Trading Entry and Exit Examples
For the Investools Discussion Group
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4/18/09

Several people in the group asked about effectively entering and exiting a trade. This transcript is from a presentation made to the April local Investools' Discussion Group meeting.

Each time I give a presentation I learn more. Presenting gives me the opportunity to review my work in putting a presentation together. It also enables "group synergy." The group always has good questions and suggestions to further enhance my trading.

The charts were created using Tradestation.

This presentation starts by entering a trade at the opportune time. It also shows what happens if we miss the initial trade and what can be done to get in with minimal risk and still participate in the trend.

Finally it suggests day-trading for fun and profit—for those that like action.

SSO Purple Crayon

Jeff Macke of CNBC fame has a concept he calls his purple crayon. When he sees a trend developing he uses a purple crayon to highlight when to enter or exit a trade. He uses a crayon instead of a sharp pencil since the line is not exact—there is some width to it and the associated uncertainty.

Below is a recent market trend on SSO and the purple crayon line. When the price broke above the purple line enter the trade—Buy 100 shares of SSO.

Notice the initial buy was on 3/10/09 at about $16.00 and ran till 4/20/09 at the price of $23.61. Thus yielding an open position of $761 per 100 shares. Trade draw down is $0 and max draw down is $276 on 3/30/09.

Scale in shares per buy	100
Maximum shares	100
Trade draw down	0
Max draw down	276 on 3/30/09
Unrealized profit	$761 or a 47% gain
Realized profit	0

To do this on the TOS platform requires an alert that is adjusted regularly to follow the trendline so you can buy the equity. Some may adjust the alert daily whereas others may want to adjust it on an hourly basis.

SSO Stochastic scale in

The buy signal called StochLE (standing for Stochastic Long Entry) parameters used were 14,3,3 to maximize profitable entries but the above chart used 14,4,5 to enhance visual clarity. It shows 100 shares per scale and now long 500 shares.

At the end of this chart the open position grew to $1,460 while the trade drawdown was $0 and the max drawdown was $645

The Purple Crayon line is used as an emergency exit.

Scale in shares per buy	100
Maximum shares	500
Trade draw down	$0
Max draw down	$645
Unrealized profit	$1,460 or a 14.6% gain
Realized profit	0

To do this on TOS requires an alert to let you know to buy and set a trailing stop…then walk away.

SSO Stochastic with a 5% profit target

Using 100 shares per entry and a maximum of 200 shares. This had 4-cycles during this time which were all profitable. The max trade drawdown was $75 and the maximum total draw down $134. Total realized profit was $572.

Scale in shares per buy	100
Maximum shares	200
Trade draw down	$75
Max draw down	$134
Unrealized profit	$0
Realized profit	$572 for a 11% gain

This simple strategy scales up nicely to very large capital trading. Instead of just 100 shares per trade this could easily become 10,000 shares per trade or 100 times larger. Yielding a total profit of $57,200.

Since each trade's profit was 5% we could have compounded these gains. So with at least 4-sequential trades the effective gain would have been over 20% in just 8-days.

Once again the Purple Crayon line is used as an emergency exit.

To do this on TOS requires an alert to let you know to buy. Then buy with a fixed profit target…and walk away. Adjust the stop loss to follow the trendline.

GLD $87 breakout

It looked like GLD might be poised for a breakout above $87. My purple crayon was indicating a rising price. So I just waited until I saw the break out.

GLD scale $3

When the break out happened I decided to do some trading. After watching GLD for a quite a while I decided Stochastics would not work effectively. But since price was so erratic, I decided to suck money out of the market using a scaling strategy. Each time GLD would fall by $3, I would buy 100 shares. When I made a $3 profit (about 3%), the strategy would automatically sell it.

Again using the purple crayon as a stop. Once it crossed the purple crayon, the strategy closed the position. Because of this there were some losses at the very end. You can see these in the dashed red lines.


Created with TradeStation

Scale in shares per buy	100
Maximum shares	300
Trade draw down	$715
Max draw down	$1,123
Unrealized profit	$0
Realized profit	$1,141

To implement this type of strategy on TOS would require writing OTO (Order Triggers Orders) orders. You can set these up ahead of time and let them run on the TOS servers. Mike mentioned there was a way on the TOS platform to capture an order queue and send it to other members using MyTrades. We will have to try this.

Financial Comparison study

Recently the financial sector has been in the news. On March 6, 2009 there appeared to a low in the financials. So how have the various stocks and financial ETFs done since then? Creating a study with percentage gain shows a comparison of the best of the best versus FAS—the triple ultra financial ETF.
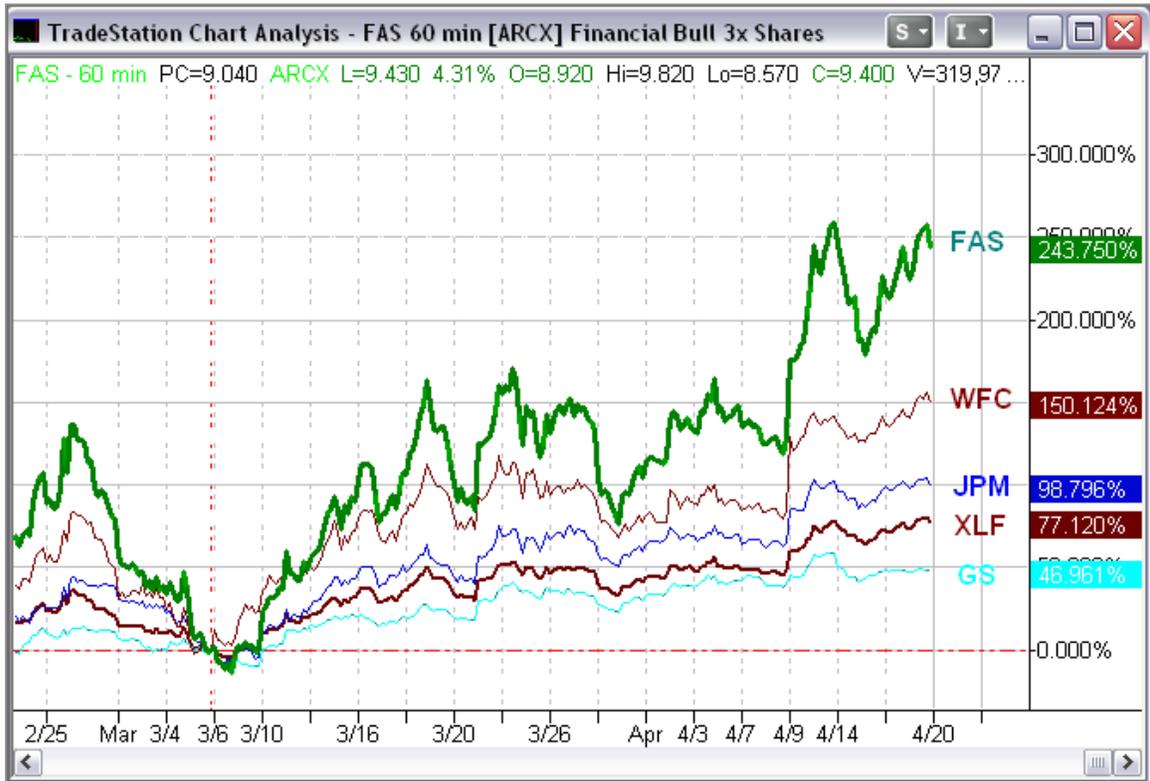
FAS's gain of 250% since March 6 far outshines any of the components that make up this financial ETF. So why trade an individual bank stock?

FAS $6 breakout scale-in

FAS seemed to be consolidating around $6 for a breakout. Also CNBC had it in the news. So I decided on April 1, 2009 to scale into a position of a maximum of 300 shares (a big spender ☺) with a Trendline stop just below $5.60.

The reason to use a trendline instead of a fixed stop was if the stock moves in my favor, I merely edit the trendline by clicking and moving it to an upward sloping line and Tradestation automatically takes care of issuing new stops defined by the trendline. This allowed me to maximize my profit. But for this study I just left it alone as a horizontal line.
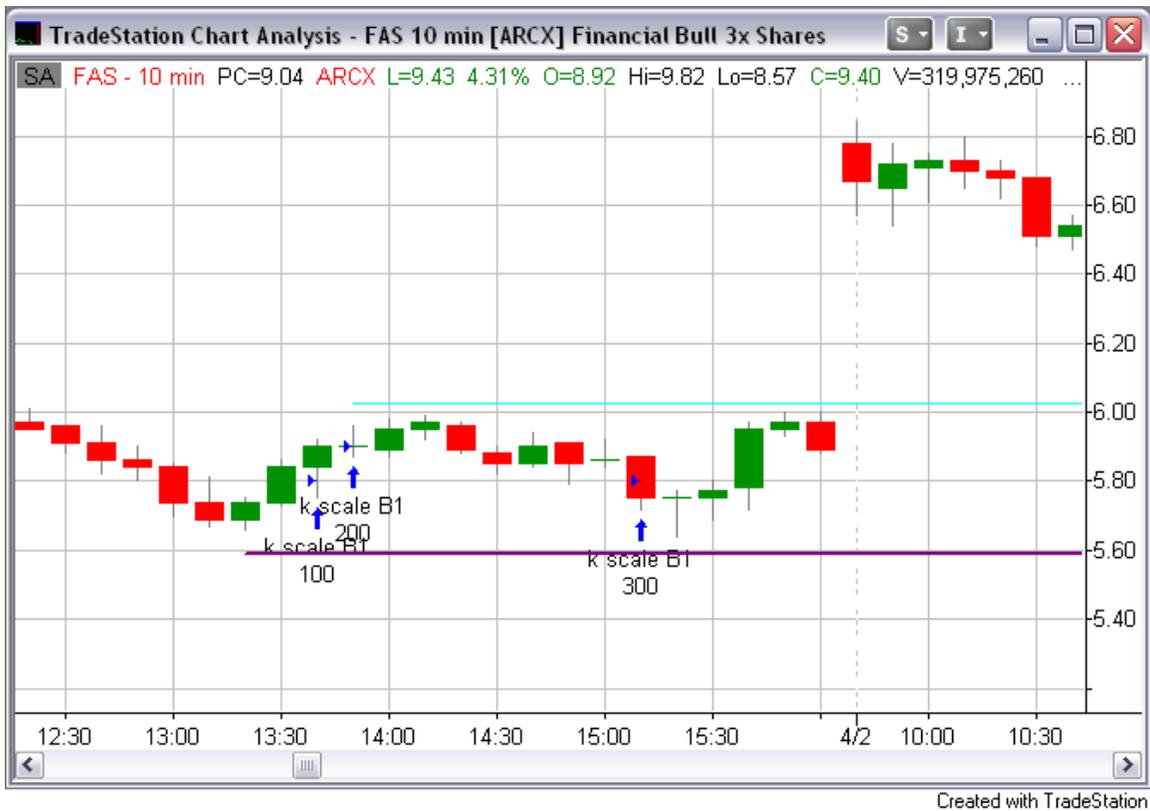

This chart shows the scaling in below $6. Each time the price dropped another $0.10, the strategy would buy 100 more shares up until reaching a limit of 300 shares.

The following chart zooms into the above trades for clarity.

FAS $6 breakout scale-in zoomin

This chart is a zoomed in view of the previous scaling in.

It shows scaling in using $0.10 steps. So for every ten cents reduction in price it would buy 100 more shares of stock up till 300 shares on 4/1/09. The reason was news came out on CNBC that had me convinced the financials were going to rip upward and I wanted to get into a position. The purple crayon stop loss line (at about $5.60) was in place just in case it went against me. I would be out of the trade.

Scale in shares per buy	100
Maximum shares	300
Trade draw down	$0 very low <$1
Max draw down	$852
Unrealized profit	$1,055 (about 58% profit in 11 days)
Realized profit	$0

Day-trade FAZ and FAS?
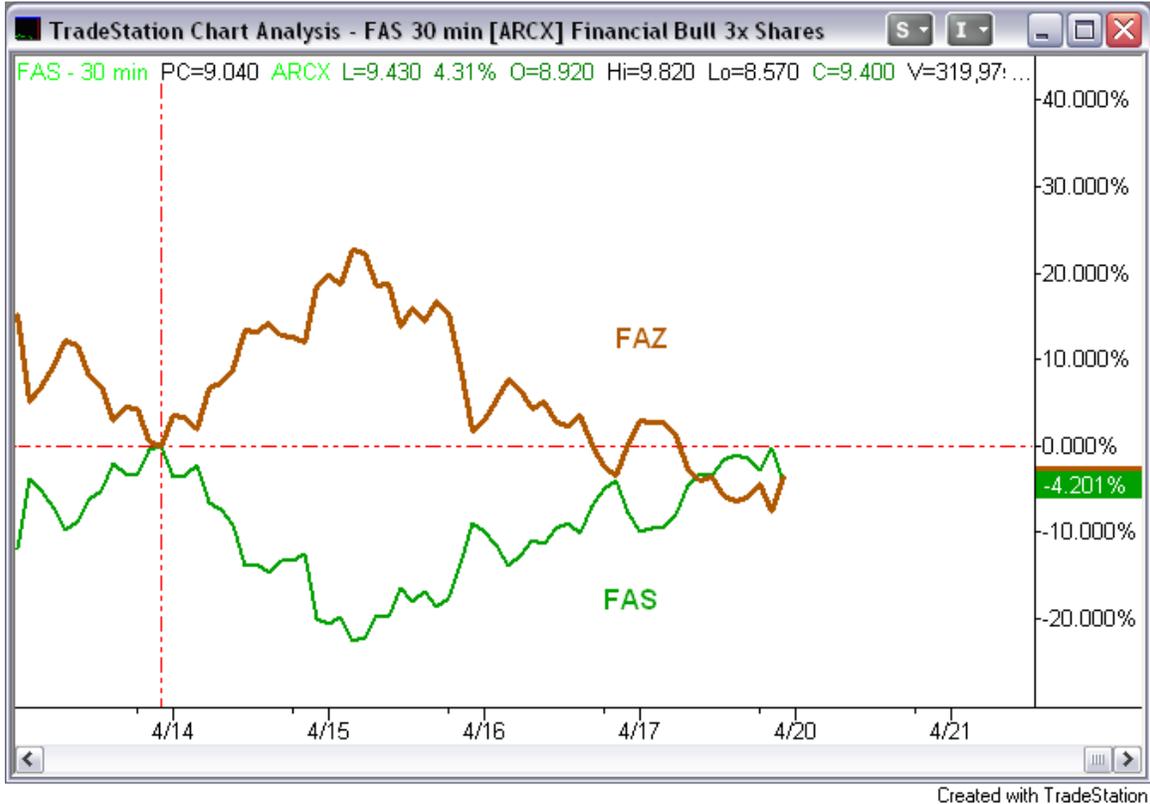
Some bull and bear ultras do not have perfect inverse correlationships. This would make trading them both might not be an effective swing trade strategy.

So what is the relationship between FAZ (3-times bear) and FAS (3-times bull)? Is there strong enough correlation to day-trade these. The above chart (some call it an eye chart since it opens like an eye) shows for the past 4-days there was excellent correlation. With perfect correlation the two lines would always meet back in the middle of the chart (at 0%) and be completely symmetric. You can see there is a slight downward drift where the lines cross in this short time span.

This looked good to me so I attempted to day-trade them. If the market was going up I would go long FAS and if it was going down I would go long FAZ.

FAS 2% profit target

Using the purple crayon to identify a downtrend, it broke out. This made a $20 profit or a 2% profit in 23 minutes. Very nice!

Realize to do this requires significant liquidity. The volume on FAS was averaging about 1 million shares per minute. This corresponds to about $10 million of stock traded per minute. This is plenty of room for day trades. They don't even notice me jumping in on a rally.

Scale in shares per buy	100
Maximum shares	100
Trade draw down	$3
Max draw down	$7
Unrealized profit	$0
Realized profit	$20 (or 2% in 23 minutes)

Conclusion

Even if you miss the initial big move there are many other ways to play the market with some really nice gains.