

# 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,*

*Could you please explain program trading—how it originated and how it affects chart patterns? It is said that 70% of all trades (in the S&P 500) are related to programs. Is there a way for a small trader to anticipate and participate in program trading?*

*With many thanks.*

*-George S, via email*

Dear George,

Program trading is the simultaneous buying or selling of a portfolio of stocks, usually 15 or more. It is normally done to create a basket of stocks that exactly matches or has a high correlation to a stock index. This trading strategy is most commonly executed when a computer program identifies a derivative that is priced out of line, offering a small "edge" in an arbitrage situation. Program trading was born along with the derivatives markets and development of related computer programs.

Here is an example; a large order comes into OIH (Oil Service Holders) options to buy calls. This pushes the call prices above and put prices below price model valuations, alerting computers to a mispricing. The computer program calculates commissions, carrying costs and dividends. Then it alerts the trader it is advantageous to buy the eighteen underlying stocks in the OIH index, sell the overpriced calls and buy underpriced puts. With the push of a button, the computer executes the trades, creating a neutral position with a built-in profit if held to option expiration.

As you can see, this is a complex transaction, which takes a very significant amount of capital to execute. Imagine if the trade happens when S&P futures get priced out of line, trading 500 stocks instead of the 18 described in the trade above. Thus, it is usually only undertaken by institutional traders. The best thing a smaller trader can do is to use charts to identify the momentum created by the program trade and then go with the flow.

*Dear Slim,*

*I am a beginning stock trader and could use some advice. I have two questions. What is the technique for determining a target price on a stock trade? How do I determine what is a better fit for me, day trading or position trading?*

*Thank you,*

*-Frank H., Winston-Salem, NC, via email*

Dear Frank,

As in all areas of futures and securities trading, there are two general categories of analysis determining the price objective for a stock. Fundamental analysis would have you compare current price to earnings ratio (P/E), price to cash flow, book value, growth rates and other factors of similar stocks to extrapolate a valuation for your stock. So an analyst might take a stock with a P/E of 15 and a growth rate of 25 percent and compare it to similar stocks that have 20 P/Es. That would suggest a price target of 33 percent higher than present value.

Technical analysis, which most active traders use for targeting a stock, uses chart patterns to project where a stock might go. Some tools that are used are "channels" or continuation patterns like "pennants," "flags" and "triangles." For example, XYZ stock just rose from 33 to 37 and is now forming a triangle. Once the stock moves out of the consolidation pattern, the next move should be similar to the previous advance, adding four points from the level of the breakout.

Whichever way you choose to project a price for a stock, know that conditions change and these tools only work some of the time. Use good risk management to keep out of trouble.

Generally, if you have a good amount of patience, significant capital and a high risk tolerance, you may be more suited to position trading (holding trades overnight; for one day or many weeks). If you tend to need instant gratification and are relatively low in capital, which would prevent you from holding onto positions overnight, and/or you have a low risk tolerance, you are probably more suited to day trading.

Try both styles and test what is the most comfortable and most profitable. Your gut will help you make the choice.

*Dear Slim,*

*Can you please explain the "Trin"? How is this index calculated and how should it be used?*

*-Alec H, Chicago, via email*

Dear Alec,

This market indicator was created by Richard Arms. Hence, it is also known as the "Arms

Index". It was developed to gauge stock market strength and signal when the market was overbought or oversold.

The Trin is a ratio of two ratios. It is calculated by dividing the number of "up" issues by the number of "down" issues, and dividing that number by the up volume divided by the down volume ((#up issues/#down issues)/(up volume/down volume)). Most data vendors supply the Trin, so you don't have to do the calculations.

It is said that when the Trin is over 1.00 the market is bullish and below 1.00 is bearish. Fluctuations are much wider, however. On days when the stock market is very strong and volume is very concentrated in advancing stocks, the Trin gets as low as 40. On very weak days, with volume pouring into declining stocks, the Trin moves well over 2.00.

The most common way to use the Trin is to calculate the 10-day moving average and wait for overbought or oversold conditions. Traditionally, the market was oversold when the 10-day MA of the Trin neared 130 and overbought near 80. In the past 5-month rally, however, the 10-day Trin stayed mostly between 100 and 115, dipping once to 95, an amazingly narrow range. Being the Trin never got overbought by this measure, it signified that the stock market was correcting internally, feeding the astounding rally.

When you use the Trin as suggested above, you will be entering a trade counter to a very strong market trend. So enter with a partial position, preparing to add to positions as market conditions warrant.

*Dear Slim,*

*I am very concerned about the environment and would like to invest in companies that are environmentally conscious. Can you let me know how I can locate these types of investments? Are there mutual funds that only buy companies that are environmentally responsible?*

*Thank you very much,  
-Erica D, vial email*

Dear Erica,

There are many ways you can participate in what's now called "green investing," whether by buying stocks of companies involved in alternative energy resources or investing in mutual funds that only invest in companies that produce products acceptable under their socially-conscious models.

You can do your own screening, avoiding companies that do not meet your standards of environmental or social consciousness. According to [www.soyouwanna.com](http://www.soyouwanna.com), the most commonly screened issues are tobacco, gambling, alcohol, defense, environmental record, human rights practices, labor issues, abortion and animal rights.

You can also search the internet under "green investing" and you will find many mutual funds in this category. You'll have to discover on your own which funds have an acceptable track record of returns and the level of purity of their green investing.

Another aid is the GreenMoney Journal, [www.greenmoneyjournal.com](http://www.greenmoneyjournal.com), an online guide to socially responsible investing. ■

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SEND ME YOUR  
QUESTIONS!  
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