

# 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,

I see ads all the time touting the performance of various trading systems. For instance, 62 percent winners, \$1420 average winning trade, \$770 average losing trade, \$5690 maximum drawdown. How does one manage one's trades using this information? How do you protect yourself if future performance is less robust?

Thanks,

-Leon M., via email

Dear Leon,

I see this type of ad all of the time. The best advice I can give you, if you spend your money on trading signals from others, is to evaluate the trades on your own and see if they make sense based on your analysis. And don't count on them to tell you when you are in trouble with these trades. Maintain your disciplines on trading unit and maximum loss rule.

Dear Slim,

In November you answered a question for a reader who was day trading crude oil with mixed success. You showed a 15-minute chart with a momentum oscillator. Can you tell me what oscillator that is and the settings on it?

Thanks,

-Bob K, via email

Dear Bob,

The momentum oscillator is like an MACD (Moving Average Convergence-Divergence). It identifies when a trend is in force and when it gets overbought or oversold. I use settings of 8 and 13, with an offset of 5.

Slim's Stock Market Predictions for 2007

After timing the stock market very well the previous three years, my predictions for 2006 were way off the mark. I had expected a rise in 10-year notes to 5.5 percent, a slowing economy and a real estate bust to cause the stock market to go into a bear phase. My anticipated high for the DJIA was 11,375, with a decline taking the market down to 8303 by November.

My economic analysis was right, as nearly all of the expected underlying factors came true. However, investors disregarded all of the negatives, barely flinching at a summer high in crude oil of near \$80 a barrel. After a mild 8.5 percent springtime correction, the stock market rallied steadily from its June low, with the Dow powering over 12,300 into late November (the time of this writing).

In the coming year, some very significant technical factors will come into play. The bull market is now 49 months long, mature by historical standards. In the past century, there were four bull markets that had similar patterns. The bull market of 1953-1957 lasted 47 months, followed by a three-month bear that gave up 19 percent. The 1957-1962 bull extended to 50 months, which brought a 27 percent, six-month crack. The 1982-1987 bull rose an astounding 61 months before the infamous crash of '87 stunned investors, losing 40 percent in two months, with most of the loss coming in a two-day crash. And the 1994-1998 bull climbed for 50 months, only to suffer a three-month, 17 percent bear.

As you can see, these very long bull markets were all followed by a short and very sharp bear market. If history repeats, there is a strong likelihood that today's bull market will end with a similar result.

There is one similarity to 1987 in the present situation that is very worth noting. The bull that began in 1982 was accompanied by the birth of index futures. When the '87 correction hit, it was exacerbated by a panic in S&P futures. Sellers pushed these contracts to big discounts trying to protect portfolios, which lifted put option contracts to unrealistic levels. This created a snowball effect as program trades caused waves selling in stocks and traders moved to take advantage of these extreme divergences.

Today's bull market has come with the birth of ETFs. These are exchange traded funds which mirror a basket of stocks, creating an index. There are now almost 300 of these funds, which, it is said, will reach assets of over \$1 trillion in 2007. When a real correction hits—and it always does—will these investments worsen the drop, as in '87, as investors bail out?

You might argue that this market is clearly very strong. As I said above, nothing has shaken investor confidence; there hasn't been a single 10 percent correction in the past four years and volatility is at multi-decade lows. There are, however, a multitude of factors that could be the impetus for this overdue bear to hit.

Here are my top five events that could bring back the bear. 1. The real estate bust surprises the analysts and worsens, causing consumer spending to slow down severely, pushing the economy into recession. 2. The dollar crashes, as a trade war evolves due to Democratic protectionism, causing interest rates to spike. 3. Democrats impose a windfall profits tax on oil companies. 4. Japan raises rates, causing a liquidation of U.S. assets in an unwinding of the yen carry trade. 5. The crisis in the Middle East brings the U.S to the brink of war with Iran.

I have made a case here for a significant decline in the stock market sometime in 2007. Because in January, this bull will be 51 months old, odds are high that we'll see a significant top in the first half with the highs only slightly above the year's close. Based on the historical norm, the stock market should decline between 14 percent and 27 percent. I will call for a drop of 14 percent for the broad indexes before summer, which would bring the S&P 500 down to support at 1220 and the DJIA down to 10,650.

Sure, you're thinking, Slim must be a "permabear." He was bearish last year, and got it wrong, and he's bearish now. Think again. Last year I expected the stock market to decline after what had been a sub-standard bull market, indicating that the market was still in a secular bearish condition which began in 2000. However, the history I shared above about the four similar bull markets all came during secular bulls. That made the bear markets brief, with the following rallies all going to new highs.

Because this bull has run so long, odds are high that the stock market is in a new secular bull market and that the coming bear will be brief. The second half of the year should see a new cyclical bull, lead by the revived technology sector.

I expect the stock market to close 2007 at or near significant all time highs, with the S&P 500 having made a high at 1512 and the peak in the DJIA 13,100. The index to watch, however, will be the tech-heavy NASDAQ 100, which I see gaining 33 percent to resistance at 2337. ■

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SEND ME YOUR  
QUESTIONS!  
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