will be looking at hourly and daily statistics and charts.

Before you enter a trade, ask yourself, "What is the objective of this trade? How much do I intend to risk? How long do I

intend to hold this trade? How will I know when I'm wrong? Do I need to use a stop-loss?" This will give you clarity and confidence that you will not hurt yourself if the trade is a loser. After you do this for some time, you will feel less anxiety when entering a trade. You will feel more in control. Also, you'll get a better sense of your trading style and which indicators to use when analyzing the market.

I think one of the safest ways to enter a market comes when there is a clear trend, then the market pauses or consolidates, and then resumes the primary trend. I use multiple indicators to find these trades – for instance, assuming the daily chart is in a rising pattern (higher highs and higher lows). Also, the RSI (Relative Strength Index) and stochastics are rising. The market goes into a sideways flag, pennant or some other consolidation pattern. The 60-minute chart is pulling back,

but holding above the previous significant low. When the 15-minute stochastics gets oversold, I make a long-side entry. At this point, some of the risk is out of the trade, because the market has already retraced part of the previous rally. Once the market resumes upward and breaks out of the consolidation pattern, I add to the long position and attempt to maximize the trade.

What I have described here is a trend-following model. Since the breakdown of the bull market in the middle of 2001, I have found the market to be very unforgiving. When there is a lot of action in the markets, you can make a mistake and the market lets you out. No more! The daily and weekly ranges have narrowed. So it's very important to try to stay with the trend. Then the forces of the marketplace will be less likely to scare you out of a trade.

