

# 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,*

*When I started trading the S&P market, we had 25- to 40-point ranges each day. Now it's hard to find two days a week with moves over 10 points. What happened to volatility?*

*-Dave, via e-mail*

Dear Dave,

The S&P market, except for the days following 9/11, has not had that kind of volatility for more than a decade. Volatility, as measured by the VIX (CBOE Volatility Index), is the lowest on record.

Several factors are causing low volatility. The stock market has been rising since the bear market low in October 2002. It makes this bull market quite mature. Towards the end of a bull market, it gets harder to make upside progress, as the bullish forces meet resistance. What happens is that a compression occurs as these two opposing forces meet. That creates smaller and smaller ranges.

Also, to get wider daily ranges in the market, there must be some downside action. There have been only small corrections over the past three years. Bear markets fall much harder as fear sets in, followed by sharp rebounds that make for much wider ranges. The VIX is a measure of fear. Readings of 10 to 13, like we have seen through the past summer, indicate there is great complacency, warning of trouble ahead. Once the bear takes hold, the market will start to have wider swings again, bringing 20-point daily ranges and greater volatility in the S&Ps. That will only be good news for those of us with experience in holding one of those snarling bears by the tail.

*Dear Slim,*

*I am a conservative investor who would like to auto trade the E-mini S&P futures market and have set aside funds for this. However, at present I personally do not have the time or the expertise to trade successfully. I would not want to hold positions overnight, along with every trade having a predetermined stop-loss to avoid margin calls. I've seen firms advertised that generate buy and sell signals for the E-minis. Are you aware of reputable and successful firms that generate these trading buy and sell signals?*

*-Lee M., via e-mail*

Dear Lee,

I receive numerous questions about software and trading systems for stocks, indexes and futures, and there's frustration at the lack of information on the reliability of these systems. Some have tried buying a system and struggled to use it successfully. I have commented on some systems in this column, but it would be impossible to do justice to the huge number of trading systems out there. There is a great resource on the Internet for sifting through many of the available trading systems. Attain Capital Management has a website (register free at [www.systemrank.com](http://www.systemrank.com)) that lists hundreds of systems and offers extensive sorting capabilities. General categories are strategy type, risk, system cost and markets traded. They also offer commentary on trading systems, backtesting with "hypothetical results," performance and more.

*Dear Slim,*

*How do you set Fibonacci retracements? Which are the zero-percent and 100-percent points? I want to avoid ambiguity when plotting support and resistance. Also, which candlestick patterns should be explored to determine possible stopping points of the retracement?*

*-H.S.G., Baton Rouge, LA*

Dear H.S.G,

Plot Fibonacci numbers on an uptrend by setting the zero number at the lowest point and the 100-percent number at the peak. For a downtrend, do the opposite. The software program should place five horizontal lines between the high and low, plotting out the 23.6%, 38.2%, 50%, 61.8% and 76.4% retracement points.

Your question about using candlestick patterns with Fibs is great, because you have to figure out which of these retracement levels will be the stopping point in the counter-trend move. I use the patterns that warn of trend change. The most reliable candlestick patterns on the bullish side are hammers, shooting stars, morning stars, engulfing patterns and piercing patterns. Bearish patterns include shooting stars, evening stars, dark cloud covers and engulfing patterns.

*Dear Slim,*

*An article in SFO's August 2005 issue caught my attention and left me puzzled. The author suggested using a put option in place of a stop to cover a long futures position. Why not simply buy a call and forget about the futures position and the put altogether? What have I missed? Are there advantages to doing it the way the article suggested?*

*—Richard K, via e-mail*

Dear Richard,

Andy McComas' article talks about the risks of using stops in a choppy, sideways market, especially for beginners. It compares two traders in the oat market. "Trader A" uses stops to control

risk, gets stopped out in a series of long-side trades and eventually misses the up move. "Trader B" hedges the long trade with a put option, which helps avoid getting taken out of the trade by the market volatility.

Andy's article was meant to compare the two strategies based on trading the actual futures. He makes an excellent point, as the hedge position takes the emotional stress out of the trade, increasing odds that the trader will be in the position when the price of the commodity finally moves his way.

If you are long a future and long a put, you have created a "synthetic" call. This position is essentially the same as buying a call. In fact, because there is a margin requirement on the futures, the hedge position may have a greater out-of-pocket cost than buying the call outright. Also, there are double commissions. So buying a call might be a better choice.

The one situation that could make buying a put against a long futures position a better choice than buying the call outright is when you "leg" into the hedge. Assuming the same choppy market, you buy the futures on a dip, and on an upward bounce you buy the put option – using market "noise" to your advantage. Your hedge has a lower cost. Of course, you will take more risk to get into the trade than if you executed both sides of the hedge simultaneously. **SFO**

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SEND ME YOUR  
QUESTIONS!  
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