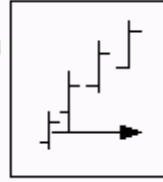


TUTORIALS IN APPLIED TECHNICAL ANALYSIS



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The Australian Internet Trading Weekly

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Weekly for Monday April 21, 2003 Based on Wednesday's Close 19 pages


With contributions from S Nicholas, P Rak

Guppy Trading Essentials Chart pak, Metastock, Ezy Charts & SuperCharts. Data from JustData, Paritech, MarketCast & Keyquotes.

Stocks mentioned in this issue

UEL, NBL, PTD, UNI, XJO,
DUI, AMH, AFL, CPK, MDE,
LOD, IDT

Note. The more computer icons

 appearing after a section heading, the more advanced the material.

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LOOKING FOR AN EXCUSE TO EXIT

SUBJECT SUMMARY

GREED AND THE EXIT

Greed acts most dangerously in the exit. It is greed that keeps the trader in deteriorating trades - he hopes prices will climb back to old levels so he can exit. It is greed that keeps him in losing trades - hoping prices will climb back to break even after his stop loss has been passed.

Defining the exit conditions helps control greed. The best exit conditions are based on a set financial return from the trade. The worst are open ended positions that depend on a set of indicator signals. Signals invariably given after the most recent high Here the exit is made more difficult because the trader compares what could have been with what is. So he waits, often with disastrous results.

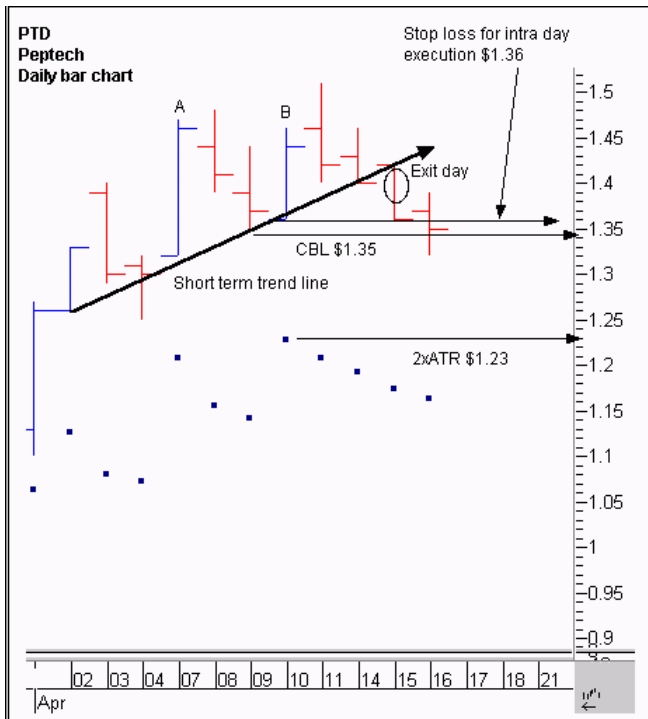
Last week we noted concerns about the failure of the case study PTD trade to move in the way we expect bullish flags to develop. The case study PTD trade is an example of a bullish flag. In this type of trade we expect to see a rapid breakout from the top of the flag and a fast move towards the achievement of our price objectives. Pattern trades are expected to move in a consistent fashion. When they don't we tighten the stop loss conditions to protect our profits.

In short, we are looking for an excuse to get out at the best possible price. Not only do we have profit at risk, but the trade is failing to develop as we anticipated. It is a time to cut our losses, or in this case, maximize our profits, and abandon the trade.

We monitor the way price moves. The flag pattern is a bullish breakout. We expect to see strong up moves once the rise starts. Bar A is an example of this type of strong up move. The next two days are down days. The strength of the up move has faltered.

We have a choice of five stop loss techniques.

- The 2xATR, which lags behind the price action. This is set at \$1.23. One option here is to change the calculation to 1xATR to move the stop closer to the action. Remember, we are looking for an excuse to exit.



- The count back line. This is closer to the price action, but will still not lock in good profits. We have to wait too long before the signal is generated. We can tighten the application by acting on any intraday trade below the CBL value. This is set at \$1.35.
- Using the low of the most recent bullish day – displayed as blue bar B. This is when the close is higher than the open. This helps to capture any decline in bullish sentiment. This is set at \$1.36.
- Define the very short term trend with a straight edge trend line. This captures the trend development after the initial breakout. Any intraday trade below this value triggers an exit.

We are looking for an excuse to exit because the trade has lost momentum.

- Use gut feel and get out at any price above the previous high at \$1.48. This is a tempting strategy that works best on a retrospective chart. We do not apply it to this trade. However, it is a valid strategy when faced with a momentum trade that has stalled in its development. Rather than being smart and complicated, at times it may be just better to jump ship when your nerves give out.

Our objective is to set a series of progressively higher stops all based on intraday traded prices. We act when the stop is triggered by an intraday price move.

On Tuesday the market opens with a roar, gapping upwards in a display of bullish strength. PTD opens with a whimper, and then drops. The order lines are full of sell orders. Time to jump ship. If this bullish breakout cannot be lifted by a bullish market then the momentum in this trade has disappeared.

Contingent stop loss order					
Contingency					
Security	If PTD reaches a Last price Less than or equal to				Stop Price (c)
					141
	Start Time	End Time			
	between 10:00 AM and 04:00 PM				
Action					
Volume	Security	Limit Price (c)			
Sell 16000	PTD	at 138			

The first exit signal comes with trades below the value of the straight edge trend line. Our contingent stop order is activated and we get an exit at \$1.40. This is not a clean exit. It is an exit that recognizes that the planned trade was failing so we progressively tighten the stop loss exit points to force an exit at a better price. We implement this by using contingent stop loss orders triggered by intraday price moves. Once

triggered, the sell order is placed 'at market' by setting a sell price below the trigger price. This lower sell order immediately moves to the head of the order line, and is filled by the highest current bid. The risk is that you will end up with a lower exit price, but the advantage is that you have a higher

probability of the order being filled. In a momentum trade where momentum is reversing, getting the order filled and executed is particularly important.

Fortunately, these type of exit conditions do not happen very often. Every trade has the potential to fail to develop as we anticipated. When this happens we need to recognize the change in conditions and develop a new plan to capture the best possible profits. This exit returns a disappointing 11.11%, or \$2,240. It returns the same percentage in the 6 to 21 portfolio, but the dollar return is reduced to \$623.56.

The annual realized return on the case study portfolio trades is lifted to 69.7% since July 1, 2002. This means that \$69,770 has been added to the original nominal \$100,000 of case study capital.

The six to twenty one portfolio started with \$6,000 in November 2002 and has added \$5,241.36 in profit. This is an 87.35% return. When the open profit on the case study UEL trade is included, total return for the period is lifted to 91.45%.



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A SHORT TERM TRADER'S TRAVELING TALE

By Stuart Nicholas

TRADING METHODS

ENTRY AND EXIT RISK

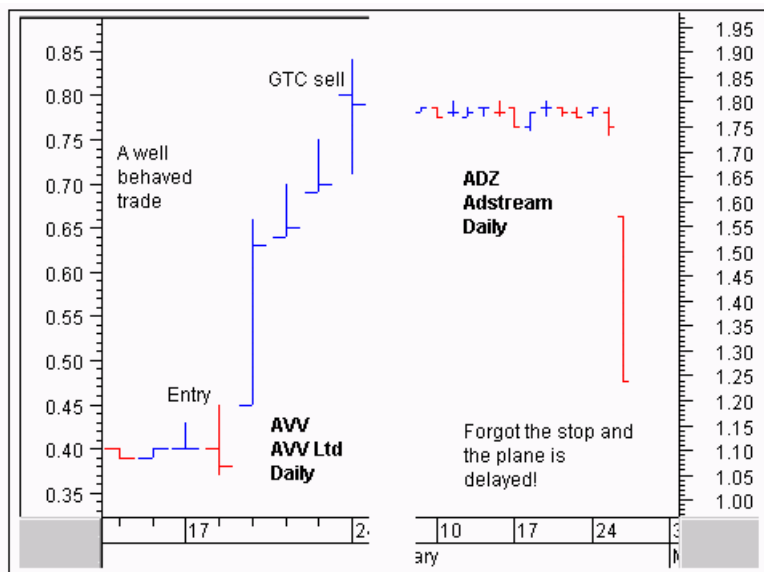
Traders have well established methods for establishing the level of risk when they enter a trade. The stop loss conditions make sure that no more than 2% of trading capital is risked should the planned trade entry turn out to be incorrect. If traders are prepared to risk 2% of trading capital on the entry then it makes sense to risk no more than this in lost profit on the exit. Lost or surrendered profit is calculated by taking the most recent high and using this to calculate the value of the position. The dollar amount at risk on the entry - 2% of total trading capital - is subtracted from this. The result is divided by the number of shares held to give a stop loss or protect profit figure. If prices fall below this figure then an exit is made. This locks in profits before falling prices have time to eat away at them too much.

I am a private trader working from home and living in Hobart, Tasmania. I quite regularly travel to Melbourne by air for short periods of time for various reasons. The flight time terminal to terminal is quoted at a bit over an hour and hence Melbourne city to my Hobart home and vice versa is about a three hour trip, normally allowing travel to occur outside ASX market hours. Major flight delays in either direction are not that common. However, there are exceptions to that rule as any air traveler will know!! Such unexpected problems can make a trader's day rather more difficult than planned or hoped for.

A recent case illustrates the issues very clearly. An overnight trip to Melbourne to see a certain well known rock band ought to have had me back home in Hobart about lunch time the next day, that is not too long after market opening. Unexpected return flight delays one after another finally were sorted after several hours, but my eventual arrival home was not until well after the market closed on that day. I was holding one short term overnight trade from the previous day that had a high probability of being successful. An appropriate stop loss order was in place, as was a profitable sell order at a price suitable for that particular trade.

Arriving at Melbourne airport about market opening time I pondered the price of the stock in question, given that Wall Street had been positive overnight. However as I'm not a member of any 'airline club', I did not have access to an Internet terminal in an executive lounge. Ideally I was keen to monitor that trade and a couple of other possible trades during the whole day and make the most of any opportunity that may arise whilst awaiting the delayed flight. However, that was not possible.

When the first flight delay was announced shortly after



getting to the gate lounge, I was in something of a dilemma. A pocket full of \$2 coins potentially enabled me to use one of the public Internet terminals in the airport gate lounge concourse. However, I did not know if (a) if it would allow the required software to be downloaded from the broker in order to run the trading platform on the terminal and (b) if it was secure. Unfortunately the latter question cannot reasonably be answered by mere mortals!

Sacrificing one coin, twenty minutes of the plentiful unplanned spare time and perhaps my broker login

details, I tested the system. Some minutes later after the surprisingly successful software download the

trading platform came to life and I could monitor the trade in question. The price had gone up significantly and sold at my set price. No problems there - all was well. Right away another issue came to light while I was using the very public terminal - other people watching! I had made sure there was no one in the immediate area while I logged on to my broker in the first place. However subsequently a couple of guys were obviously wondering what I was up to and stood back watching me, despite or perhaps because of my efforts to block the view of the screen. There was no problem overall, but listening to their chat had me both laughing to myself and a little concerned. At the end of the session and just prior to the paid twenty minute time period expiring I made as sure as I could that the login to the broker's web site could not be accessed from any history lists that may have been kept on the terminal and subsequently be publicly accessible.

The above notes are nothing remarkable, but the overall unplanned long delay to the return flight on what was otherwise a short trip did bring home to me the need to always avail myself of all available technology at all points in the transaction process in order to manage trades, whatever the circumstance as well as take great care with security when using terminals in a public area. Next day from the comfort and security of the home office I did change my broker login details!

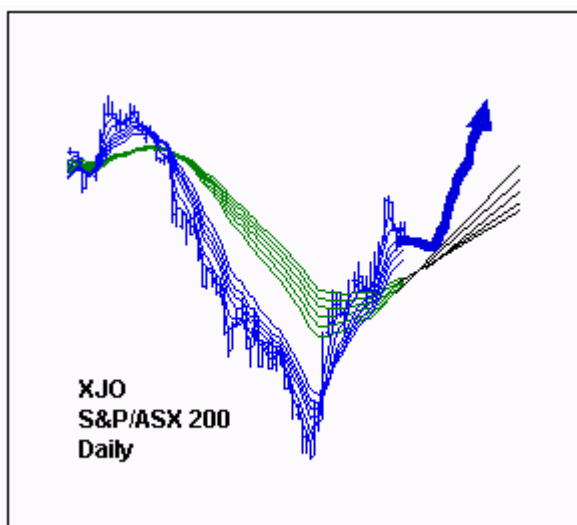


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NEWSLETTER OUTLOOK – A CAUTIOUS BULL



In last weeks XJO notes we observed that the market had succeeded in breaking above the resistance area. This movement has the potential to define the end of the rally and perhaps the start of a new up trend. This sets the scene for a bullish rally running into June when the traditional tax driven sell off is likely to cause a market decline.

The Guppy Multiple Moving Average indicator with the XJO shows the type of recovery behavior that would accompany the setting of a new up trend. We anticipate a pullback in the market as rally highs collapse. The index pullback must find support at the old resistance level if a new up trend is to develop. Traders will pay close attention to the behavior of this pullback. It is the rebound that confirms the increased

potential for a new up trend to develop.

On the MMA display we look for two features. The first is an expansion of the long term group of averages as the short term group of averages collapses. If this new up trend is valid, then we expect to see investors come into the market to take advantage of the temporary drop in prices. This should lead to some expansion of the long term group of averages, as shown by the black lines.

As some traders take profits, other traders will observe the way the investors are reacting. They wait on the sidelines for evidence that investors are buying as prices pullback. Once they observe this, the traders will also start to compete for stock in anticipation of a new up trend. The result is a recovery in the short term group of averages. The potential pattern is shown by the thick blue line.

Joining the rebound gives traders an 8 to 10 week window of opportunity. The potential pullback and rebound provides a range of opportunities in individual stocks. Traders will look for weakness in current trends as a potential rebound point. These can be located using the price oscillator style searches discussed several weeks ago.

Each week we make a choice about the material we include and the subjects we cover. The selection is based on our outlook for the current and coming market. Our objective is to illustrate effective trading strategies that readers can apply to current market conditions. We do not identify recommended individual stocks. We identify opportunities and appropriate trading methods for them. Our outlook is not a forecast. It is a probability framework. Use it as just one part of the other information you are reading about the market. Our summary outlook will be included each week.

NEWSLETTER NOTES

REASONS FOR NOT SUBSCRIBING TO THE NEWSLETTER #6

I want hot tips

“Why don’t you give trading tips like other newsletters?” one trial reader asked recently at the end of his four week free newsletter trial. The answer is simple. Our focus is education. Our objective is to provide readers with information so they can further develop their trading skills. There are many different paths to success in the market and it can be very expensive exploring them on your own.

This newsletter explores many new paths at no cost to the reader. You hear of a new trading techniques, a new twist on an old approach and chances are that we are already exploring it in the newsletter columns. We save you time by developing, testing and adapting the formulas and indicators. We save you money by including real time examples of the techniques in the sample portfolio. This is rigorous paper trading so you get to see what works, what fails, and why.

Hot tips, or a list of stocks to buy, are easy to generate and easy to sell to the gullible. The truth is, any cheap analytical program will give you a list based on conditions as simple or as complex as you like to make them. The real problem is deciding which hot tip represents a real opportunity that suits your preferred trading style. To make that decision you need the knowledge that comes from education and experience. We provide education based on sharing our experience.

Tips are for waiters, not traders. There is only one hot tip in this newsletter and it is this: “Market success is built on education.”

NEWSLETTER CASE STUDIES PORTFOLIO

PORTFOLIO CASE STUDIES - MONEY MANAGEMENT

Starting cash position \$100,000 - no brokerage or slippage 2% of risk = \$2,000

NOTE Entered date is the *newsletter date* which contains the case study discussion.

Stock	Price	Qty	Pur Value	Close	Cur Val
UEL	\$2.930	6,850	\$ 20,071	\$ 3.1500	\$ 21,578
		Newsletter date	27-Jan	Open Profit	1,507.00

Dividend 685.00

Total return 2,192.00

Darvas box Darvas stop loss

Percentage 10.92

plus dividend @ \$0.10 = \$685

Stock	Price	Qty	Pur Value	Close	Cur Val
PTD	\$1.260	16,000	\$ 20,160	\$ 1.4000	\$ 22,400
		Newsletter date	7-Apr	Open Profit	2,240.00

Flag trade starts at top of flag Percentage 11.11

Stock	Price	Qty	Pur Value	Close	Cur Val
NBL	\$1.230	16,300	\$ 20,049	\$ 1.4500	\$ 23,635

	Newsletter date	10-Mar	Open Profit	3,586.00
PO based trade	Trend line stop loss		Dividend .04	652.00
			Total return	4,238.00
			Percentage	21.14

SUMMARY MONEY MANAGEMENT

Close NBL at \$4,238 profit or 21.14% return.

Close PTD at \$2,240 profit or 11.11% return.

Overall profit to date since July 1, 2002 = \$69,770 or 69.7% return on trade equity.

Profit 2001/02 = 71.3% return on trade equity. Profit 2000/01 = 59.2% return on trade equity.

Profit 99/00 = 111.2% return on trade equity. Profit 98/99 = 102% return on trade equity.

Profit 97/98 = 94% return on trade equity. Profit 96/97 = 66.5% return on trade equity.

Direct investing in the stockmarket can result in financial loss.

Historical results are no guarantee of future returns.

SIX TO TWENTY ONE - A CASE STUDY IN AGGRESSIVE GROWTH

Starting cash position \$6,000, Nov 2002. Profits are pyramided.

SPECULATIVE POSITION - starting capital \$2,000

Stock	Price	Qty	Pur Value	Close	Cur Val
PTD	\$1.260	4,454	\$ 5,612	\$ 1.4000	\$ 6,236
	Newsletter date		7-Apr	Open Profit	623.56
Flag trade	starts at top of flag			Percentage	11.11

BLUE CHIP POSITION - starting capital \$4,000

Stock	Price	Qty	Pur Value	Close	Cur Val
UEL	\$2.930	1,564	\$ 4,583	\$ 3.0900	\$ 4,833
	Entered		27-Jan	Open Profit	250.24
				dividend	156.00
				Total return	406.24
				Percentage	8.86

Darvas, add Jan 27

Plus dividend \$0.10 = \$156

SUMMARY - SIX TO TWENTYONE

Starting capital	6,005
Current combined value	11,497
Current profit	5,492
Return %	91.45

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