

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 am contemplating trading full-time in the near future. I've been an active investor over the past 10 years, and I think I have enough capital to try to make the jump.

I am contemplating following a strategy that is a combination of selling condor spreads and trading futures short-term/intraday. For example, I have the following condor spread: Short SPX May 1390-1400 put vertical spread and short May 1520-1530 call vertical spread. I would receive a net credit that I get to keep if the S&P final settlement ends up in between 1400 and 1520. Obviously, there is a great deal of risk involved if the market moves sharply in one direction or the other.

To combat that risk, I would short-term trade E-minis to take advantage if it trends sharply in one direction while closing out the side of the spread that the market is moving against. If the S&P remains range bound, my E-mini trading would be limited but I would keep the full credit I received from the option spreads.

Do you think this is a viable strategy? Outside of a huge overnight move in one direction (most likely down since down moves tend to be sharper than up moves), I don't see a great deal of risk if proper money management techniques are followed. I can see how each part of this can be risky when done individually.

The condor spreads require a sideways market for the time decay to take effect while trading E-minis requires volatility for trading opportunities. But when done in combination, the risks of each part seem to offset each other to a large degree and would allow a potential profit on both parts of the trade.

In a way, it's kind of like delta hedging to keep my net delta small while taking advantage of the time decay. At a minimum, the futures trading can mitigate any of the losses suffered on the short spreads. I am curious what you think of the viability of this.

By the way, I am a huge fan of yours, and I hope you continue to write about interesting topics.

Regards,

-DJL

Dear DJL,

I can see you have a very good understanding of the options and futures markets. Your strategy looks good in theory. However, in practice you may find it difficult to execute.

As you properly explained, condors need a sideways trading market. When the underlying security threatens to move out of your profitable range, proper risk management calls for an adjustment. Your method is to short-term trade the S&P futures to offset the risk.

Here is the problem: You will be trading futures because the condor is a threat, not because it is a good entry. Furthermore, you will probably be buying or selling the futures after the move is quite mature, on a short-term basis. If the market retraces, you'll be threatened by the futures position, which you are only day trading. And you will have not adjusted the condor, which is a longer-term trade. You'll be taking a low-risk position and making it higher risk. You will have to be very nimble to make this work.

What you will be doing is taking two very different trading methods and styles, combining them and contaminating each one.

Often, traders find it challenging to trade multiple strategies. If you wish to trade both S&P condors and futures, I suggest you have separate trade entry, exit and risk management rules for each strategy. Then, if the condor goes badly, you only offset with futures if you have a reason to believe you cannot trade in the option market because of unusual circumstances. Otherwise, make the proper adjustment to the delta of your option position or close it out because it has reached your stop-loss rule.

Slim,

Am I naïve to believe it is possible to develop a sixth sense for the market? If, you agree it is possible, what are a few steps or disciplines one might use to begin to develop this intuitive sense?

Thanks,

-J.W. Masters, Greensboro, NC.

Dear J.W.,

I believe all people have within them an intuitive sense for trading the markets. However, I don't see it as a sixth sense, like ESP. It is more like when a race car driver spontaneously accelerates into a gap, knowing it was the right opportunity to move up a position. It came from his experience, driving thousands and thousands of laps.

For traders, intuition is developed after experiencing the market for hundreds or thousands of days. For some, it comes from going over the charts day after day for years. Then, when the data comes off

the screen, traders react, as if they knew what was happening in advance. Really, they are reacting to their minds processing the present data and extrapolating a high probability trade based on what they have learned from the past. It happens instantaneously. That's how the intuitive sense works.

The question to ask is what gets in the way of freeing this intuition? Many traders struggle to "feel" the market because of the distraction of all the noise coming from the market, their environments or from their own heads. The challenge is to clear a path to free your intuition.

Here are a few tips. Allow yourself the time necessary to experience the multitude of market situations. Keep your trade size appropriate to your capital, so you won't be threatened as the market bounces up and down and you can keep your focus. Avoid distractions in your trading environment, such as many phone calls, interruptions from other traders, screaming kids or surfing the net.

What I have experienced as the greatest obstacle to trading intuitively is the chatter in our own heads. Do I enter this trade now or should I wait? Should I take a profit? Should I add on to this winner? What if I lose? What will my spouse think if I say how much I lost? How will I pay the mortgage or my child's college education? It goes on and on. All of these fear-based ruminations make it impossible for the intuitive process to work.

So the best tip I can give you is to do everything you can to clear your head of anything that doesn't relate to trading. Know that if anything goes wrong with your trading decisions, you will survive. Then, with experience and obstacles removed, when you turn on the screen, you'll "feel the force."

Dear Slim,

I have two questions for you: How does one get access to Level II information and participate in Level III? How can I trade the foreign markets, overnight, when the markets are closed in the U.S.?

Thank you very much,

-Teri P., Michigan

Dear Teri,

Level I is a quote system that provides real-time viewing of stocks listed on the NASDAQ, showing only the highest bid and lowest offer. Level II shows the depth of the market, providing a view of bids and offers at all levels. Level III is for NASDAQ-listed firms, which gives a trader the right to be a market maker, providing two-sided markets and executing orders.

The only way for U.S. traders to participate in overnight foreign markets is with a variety of available futures contracts. The U.K. stock market can be traded with FTSE 100 Index futures and the German market with the DAX 50 futures. Another choice to participate in Euro markets is STOXX 50 futures, which track a basket of some of the world's top hi-cap stocks. To trade Asia, you have a choice of Japanese Nikkei futures or Hong Kong's Hang Seng futures.

Of course, if there is a big move overseas, often U.S. index futures respond to world markets. Teri, don't you sleep at night?

Dear Slim,

I am having difficulty locating data on put and call option volume and open interest for major commodities. These figures used to be published daily in The Wall Street Journal, but they are no longer available there. I would prefer weekly data for each individual commodity: total call volume and open interest, and total put volume and open interest.

Can you help me in this regard?

-Roy W.

Dear Roy,

The information age has brought a changing landscape for print magazines, necessitating many cost-saving measures. Barron's has moved this free information to its online version at www.online.barrons.com. ■

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