

ASK SLIM

I'll share a quick history of my trading career and let you decide. I've been a trader for 31 years. My trading career began in 1974, at 24 years of age, on the Chicago Board Options Exchange (CBOE). Over the 17 years I was a member of the CBOE, I traded in nearly every pit on that floor. Much of that time was spent in the chaotic OEX pit. Over the years I was a member of the Chicago Mercantile Exchange (CME) and the Chicago Board of Trade (CBOT). I have traded "off the floor" since 1984.

In this column, I will answer your questions on the technical and psychological aspects of trading and trading methodologies. Oh, and the next question would be, why the name "Slim?" My badge on the CBOE was "SLM" (Steven L. Miller). Other traders gave me that nickname on my first day of trading, back in 1974. So, ask Slim!



Dear Slim,

This year the stock market was down about three percent in January. I have heard a lot of talk about the "January Barometer." I hear that it works better on the up years than on the down years. Do you have any comment on the overall value of this indicator? Would you make investment decisions based on it?

—Gary M., Arlington Heights, IL

Dear Gary,

The "January Barometer," credited to Yale Hirsch in 1972 (Stock Trader's Almanac), indicates that "how January goes, so goes the year." I also have heard commentary questioning the reliability of this indicator. Thus I spent some time reviewing the charts for the last 100 or so years. The majority of years began strongly as the flow of new money came quickly into the markets, but 20 Januarys started out with significant declines. Only a couple of the sharp January drops had quick recoveries (1955-1965, for example), which seemed to save the year. Eerily, in most of the years with bad Januarys, the stock market seemed to have some knowledge of a negative event that was to come later in the year.

The following is a list of the years with significant declines in January and what followed that year, including important news events that affected the stock market. Credit goes to "Dow Theory Letters" for part of this information from a chart book they published more than 25 years ago.

1907: The spring brought what is infamously known as the "Panic of 1907." A run on the banks brought a market collapse, with the Dow losing 25 percent of its value.

1910: Haley's Comet brings talk of doomsday and the stock market falls hard into mid-summer, losing 18.5 percent.

1913: Taxes! The 16th Amendment coincides with an 18-percent decline into June.

1917: U.S. enters WWI, and the market declines big all year – Dow down 37 percent.

1920: Down all year, with GM in big trouble losing two-thirds of its value. Dow loses 40 percent for the year.

1939: Britain and France join the war to defend Poland. The market breaks 20 percent in March-April, only to recover late in the year.

1940: The Germans blitz the French border. Stock market crashes 40 percent into May.

1942: Britain surrenders Singapore and Bataan surrenders. The auto companies stop making cars to make war equipment. The stock market again breaks big into spring, with losses of 18 percent, and recovers late in year.

1955: This was one of the rare years that January was down big, but immediately reversed upward to have a big year.

1956: A big down January brings a wild year with four moves up and down of more than 20 percent each.

1957: Another big drop in January sets a 20-percent crash in the fall in front of a big recession.

1960: U2 plane shot down. Cuba seizes oil refineries. Market makes an October low, down around 20 percent.

1962: A drop in January sets up a 27-percent crash into the spring as Kennedy confronts the steel industry on price increases.

1968: Market drops huge in January and February, but recovers all year despite assassinations of Martin Luther King, Jr. and Robert Kennedy.

1970: Nixon's State of the Union address brings disappointment and market cracks. Then in April, U.S. troops enter Cambodia. Dow falls from 811 to 631, bottoming in the summer.

1973: January starts bear market. Watergate! Gold soars. Interest rates move up sharply. The stock market loses 20 percent into the summer, recovers three-quarters of the loss by the fall and collapses to new lows in November.

1974: The bear market is in full force. The prime rate rises above 11 percent, a record. Nixon resigns! The stock market drops 45 percent from all-time high made 20 months earlier.

1978: A very bad January and February see a great rally into the fall, with a crash late in the year accompanying riots in Iran. The Shah is on the way out.

1984: A January break sets up the market for a 12-percent decline into July. A strong late-year rally brings only small losses for the year.

2000: A huge January downside reversal on the charts sets up the year of the "dot.bomb." The bull market peaks in March, but big declines don't hit until December as the tech bubble bursts. Decline lasts until 2002 with the NASDAQ losing 80 percent of its value.

As seen, most of the big down Januaries came in front of eventful years, which at some point had very large declines. I would say, though, that despite this fact some years did have rebounds; the January Barometer is credible on down years. So something is probably in store for us this year, and it likely won't be pretty. Will it be the dollar, rising oil prices, a bond-market crash, the U.S. entering a war with Iran or a terrorist attack that triggers a big decline? Whichever, based on this history, the odds are that the stock market will see a swoon this year that will bring a loss nearing 18 percent, possibly more. Why? Because even in the best of the worst years (when January was down), the market at some point in the year dropped between 18 and 27 percent. We started the year with the Dow at 10,787. An 18-percent loss would bring the index down to 8,845. Ouch!

Dear Slim,

I have been trading stocks for a while now and am considering trading E-mini futures. What are the things (pros and cons) I'd need to be aware of before making this transition?

—C.S., Princeton, NJ

Dear C.S.,

I have received a number of letters from traders who have attempted the transition from stock trading to index futures, with most expressing frustration. It's not that there is a great difference in the analysis of these markets; charts are charts. It's more that the relatively high volatility inherent in the S&P market can be tough to handle – especially for traders used to trading average beta stocks. To put it another way, the difference between trading stocks and E-mini S&P futures is like the difference between having a pet cat and a pet tiger. One will nip your finger, and the other can take your head off.

With that in mind, there are several factors to consider when switching from trading stocks to S&Ps. Stocks can be traded part-time or as a hobby. When you are actively trading S&Ps, it is hard to take a bathroom break. So make sure you can make the proper time commitment. Next, your method and style has to match your personality. Trading index futures takes quick thinking and quicker reactions. If you are a person who analyzes and reanalyzes before entering or exiting a trade, S&Ps might not be your best market. There also is a greater risk that emotional triggers will be hit when trading S&Ps. So define a trading discipline that reduces the chance of fear coming into your trading. In this regard, keep your account well funded, rejecting favorable day-trading margins offered by many commodity firms. **SFO**



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