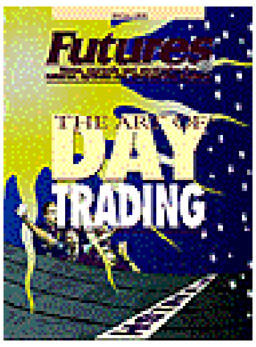

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Finding support and resistance for a day-trader can keep him alive in a volatile market. Here's one idea, implemented with others, to find those target areas.

By Joe Duffy

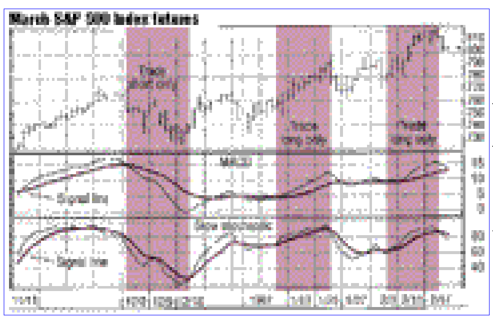
How to find the right support and resistance

My personal preference for day-trading and short-term trading is to buy dips and sell rallies.

Two components are needed to make this strategy work. First, you have to be trading in the direction that gives you the best chance of success. Second, you have to be able to identify potential support or resistance for that trading day. I'll discuss one technique from each of these two components that make up my day-trading approach.

The first step is to determine which way the market is likely to go today -- in other words, is the trend up, down or sideways?

One method to determine the market trend involves a couple of old standby technical indicators that are available on virtually any charting software: the Moving Average Convergence Divergence (MACD) and the stochastic indicators. These oldies but goodies really can be useful if used in the proper combination.

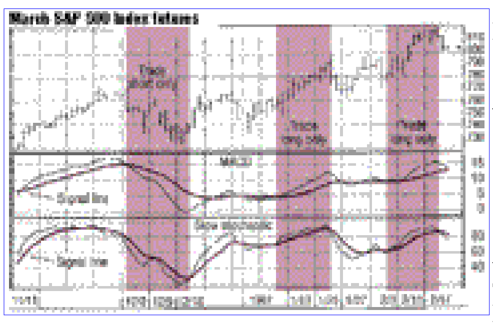


Look at both the MACD and the Slow Stochastic on a daily chart to determine in which direction you want to trade the next day. For the MACD, I use a little longer time value for my inputs then the standard -- say, around a 10-30-10 exponential moving average combination. I also use a slow stochastic indicator with an input value of somewhere around 20 days.

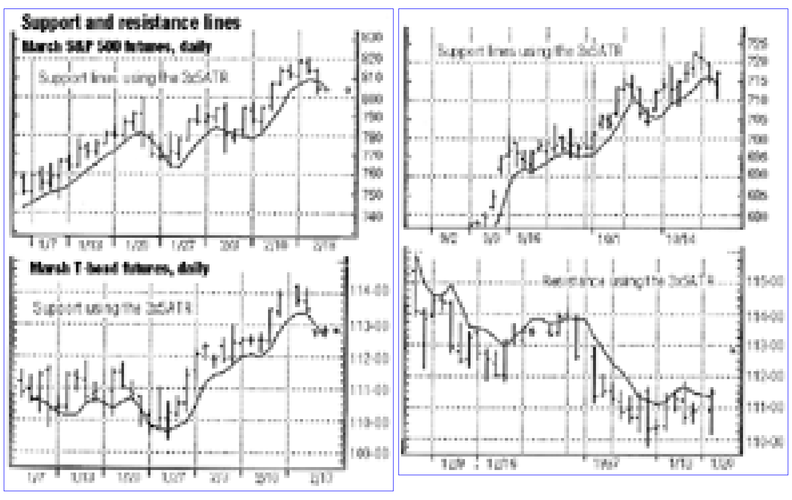
Both of these indicators should be displayed together under the price data. Look for situations when *both* the MACD indicator and the stochastic indicator are on the same side of the signal line.

If both are above their respective signal lines, then trade the buy side. If both are below their respective signal lines, trade the sell side. Quite often you'll find the MACD and the stochastic indicators are on opposite sides of their respective signal lines. In these instances, avoid the market.

The accompanying charts show this simple combination eliminates a lot of noise from the market and identifies those times when the market has the best chance to make a trend move. Throw these indicators up on any chart together, and you will see this combination works infinitely better than either indicator alone.



Once you've determined the direction to trade, the next step is to find support if you want to buy or resistance if you want to sell. There are several ways to do this, and my usual strategy is to employ several methodologies to come up with a confluence or a "keypoint" high-probability trading zone.



Here is one methodology that is being described for the first time. There is no neat name for this indicator, so I'll just call it the 3x5ATR. To construct it:

1. Add up the true ranges for the last five days and divide by five. This is the 5ATR.

2. Calculate a three-day simple moving average of the highs and a three-day simple moving average of the lows.

3. To calculate the 3x5ATR for potential resistance, add the 5ATR to the three-day moving average of the lows. To calculate the 3x5ATR for support, subtract the 5ATR from the three-day average of the highs.

An important point is that this is not a total day-trading strategy. Look to combine other techniques that identify potential support and resistance points. A good rule to live by is to look for a confluence of support or resistance by integrating analysis techniques and integrating time frames.

Joe Duffy is a former trading contest champion and author of three books and videos on his trading techniques. A private trader, he contributes research and analysis to the "Professional Traders Advisory," a daily market letter specializing in stock indexes, bonds and selected special situations in the futures markets. E-mail: Joeduffy@interlog.com.

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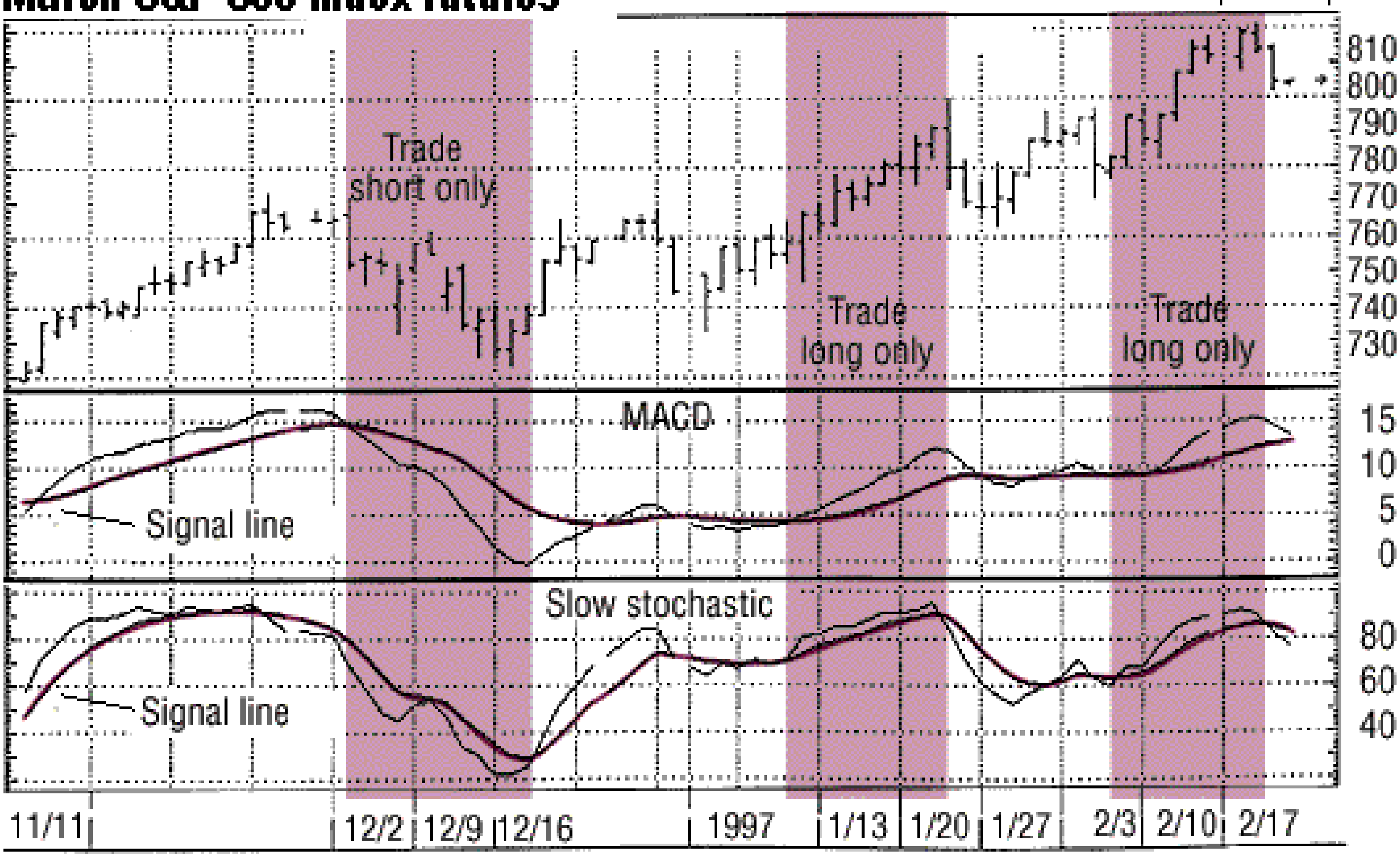
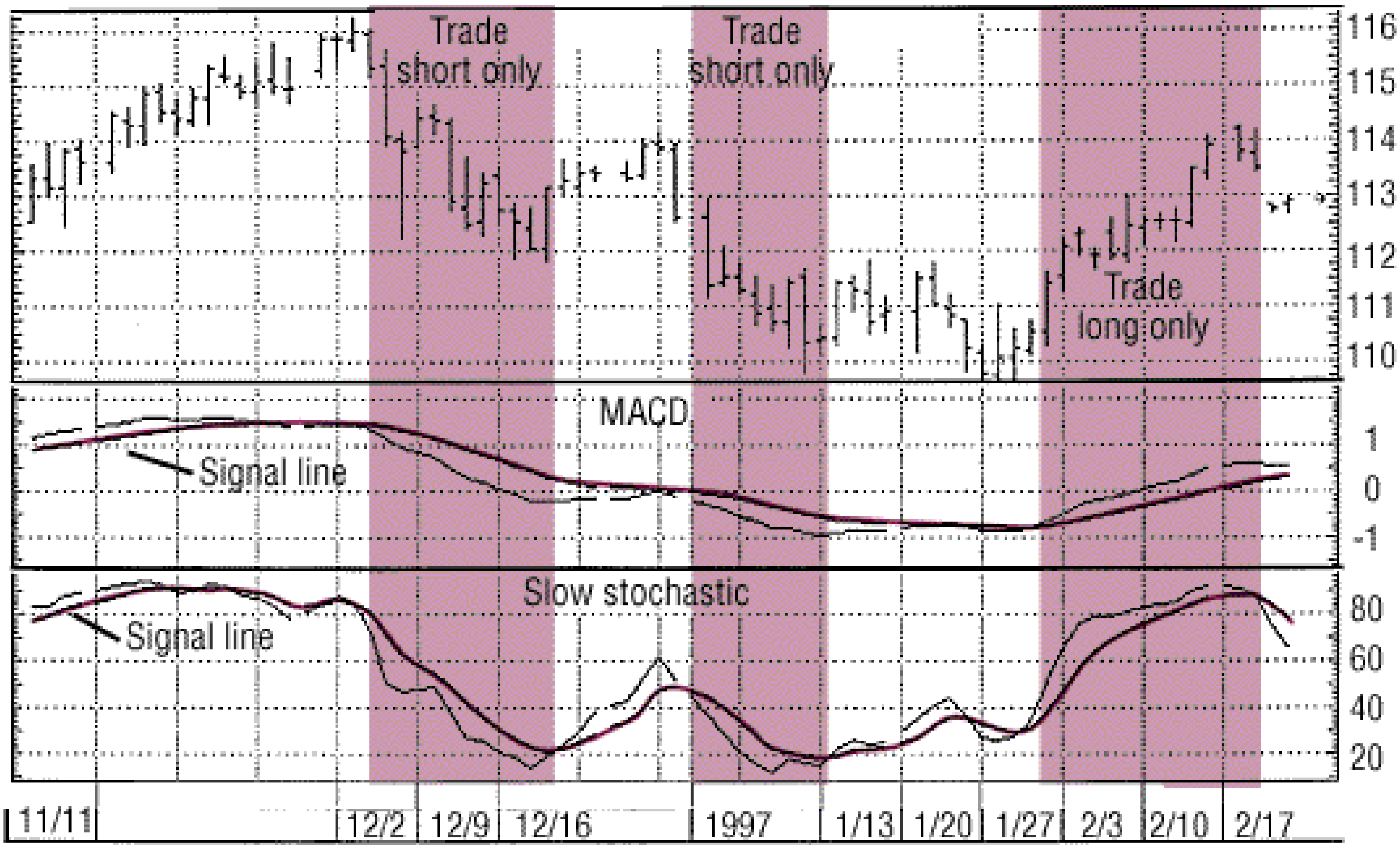
The alignment of the MACD and stochastic indicators together shows you the market trend. When both indicators are below the signal line, as they were in early December for both the S&P 500 Index and T-bonds, you should be a seller; if both are above the signal line, as they were in early February, you should be a buyer.

March S&P 500 Index futures



March T-bond futures



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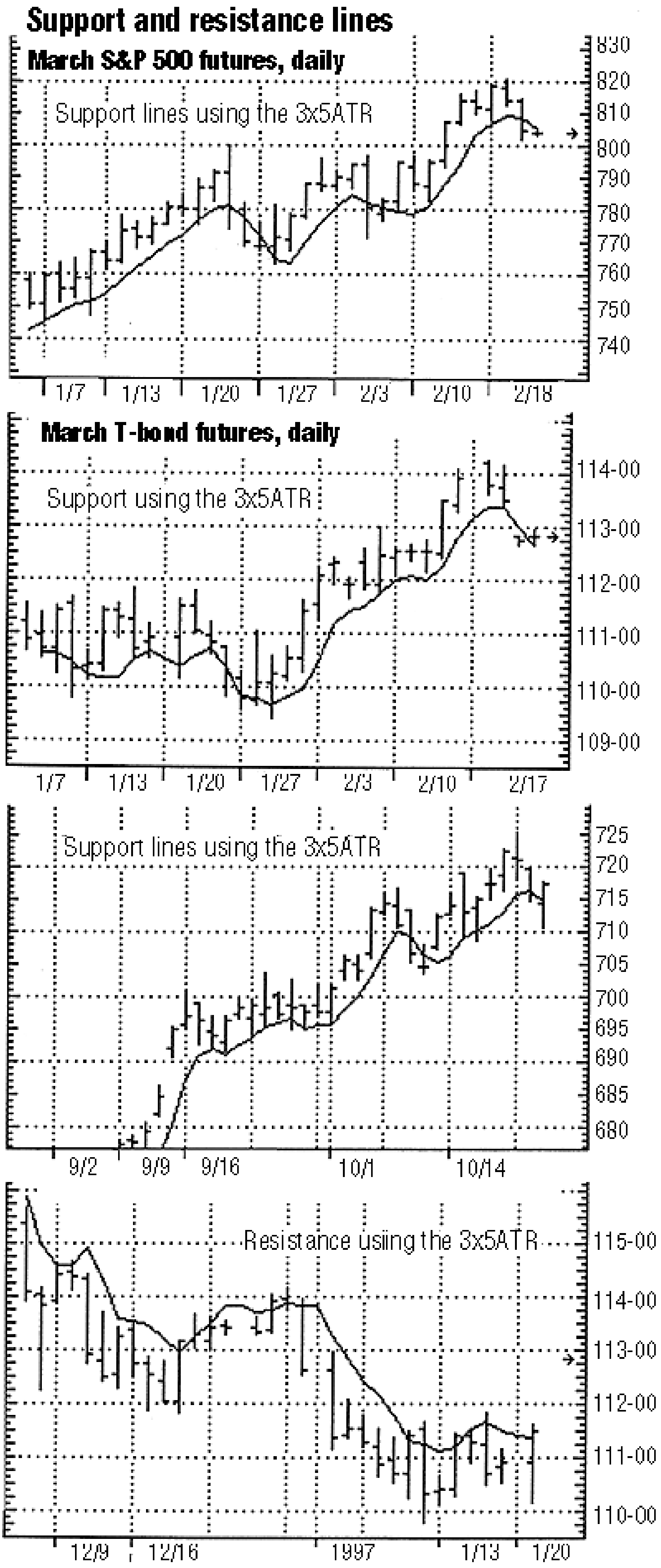
By combining the five-day average true range with simple three-day moving averages of the highs and lows, you can create the 3x5ATR indicator to find support and resistance areas that can be used in a day-trading strategy of buying on dips and selling on rallies. The S&P charts above and the above, left T-bond chart show examples of support lines using the 3x5ATR; the above, right T-bond chart illustrates a resistance line using the 3x5ATR.



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If you want to develop a system, here are some ideas gleaned from studying top performing day-trading systems. If you would rather buy a system, those that trade only the S&P 500 seem to do best.

By George Pruitt

S&P day-trading systems:What works and what doesn't

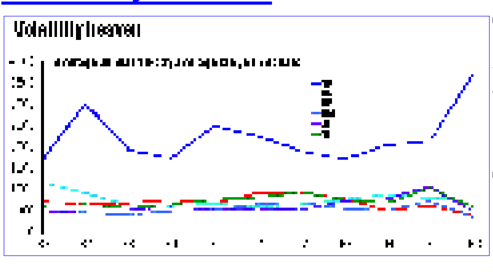
Of all the day-trading systems I've tested over the years, 90% of them trade the S&P 500. This is the market of choice for most day-traders because it affords enough potential to make it a worthwhile venture (see "Volatility heaven," below). By definition, day-trading means you exit at the end of the day, so your profits must at least cover your commissions and slippage.

Although a key difference with the S&P systems I've tested is their approach to entering the market -- they have ranged from basic breakout systems to systems based on the phases of the moon -- the exit signals usually fall into four categories: protective stop, profit target, trailing stop and, of course, market on close. Many of the systems use a combination of these exits.

Because the exit technique is as much or more important than the entry in day-trading the S&P 500, I'll demonstrate that different types of exits work with various types of systems.

Over the past eight years I've often been asked which exit technique is the best. The answer is it depends on the system; there is no black or white answer. However, through research, I've found the success of these exit techniques usually depends upon the frequency of trades a system generates: More frequent trading systems need tighter exits whereas less frequent trading systems need looser exits.

Volatility heaven



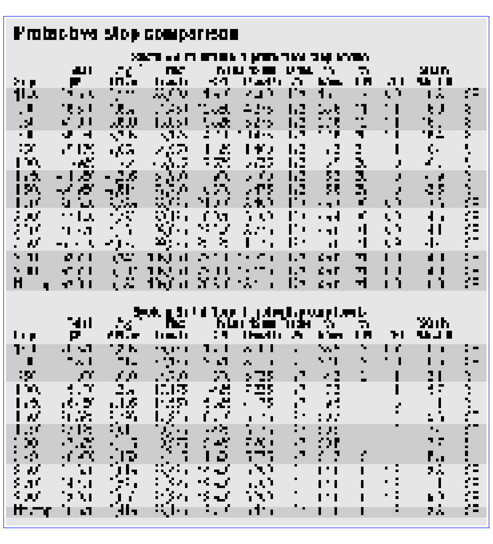
To demonstrate the success or failure of protective stops, profit targets and trailing stops, I've created two systems and tested them over the past 11 years.

These systems use basically the same entry technique, except one trades about five times as much as the other. Buy and sell signals are calculated by adding/subtracting a certain percentage of the 10-day-average range to yesterday's close. In addition, today's range must be less than the 10-day-average range before a buy/sell signal can be placed. The only difference in the two systems is the percentage used to calculate the buy/sell signals. System A uses 50% and System B uses 120%. These percentages were determined by the frequency of trades I was trying to attain.

The systems were tested using five-minute bar data and deducting $100 commission/ slippage per trade. I ran three tests on each system, optimizing different dollar levels for each exit technique. None of the test results of these two systems includes any trades that took place during October 1987 and October 1989. Due to extremely high market volatility, these two time periods can skew performance data.

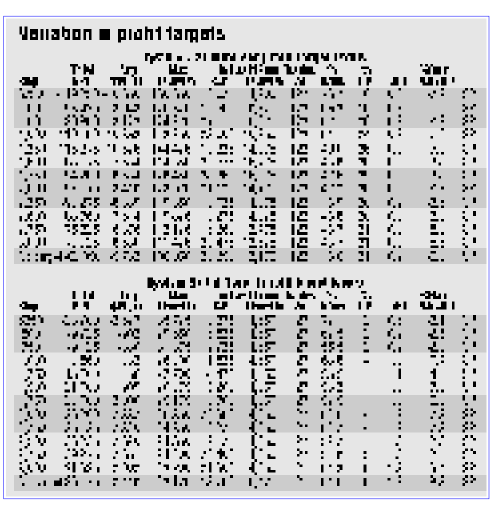
Protective stop If a system has a high frequency of trades, tight stops usually work best. My definition of a tight stop is anywhere between $300 and $750. Systems that trade frequently are trying to make money almost on a daily basis. If the system takes a small loss, then there is always tomorrow; why take a major loss when you know a trade probably will be generated tomorrow?

System A (see "Protective stop comparison," right) shows the performance of the system using several different protective stop levels. Notice that too tight of a stop also degrades performance. A protective stop, at the right level, can turn a losing system into a winner. A system that trades less frequently usually will need a larger stop.

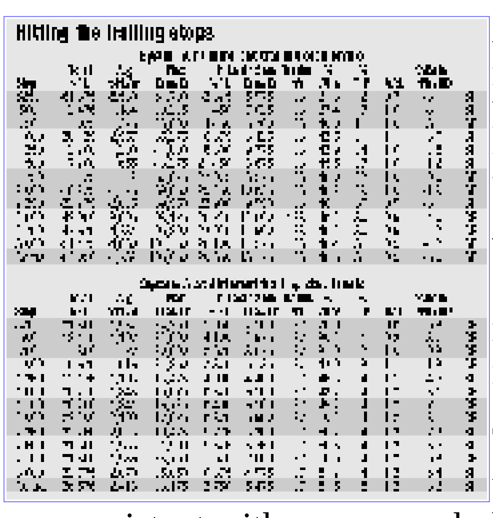


Unlike faster approaches, these systems are in the market for considerably less time and therefore need to make more money per trade. A larger stop prevents a premature loss due to market volatility. System B shows the performance of the slower system using different protective stop levels. As you can see, a larger stop is needed in this case.

Profit targets Pure profit targets generally don't work. A good portion of the profit that is generated by an S&P day-trading system comes from those days when the S&P takes off and keeps going in the same direction. If you limit these potential high-profit days, then you limit the overall profit of your system. System A (see "Variation in profit targets," right) shows terrible performance using tighter profit targets. Due to its frequency of trades, the risk reward ratio is out of whack. Are you willing to risk trading the S&P 500 on a daily basis in hopes of a $250 win? System B also shows degraded performance by using tight profit targets. This system trades so infrequently, it almost has to hit a home run on every trade.



Trailing stops A trailing stop is a combination of a protective stop and profit target. This type of stop gives the market room to breath but at the same time tries to lock in profit. In this analysis, I trailed the high/low of the day by x-amount after a trade was initiated. The trailing stop did not help System A (see "Hitting the trailing stops," below, left) as much as the fixed protective stop. The profit target aspect of the trailing stop was too limiting on the big profit days. Nonetheless, the trailing stop turned a losing system into a winner. System B showed a slight increase in performance at the high end of the trailing stop. This re-emphasizes the need for a large protective stop and large profit target.

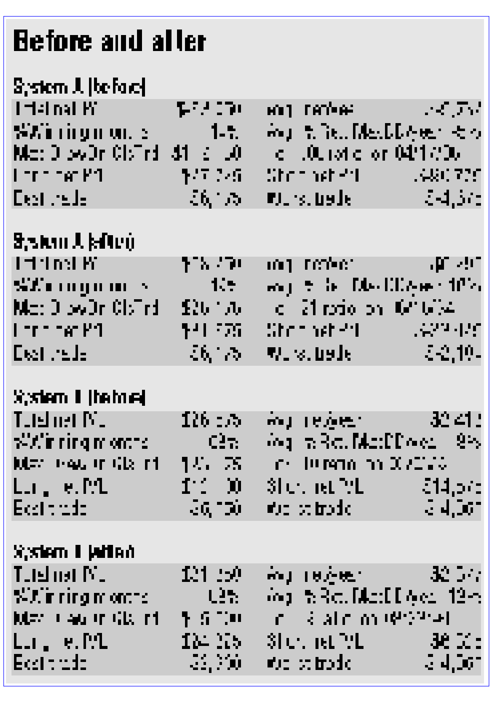


All tests were done using static stop amounts. In today's market, $500 is totally different than it was in 1986. I have found, in almost all cases, that self-adjusting parameters create a much more robust system. An alternative to static dollar stops, would be to use volatility-based, self-adjusting stops. For example, instead of $500 fixed stop, use 10% of the past 10-day average range. This market-defined stop would change with market conditions.

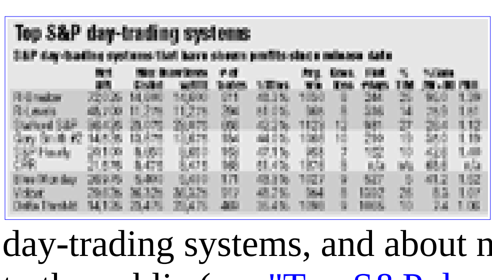
There is no black or white answer to which type of stop is the best to use in a day-trading system. The results shown are consistent with my research; however, it is not a guarantee that all systems will follow suit. A large portion of S&P day-trading systems use a combination of these exits. I have seen systems that will use a protective stop early in the day and a trailing stop later in the afternoon. Whichever stop you pick, it should be based on thorough research. The longer time frame over which you can test, the more robust your parameter selection will be.

We are fortunate to have so much intraday data at our disposal, yet at the same time the data is somewhat skewed. We basically have been in a bull market ever since the S&P 500 futures contract has been traded. Close to 100% of the symmetrical S&P day-trading systems (buy/sell signals are mirror images of each other) have shown much more profit on the long side. With this fact, the question "Why short the S&P?" always arises. And of course the answer always is: "Who knows when a major retracement or bear market is going to occur." The second question is: "Is it okay for a system to have a bullish bias?" In other words, should a system try to buy more often than it sells? Again, there really is no correct answer. There won't be good answer until we have a good sample of bear market data on which to test.

Let's look at some before and after performance numbers on System A and System B (see "Before and after," right). System A, without an exit, was a big loser. However, with a simple $500 protective stop, the system turns into a winner. System B was a mediocre winner without any type of stop, but with a $1,250 protective stop and a $3,000 profit target, the system's overall drawdown decreased by about 60%. Notice the profit/loss that came from the long and short positions.

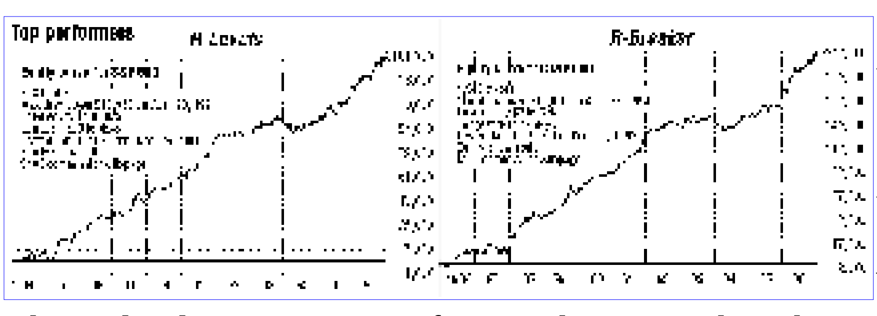


The changes we made look great, but I must warn you about curve fitting, which is when you historically back test to derive a parameter. Don't fool yourself into thinking you've found the holy grail, when in fact you had your 166 MHz computer run two weeks optimizing six parameters. You don't want history to have to repeat itself exactly for your system to make money. Never test the S&P with less than $100 commission/slippage; in fact real-time analysis has shown slippage to be well over $100. A system tested at $50 commission/slippage looks totally different than one tested at $100.



The lack-luster performance of System A and System B may lead you to believe that day-trading the S&P 500 is not your cup of tea. I derived these systems for demonstration purposes only and didn't strive to make them profitable. *Futures Truth* monitors about 20 S&P day-trading systems, and only a handful of them have shown a profit since they were released to the public (see "Top S&P day-trading systems," above).

The best two systems, R-Breaker and R-Levels by Richard Saidenberg, have shown real-time performance similar to hypothetical performance (see "Top performers," below, left). These systems were released to the public in July 1993. The equity curve after this date looks as good as the equity curve before. These systems have been successful because of Saidenberg's countertrend approach to entry and his exit mechanisms. He incorporates a combination of the exit techniques discussed here. His two systems took advantage of the heightened volatility in 1996. In the 1980s, any simple breakout approach seemed to work in the S&P. But during the 1990s, other types of entry and exit techniques have excelled.



Because no system wins all the time, exit techniques provide a form of insurance when the system is wrong. As with all trading, risk should be measured and taken into consideration before placing an order. Don't arbitrarily place some type of exit technique without knowing the mentality of the system. I've been told that 40% of research should be spent on the system and 60% should be spent on money management. In day-trading, your exit is your money management.

George Pruitt is director of research of the independent system testing firm, Futures Truth Inc., in Hendersonville, N.C., which publishes a monthly report of the systems it tests. A top-10 system performance list can be found in Futures *on a bi-monthly basis.*

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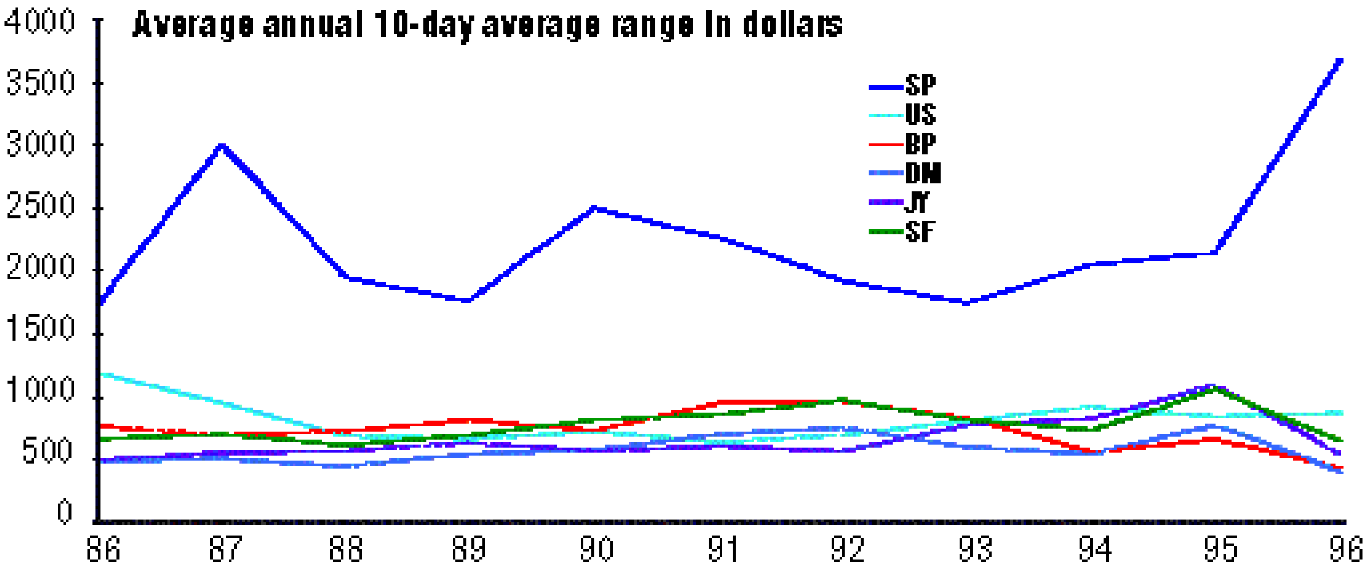
Volatility heaven



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Protective stop comparison

System A at different protective stop levels

Stop	Total $PL	Avg $PL/Yr	Max Draw Dn	in Last 12 mn %PL	in Last 12 mn Draw Dn	Trades /Yr	% Wins	% TIM	W:L	%Gain /Mr+DD	
$100	-23,550	-2,141	33,000	1,650	7,050	123	15.7	7	0.9	-5.3	SP
200	18,500	1,682	21,450	12,350	4,375	123	23.5	11	1.1	5.9	SP
250	41,900	3,809	18,050	9,325	5,275	123	27.6	13	1.1	15.2	SP
500	58,250	5,295	25,175	4,700	10,475	123	37.8	20	1.1	16.4	SP
750	29,175	2,652	34,550	11,125	11,400	123	42.2	24	1.1	6.4	SP
1,000	-925	-84	43,925	7,575	18,925	123	43.9	26	1.0	-0.2	SP
1,250	-14,350	-1,305	61,900	14,900	13,100	123	45.3	28	1.0	-1.9	SP
1,500	-30,950	-2,814	72,700	10,600	13,475	123	45.8	29	1.0	-3.5	SP
1,750	-35,600	-3,236	83,025	21,050	13,400	123	46.3	30	0.9	-3.6	SP
2,000	-47,100	-4,282	89,125	16,975	16,500	123	46.4	30	0.9	-4.5	SP
2,250	-45,775	-4,161	93,675	23,200	13,775	123	46.5	31	0.9	-4.1	SP
2,500	-51,450	-4,677	99,575	25,125	11,675	123	46.6	31	0.9	-4.4	SP
2,750	-58,750	-5,341	103,050	22,100	12,925	123	46.6	31	0.9	-4.9	SP
3,000	-62,775	-5,707	108,950	23,950	12,125	123	46.6	31	0.9	-4.9	SP
No stop	-63,050	-5,732	106,050	20,850	13,175	123	46.6	31	0.9	-5.0	SP

System B at different protective stop levels

Stop	Total $PL	Avg $PL/Yr	Max Draw Dn	in Last 12 mn %PL	in Last 12 mn Draw Dn	Trades /Yr	% Wins	% TIM	W:L	%Gain /Mr+DD	
$250	-20,825	-1,893	26,725	1,250	3,750	27	23.9	2	0.7	-5.6	SP
500	-2,350	-214	27,125	2,525	3,775	27	37.5	3	1.0	-0.6	SP
750	11,000	1,000	24,700	600	6,025	27	44.2	3	1.1	3.1	SP
1,000	15,200	1,382	17,175	-425	7,625	27	47.2	4	1.1	5.7	SP
1,250	26,450	2,405	14,550	5,325	4,175	27	49.5	4	1.3	11.1	SP
1,500	26,325	2,393	17,925	6,750	5,175	27	50.2	4	1.2	9.6	SP
1,750	22,125	2,011	20,275	7,425	6,175	27	50.5	4	1.2	7.4	SP
2,000	23,375	2,125	20,575	5,925	7,200	27	50.8	4	1.2	7.7	SP
2,250	26,950	2,450	22,325	11,800	5,575	27	51.2	5	1.2	8.3	SP
2,500	27,675	2,516	23,425	14,600	5,200	27	51.5	5	1.2	8.3	SP
2,750	24,475	2,225	24,375	13,600	5,700	27	51.5	5	1.2	7.1	SP
3,000	28,075	2,552	21,275	12,600	6,200	27	51.5	5	1.2	9.0	SP
No stop	26,575	2,416	23,175	13,750	5,475	27	51.5	5	1.2	8.3	SP

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Variation in profit targets

System A at different profit target levels

Stop	Total $PL	Avg $PL/Yr	Max Draw Dn	in Last 12 mn %PL	Draw Dn	Trades /Yr	% Wins	% TIM	W:L	%Gain /Mr+DD	
$250	-119,350	-10,850	130,650	10,025	4,900	123	78.3	10	0.6	-7.9	SP
500	-98,425	-8,948	120,825	16,950	6,225	123	66.3	16	0.8	-7.0	SP
750	-89,350	-8,123	124,275	27,575	5,975	123	57.7	20	0.8	-6.2	SP
1,000	-119,550	-10,868	148,250	23,000	10,250	123	51.7	24	0.8	-7.0	SP
1,250	-116,875	-10,625	144,425	19,625	14,075	123	49.0	26	0.8	-7.0	SP
1,500	-83,975	-7,634	114,850	20,775	15,775	123	48.6	28	0.9	-6.3	SP
1,750	-94,200	-8,564	128,450	23,350	15,275	123	47.5	29	0.9	-6.3	SP
2,000	-92,575	-8,416	128,575	21,125	14,775	123	47.2	30	0.9	-6.2	SP
2,250	-92,275	-8,389	119,850	13,025	14,275	123	46.9	30	0.9	-6.6	SP
2,500	-83,750	-7,614	119,325	18,275	14,025	123	46.8	30	0.9	-6.0	SP
2,750	-75,625	-6,875	112,125	16,850	13,775	123	46.7	31	0.9	-5.8	SP
3,000	-72,925	-6,630	111,425	20,475	13,525	123	46.7	31	0.9	-5.6	SP
No target	-63,050	-5,732	106,050	20,850	13,175	123	46.6	31	0.9	-5.0	SP

System B at different profit target levels

Stop	Total $PL	Avg $PL/Yr	Max Draw Dn	in Last 12 mn %PL	Draw Dn	Trades /Yr	% Wins	% TIM	W:L	%Gain /Mr+DD	
$250	-28,900	-2,627	35,725	2,675	4,650	27	72.1	2	0.6	-6.1	SP
500	-9,925	-902	29,650	6,525	4,650	27	62.5	3	0.9	-2.5	SP
750	-9,125	-830	31,375	9,925	4,650	27	55.5	3	0.9	-2.2	SP
1,000	2,550	232	25,200	11,525	4,650	27	53.8	4	1.0	0.7	SP
1,250	13,600	1,236	22,700	14,475	4,650	27	53.5	4	1.1	4.2	SP
1,500	21,000	1,909	20,275	15,200	4,650	27	53.2	4	1.2	7.0	SP
1,750	22,000	2,000	25,175	18,700	4,650	27	52.5	4	1.2	6.2	SP
2,000	26,200	2,382	25,350	20,950	4,650	27	52.5	4	1.2	7.3	SP
2,250	25,525	2,320	24,850	19,225	4,650	27	52.2	4	1.2	7.3	SP
2,500	28,825	2,620	24,350	19,625	4,650	27	52.2	4	1.3	8.3	SP
2,750	29,275	2,661	24,200	20,400	4,650	27	51.8	5	1.3	8.5	SP
3,000	31,925	2,902	23,700	21,900	4,650	27	51.8	5	1.3	9.4	SP
No target	26,575	2,416	23,175	13,750	5,475	27	51.5	5	1.2	8.3	SP

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Hitting the trailing stops

System A at different trailing stop levels

Stop	Total $PL	Avg $PL/Yr	Max Draw Dn	In Last 12 mn %PL	In Last 12 mn Draw Dn	Trades /Yr	% Wins	% TIM	W:L	%Gain /Mr+DD	
$250	-61,375	-5,580	61,700	-2,825	5,975	123	31.8	2	0.7	-8.1	SP
500	-12,475	-1,134	29,225	-450	7,025	123	37.4	7	1.0	-3.1	SP
750	14,025	1,275	28,600	4,450	5,700	123	40.0	15	1.0	3.6	SP
1,000	28,125	2,557	35,275	6,675	8,425	123	42.5	21	1.1	6.0	SP
1,250	13,200	1,200	41,800	8,800	9,775	123	43.9	24	1.0	2.5	SP
1,500	7,200	655	48,375	21,450	6,675	123	45.5	27	1.0	1.2	SP
1,750	25	2	57,875	33,075	8,575	123	46.0	28	1.0	0.0	SP
2,000	-16,225	-1,475	69,650	29,250	10,825	123	46.2	29	1.0	-1.9	SP
2,250	-33,275	-3,025	89,550	32,900	9,950	123	46.1	30	0.9	-3.1	SP
2,500	-43,950	-3,995	93,175	25,725	12,500	123	46.2	30	0.9	-4.0	SP
2,750	-47,675	-4,334	95,800	23,025	11,900	123	46.2	30	0.9	-4.2	SP
3,000	-51,475	-4,680	101,450	26,100	11,575	123	46.4	31	0.9	-4.3	SP
No trail	-63,050	-5,732	106,050	20,850	13,175	123	46.6	31	0.9	-5.0	SP

System A at different trailing stop levels

Stop	Total $PL	Avg $PL/Yr	Max Draw Dn	In Last 12 mn %PL	In Last 12 mn Draw Dn	Trades /Yr	% Wins	% TIM	W:L	%Gain /Mr+DD	
$250	-21,800	-1,982	24,350	1,050	2,150	27	25.9	0	0.6	-6.3	SP
500	-12,175	-1,107	22,600	4,100	2,975	27	30.2	1	0.8	-3.7	SP
750	-850	-77	20,600	2,675	3,575	27	37.9	2	1.0	-0.3	SP
1,000	5,675	516	21,850	2,375	5,125	27	43.9	3	1.1	1.8	SP
1,250	13,175	1,198	18,475	4,900	4,400	27	45.8	4	1.1	4.7	SP
1,500	20,275	1,843	15,675	6,825	6,100	27	48.2	4	1.2	8.1	SP
1,750	20,250	1,841	16,725	6,400	6,100	27	49.2	4	1.2	7.7	SP
2,000	23,200	2,109	17,675	6,875	5,950	27	50.2	4	1.2	8.5	SP
2,250	22,250	2,023	19,475	9,775	6,200	27	50.2	4	1.2	7.6	SP
2,500	21,300	1,936	21,900	9,525	5,750	27	50.5	4	1.2	6.7	SP
2,750	21,300	1,936	23,750	7,525	7,000	27	50.5	4	1.2	6.3	SP
3,000	22,775	2,070	25,050	10,875	4,975	27	51.2	4	1.2	6.4	SP
No trail	26,575	2,416	23,175	13,750	5,475	27	51.5	5	1.2	8.3	SP

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Before and after

System A (before)

Total net P/L	$-63,050	Avg. net/year	$-5,732
%Winning months	40%	Avg. %Ret. MaxDD/year	-5%
Max DrawDn ClsTrd	$106,050	or -.05 ratio, on 04/17/95	
Long net P/L	$27,725	Short net P/L	$-90,775
Best trade	$6,175	Worst trade	$-4,675

System A (after)

Total net P/L	$58,250	Avg. net/year	$5,295
%Winning months	49%	Avg. %Ret. MaxDD/year	16%
Max DrawDn ClsTrd	$25,175	or .21 ratio, on 06/15/94	
Long net P/L	$81,675	Short net P/L	$-23,425
Best trade	$6,175	Worst trade	$-2,100

System B (before)

Total net P/L	$26,575	Avg. net/year	$2,416
%Winning months	58%	Avg. %Ret. MaxDD/year	8%
Max DrawDn ClsTrd	$23,175	or .10 ratio, on 02/03/94	
Long net P/L	$12,000	Short net P/L	$14,575
Best trade	$5,050	Worst trade	$-4,950

System B (after)

Total net P/L	$31,650	Avg. net/year	$2,877
%Winning months	58%	Avg. %Ret. MaxDD/year	13%
Max DrawDn ClsTrd	$15,500	or.19 ratio, on 08/23/94	
Long net P/L	$24,825	Short net P/L	$6,825
Best trade	$2,900	Worst trade	$-4,950

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Top S&P day-trading systems

S&P day-trading systems that have shown profits since release date

	Net $PL	Max DrawDown ClsTrd	Max DrawDown w/OTE	# of trades	%Wins	Avg. win	Cons. loss	Flat #days	% TIM	%Gain /Mr+DD	PRR
R-Breaker	72,025	14,600	14,600	511	48.3%	1030	8	244	25	95.0	1.39
R-Levels	48,700	11,275	11,275	294	51.0%	965	8	316	14	75.9	1.51
Stafford S&P	36,425	23,075	23,075	656	42.2%	1123	12	931	27	26.4	1.12
Gary Smith #2	14,525	13,675	13,675	184	44.0%	1066	10	210	19	35.0	1.19
S&P Hourly	20,100	8,650	8,650	153	47.1%	953	7	152	10	42.6	1.40
CPR	21,575	8,475	8,475	168	51.4%	1376	8	n/a	n/a	68.6	n/a
Blue Monday	26,975	5,400	5,400	171	43.3%	1027	9	527	5	41.2	1.52
Volpat	29,625	36,325	36,325	917	48.2%	954	8	1392	26	8.3	1.07
Delta Thrsh ld	14,125	23,475	23,475	469	35.4%	1098	9	1065	10	7.4	1.06

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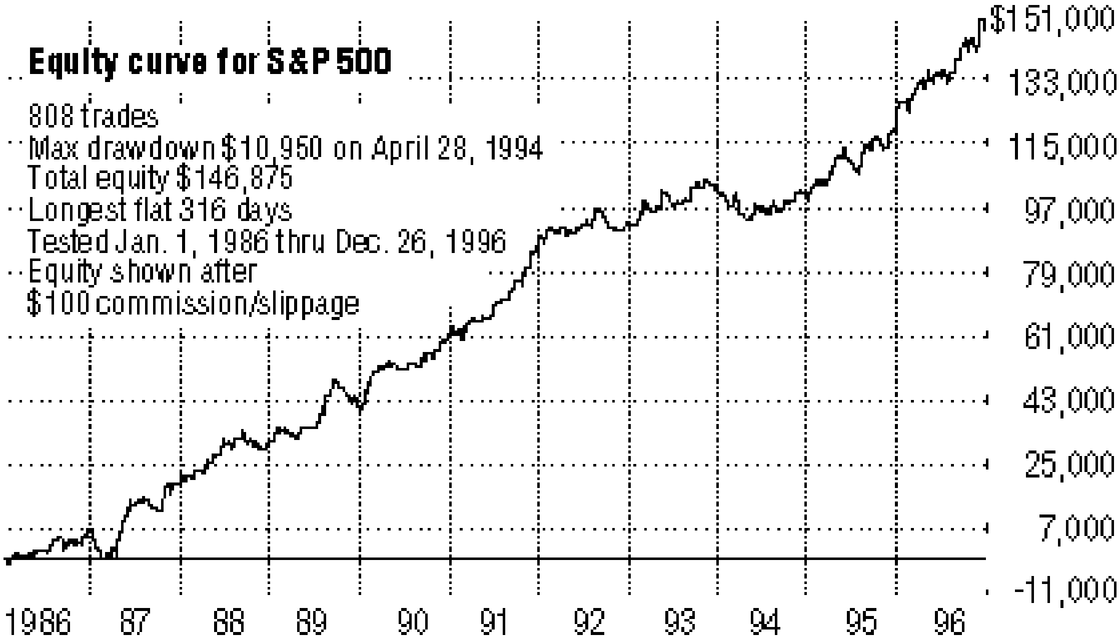
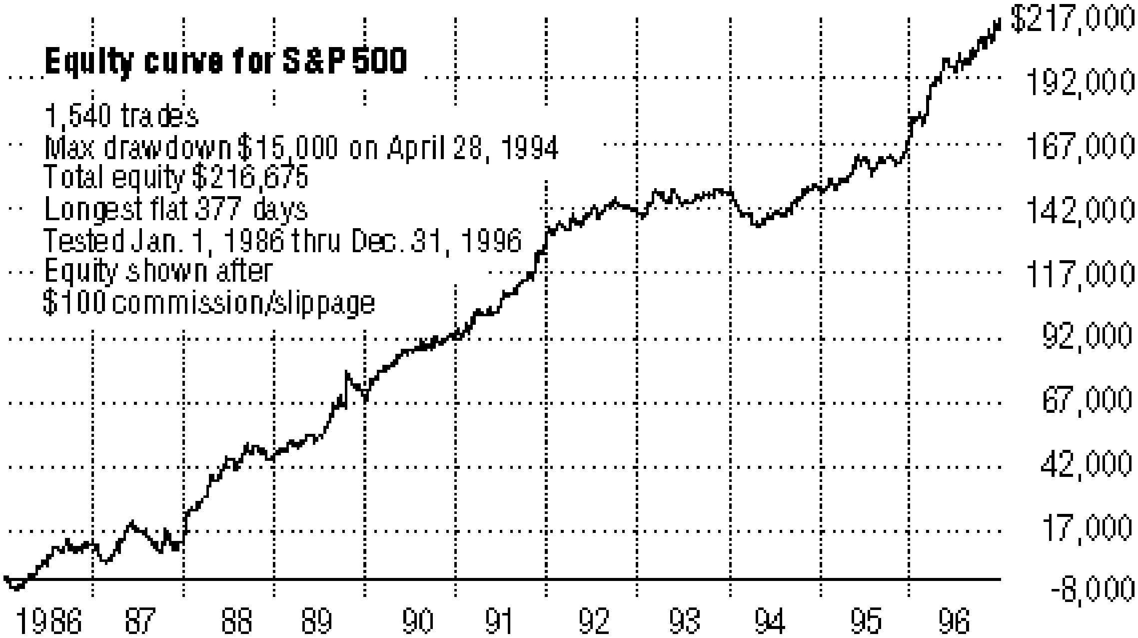
Top performers

R-Levels



R-Breaker



Source: Excalibur

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Getting the 'edge'

The best advice for an off-floor trader who wants to day-trade is to develop or buy a system that will force him into action. Buying a system may save you time, but you should use the same rigorous rules to test it.

By Frank J. Alfonso

It's no secret most day-trading profits are made by floor traders. They not only have the advantages of low commissions and ease of execution, but they have the "edge" or the ability to buy at the bid price and sell at the ask price. Although day-trading off the floor is a completely different game, traders also must have some sort of advantage that will give them a trading edge.

Certainly live, tick-by-tick quoting equipment is necessary, along with charting and technical analysis software. Most novice day-traders watch prices, analyze various intraday charts and indicators, thinking they can assimilate this flow of information and make profitable trades. They often hope for some sort of "sixth sense" to give them an advantage. Unfortunately, the market usually demonstrates it has more of a sixth sense and soon separates the trader from his money.

Something concrete is needed to give a trader the confidence and commitment to "pull the trigger." There are so many examples in books and magazine articles isolating some guru's favorite chart formation or technical indicator that shows where to buy or sell. New traders follow this advice based on "trust" that the author or guru knows from experience what he is talking about. But doesn't it make sense to ask, "How many times in the past when this indicator signaled a buy, did the price actually go up?" Or, "If we use a close $200 stop as suggested, how many times did we get stopped out for a loss, only to have the market turn around and produce what would have been a profitable trade?" Or, "If we buy a breakout of the previous day's high, how many ticks in profits can we expect, given various market conditions?"

Knowing the answers to such questions will give you an "edge" to win at day-trading. With all the computing power and historical data available today at relatively inexpensive prices, you have no excuse to day-trade without hard statistical facts.

Results of historical testing on technical indicators, chart formations or price patterns can be combined with a "signal generator" to form a trading system. Actual buy and sell signals are generated throughout the day based on trading models developed with historical testing. If you have a limited degree of computer knowledge, use TradeStation or SuperCharts RT by Omega Research or MetaStock RT by Equis International to test a myriad of day-trading strategies and create trading systems. Expert computer users can develop more advanced strategies using Microsoft Visual Basic or C++.

To develop a day-trading system, you must obtain historical data and one of the "toolbox" software programs that can test trading ideas.

There are five main rules to follow when developing a day-trading system:

1.Use long test periods Novice traders often test a strategy back over several contracts, or even several years, and think they have a tradable method. Unfortunately, day-trading based on this limited testing will end in disaster. Any trading method must be tested for a minimum of five years and preferably 10 years or longer. Then, the reality of more down-to-earth performance statistics appear.

2.Robust variables When testing, or incrementing variables for a system, it is important that wide ranges of values generate favorable results. If just a few variable increments produce acceptable results, the trading rule is fragile. Future results will be poor.

3.Limited number of rules Any trading method could be 100% accurate and display impressive profits if an unlimited number of rules were used, however the method will almost certainly fail in real-time trading with new data. Keep the number of rules or conditions a system uses to less than five or six for a 10-year period or slightly higher if the number of trades or occurrences is high.

4.Real-time or out-of-sample testing After historical tests have been completed over reasonably long time periods, and variable values have been selected, the trading method should then be tested over new or "real-time" data. This "out-of-sample" test is usually over current data, using a shorter period of one to two years. The results will give a good idea of system performance, just as if the trader were using it in the market during this time period. Out-of-sample tests on periods prior to the historical testing period also are acceptable but not as useful as tests over more recent data.

5.Walk-forward testing Most testing programs do not have this advanced feature, which is really an automated way of generating a whole series of out-of-sample tests. This approach increments or optimizes system variables over a moderate time period, such as two years. The variable values that produce the best results over this "learning" period are then used on the next quarter (three months), which is new or "real-time" data. The results should be profitable. Then, the first quarter of the learning period is eliminated, and the next quarter in the database is added to the multi-year learning period. Variables again are incremented and the best ones are selected for use in the next out-of-sample quarter. Testing continues like this all the way through the database. The net performance of all out-of-sample tests is summarized. Overall, the results should be profitable to consider the system valid for trading with real funds. If the system doesn't hold up to this testing method, it won't make money in the future...period!

Purchasing a system After new traders discover developing their own system is not that easy, they may consider purchasing a trading method from a system developer. But how do you decide which system to purchase?

First, all the rules given previously for developing your own system should have been used by the vendor. Ask him how the method was developed. Were long test periods used? Does the system have robust variables? Are only a limited number of rules or conditions used? Was walk-forward-testing employed, etc.?

Then, once you receive the program, you must be able to verify the vendor's marketing material with the software itself. Don't just buy a "signal-generator." The system you purchase should duplicate the results advertised. You should be able to run historical tests over data and see for yourself the simulated performance of the system.

Don't just rely on the vendor's brochure or performance numbers. Go back and run long historical tests over the data. Increment the variables and check for robustness. Change the system variables, and do some out-of-sample tests. Then, if the method holds up to the five rules for developing a system, it can be relied upon for real trading.

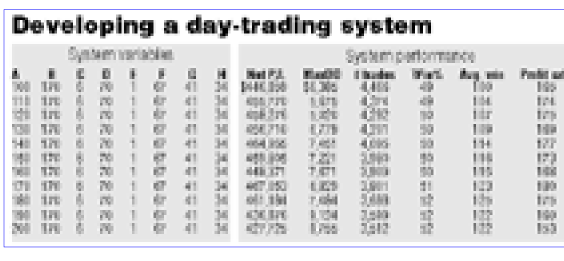
Capital Next you need to determine the right amount of capital to use. This is where the results of historical testing are helpful.

The account size should be large enough to cover the largest maximum drawdown (largest historical account equity decrease) of the system, plus margin amounts. Again, this is where the importance of using long test periods shows up. If the maximum drawdown for the last two years was only $1,800, and you don't realize a big drawdown of $5,000 occurred six years ago, you are not aware of the potential risks of trading the method and will not allocate enough trading capital.

Plan for drawdowns. Assume the maximum drawdown will start on the day you start trading the program. Also, be aware that future drawdowns can exceed previous historical maximum drawdowns.

Knowing the maximum drawdown also can be used to improve day-trading performance -- one technique is to wait for a good-sized drawdown to occur on paper before starting to trade the system.

Another technique is to keep an eye on systems and variable sets that are not performing well and are in a drawdown. Start trading them with a small profit objective. If the trades are profitable immediately, take the profits and stand aside, and wait for another drawdown. If the trades go against you, continue trading the system until the profit objectives are reached. However, you need to have the additional capital available to stay with the system until it begins to recover from the drawdown.



You also must have a high level of confidence in a system to start trading when it is in a drawdown. Systems tend to run in cycles. Most traders will hop on and start trading a system after it has had a very profitable period, only to catch the next down cycle. Then, when it is in a losing period, they start tinkering with it, trying to second guess the system, instead of just sticking with it. Often they end up missing the next big profitable cycle. Following the five rules for historical testing will give you the confidence to start trading a system when it is in a drawdown.

Many traders also try to add additional filters or rules during drawdowns. However, this breaks one of the primary rules of developing a system. Adding additional conditions or rules just makes the method less reliable in the future. Accept the drawdown as part of a necessary risk of trading. Let the system run its course and stick with it. Execute your plan...that's your "edge!"

Frank J. Alfonso is president of MicroStar Research & Trading Inc. in Sarasota, Fla. He has developed trading systems for 20 years, is a former CPA, floor trader and member of the Chicago Board of Trade.

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The below test demonstrates several of the important rules required to develop a profitable day-trading system. The test covers a trading system for T-bond futures from 1983 through February 1997 (long test period). There are eight variables, A through H (limited number of rules), which is reasonable given the long test period and the more than 3,500 trades. Variable A is incremented from 100 to 200, with the other variables held constant. System performance, measured by net profit and loss and maximum drawdown, demonstrates robust variables, as large changes in Variable A still produce very good results. Incrementing the other variables also should produce similar results.

Developing a day-trading system

System variables								System performance					
A	**B**	**C**	**D**	**E**	**F**	**G**	**H**	**Net P/L**	**MaxDD**	**# trades**	**Win%**	**Avg. win**	**Profit ratio**
100	170	6	70	1	67	41	34	$446,859	$6,385	4,466	49	100	165
110	170	6	70	1	67	41	34	455,770	5,675	4,374	49	104	174
120	170	6	70	1	67	41	34	458,276	5,020	4,282	50	107	175
130	170	6	70	1	67	41	34	456,710	6,779	4,201	50	109	169
140	170	6	70	1	67	41	34	464,955	7,451	4,095	50	114	177
150	170	6	70	1	67	41	34	459,805	7,221	3,980	50	116	173
160	170	6	70	1	67	41	34	448,371	7,671	3,909	50	115	168
170	170	6	70	1	67	41	34	467,053	6,829	3,801	51	123	180
180	170	6	70	1	67	41	34	461,184	7,484	3,688	52	125	175
190	170	6	70	1	67	41	34	436,876	9,124	3,599	52	122	160
200	170	6	70	1	67	41	34	427,725	8,755	3,512	52	122	153

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Originally designed for daily analysis, Tom DeMark's TD Sequential indicator also works for intraday analysis. It is effective for especially targeting high- and low-risk entry points.

By Tom DeMark

Applying TD Sequential to intraday charts

When I entered the investment business more than 25 years ago, volume on the New York Stock Exchange was approximately 6 million shares a day. Stock quotations appeared on a ticker tape, and futures quotes were on a large wallboard.

I did my market timing research by poring over weekly printed charts with a magnifying glass. Analysis was limited to conclusions regarding daily price activity because intraday price data were not available until the 1980s. As such, once it became available, I was pleasantly surprised to see that the TD Sequential worked on intraday price movements as well.

My research showed price movement of most markets displayed a natural rhythmic motion that could be measured by a combination of factors that either compared closing price levels or closing prices with extreme price highs and lows. Simply put, TD Sequential consists of three distinct stages: setup, intersection and countdown.

Setup The initial setup phase consists of a series of at least nine consecutive closes less than the close four trading bars earlier for a buy setup and at least nine consecutive closes greater than the close four trading bars earlier for a sell setup. Setup establishes the environment or the context for the market and determines whether a trader should be looking to buy or sell the market.

I have added a caveat to the phrase "The trend is your friend." It is "...unless the trend is about to end." At that point it is not prudent to trade with the trend. Most of my market timing indicators, as is the TD Sequential, are designed to anticipate trend reversals.

Intersection Once the setup series has been defined, I review price activity beginning on day 8 of setup to determine whether the setup process has been perfected and countdown can begin. To accomplish this, I require a phase I refer to as intersection.

Intersection requires the high of bar 8 of a buy setup be greater than or equal to the low of bars 5, 4, 3, 2 or 1 of the buy setup. If this requirement is not met, then the high of bar 9 of the buy setup must be greater than or equal to the low of buy setup bar 6 or any other price bar back to bar 1 of the buy setup. If this is not fulfilled, then each successive price bar is compared until its high is greater than or equal to the low of the price bar three or more price bars earlier back to bar 1 of the buy setup.

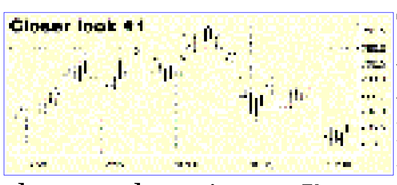
For intersection to occur in a sell setup, the low of setup price bar 8, 9 or the first subsequent bar must be less than or equal to the high three or more price bars earlier all the way back to bar 1 of the sell setup.

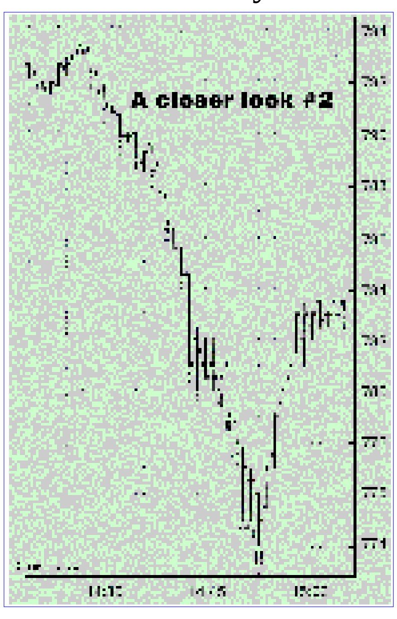
Intersection is a required step because it assures that the rate of decline or advance is decelerating sufficiently to enter the final phase, which is countdown.

Countdown TD Sequential buy countdown consists of a series of 13 successive closes less than or equal to the low two price bars earlier. Once that has been accomplished, the market generally is in a low-risk buy entry zone. The TD Sequential sell countdown consists of a series of 13 successive closes greater than or equal to the high two price bars earlier. This generally indicates a low-risk sell entry zone.

Whereas setup requires the price comparisons be maintained consecutively, countdown does not apply such restrictions. To prevent high-level, low-risk buy countdown 13 entries and low-level, low-risk sell countdown 13 entries, I've installed the requirement that day 13 of a buy countdown be postponed until it occurs below day 8 of the buy countdown and, conversely, that day 13 of a sell countdown be postponed until it occurs above day 8 of the sell countdown. "Recycling" is a concern that could arise in a strongly trending market. Generally speaking, if a subsequent setup occurs prior to completion of countdown, then a new countdown process must begin.

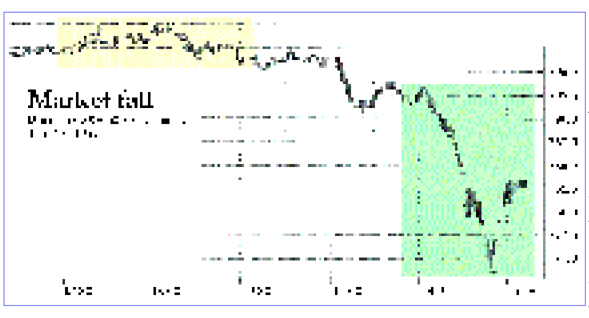
TD Sequential in action The TD Sequential is versatile over various time frames. The charts of the March 1997 S&P 500 Index futures contract on Jan. 23 ("Market fall," left) show the contract declined from approximately 800 to 773, roughly a 27-point collapse, in 1 1/2 hours.





To demonstrate the sensitivity of the TD Sequential to identify the exact high and low on the chart to the minute, I've applied it to this time period. The respective sell countdown 13 and buy countdown 13 are not levels of entry; rather, they accurately define levels of low-risk entry. "Market fall" provides you with a perspective of how the price top and bottom were formed.

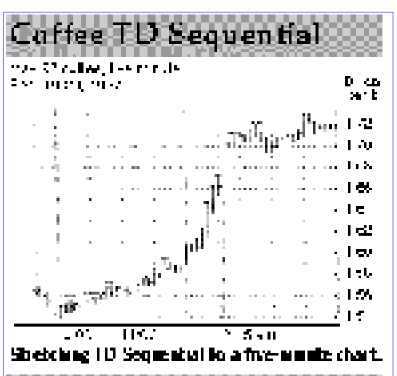
"Closer look #1 (above) and #2" (right) magnifies the sell setup period and the buy setup period to illustrate the simplicity in calculating the respective price setups and countdowns. Note that, in the case of the market advance, I insert both setup and countdown numbers above the price bar and, conversely, in the case of a market decline, the numbers appear beneath the respective price bars.



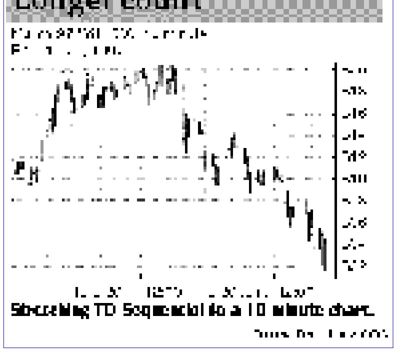
Furthermore, it is apparent in "Market fall" that, coincident with the completion of the ninth bar of the sell setup (a series of nine or more consecutive closes greater than the close four price bars earlier), price has a tendency to retrace. A similar occurrence is observed at 1:45 p.m. when the ninth price bar of sell setup is recorded.

Buy setups demonstrate a similar behavior only in reverse. At approximately 1:15 p.m. the ninth price bar of buy setup (a series of nine or more consecutive closes less than the close four trading bars earlier) was recorded, and prices subsequently rallied. A similar event took place at 2:10 p.m.

However, not every setup elicits such a response, as you can readily see at 2:35 p.m. when the ninth bar of a buy setup failed to generate any price movement to the upside.



Stretching TD Sequential to a five-minute chart.



Stretching TD Sequential to a 10 minute chart.

To demonstrate the application of TD Sequential to other markets and time periods, I've included a five-minute chart of May 1997 coffee futures in "Coffee TD Sequential" (right), which identifies a TD Sequential high-risk buy countdown completion just prior to the Feb. 20 early morning price peak before a 10-point plus decline.

Also, in "Longer count" (right), the March S&P 500 Index futures chart on a 10-minute basis, I identify the TD Sequential nine-13 high-risk buy indication on Feb. 19, coincident with the price peak.

Although TD Sequential has worked effectively on a daily basis for more than two decades, only within the last five years has it become apparent that this technique can be applied to intraday price charts as well. Because it originally was designed to be applied to longer time periods, its ability to identify high- and low-risk entry zones on an intraday basis is a testimony to its adaptability and dynamic design.

Tom DeMark is president of Market Studies Inc., a provider of indicator software for most major quote vendors, a consultant to large fund managers and author of The New Science of Technical Analysis *and* Market Timing Techniques: Innovative Studies in Market Rhythm and Price Exhaustion, *published by John Wiley & Sons. TD Sequential is a registered trademark.*

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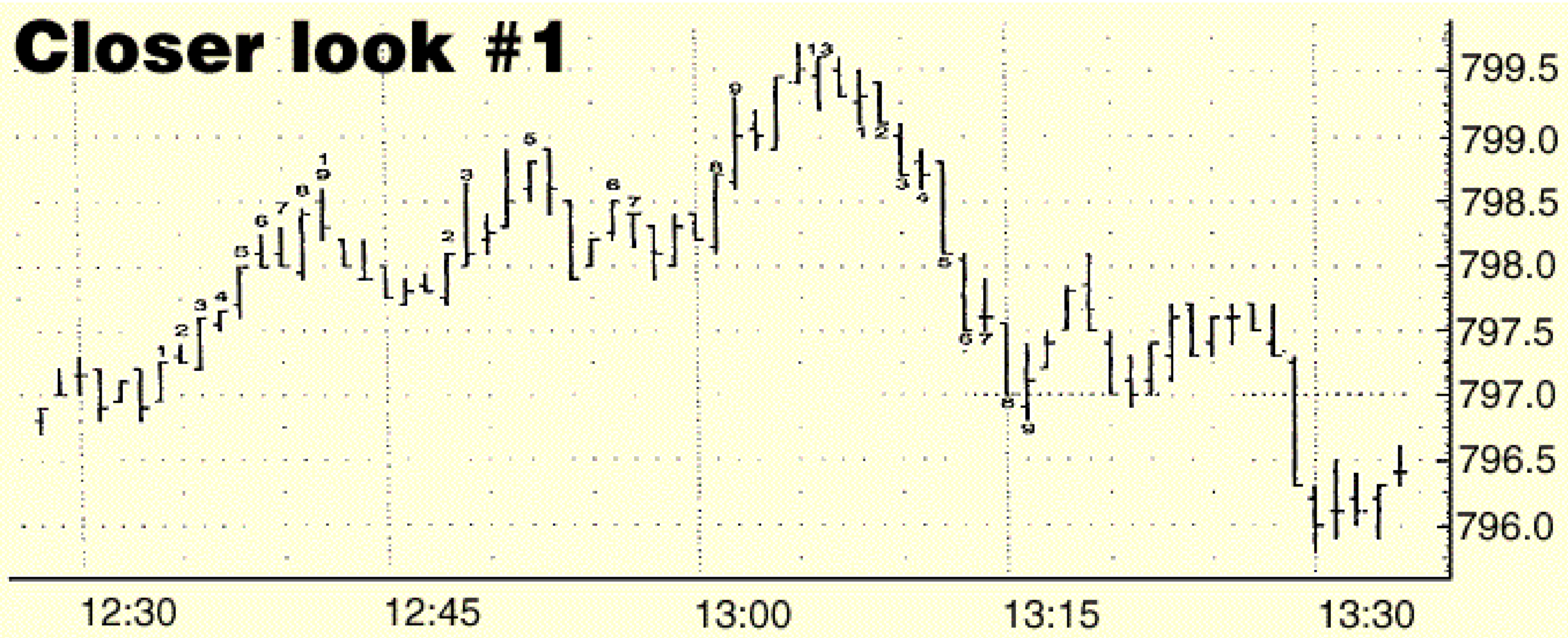

The sell setup and countdown, peaking at 13.

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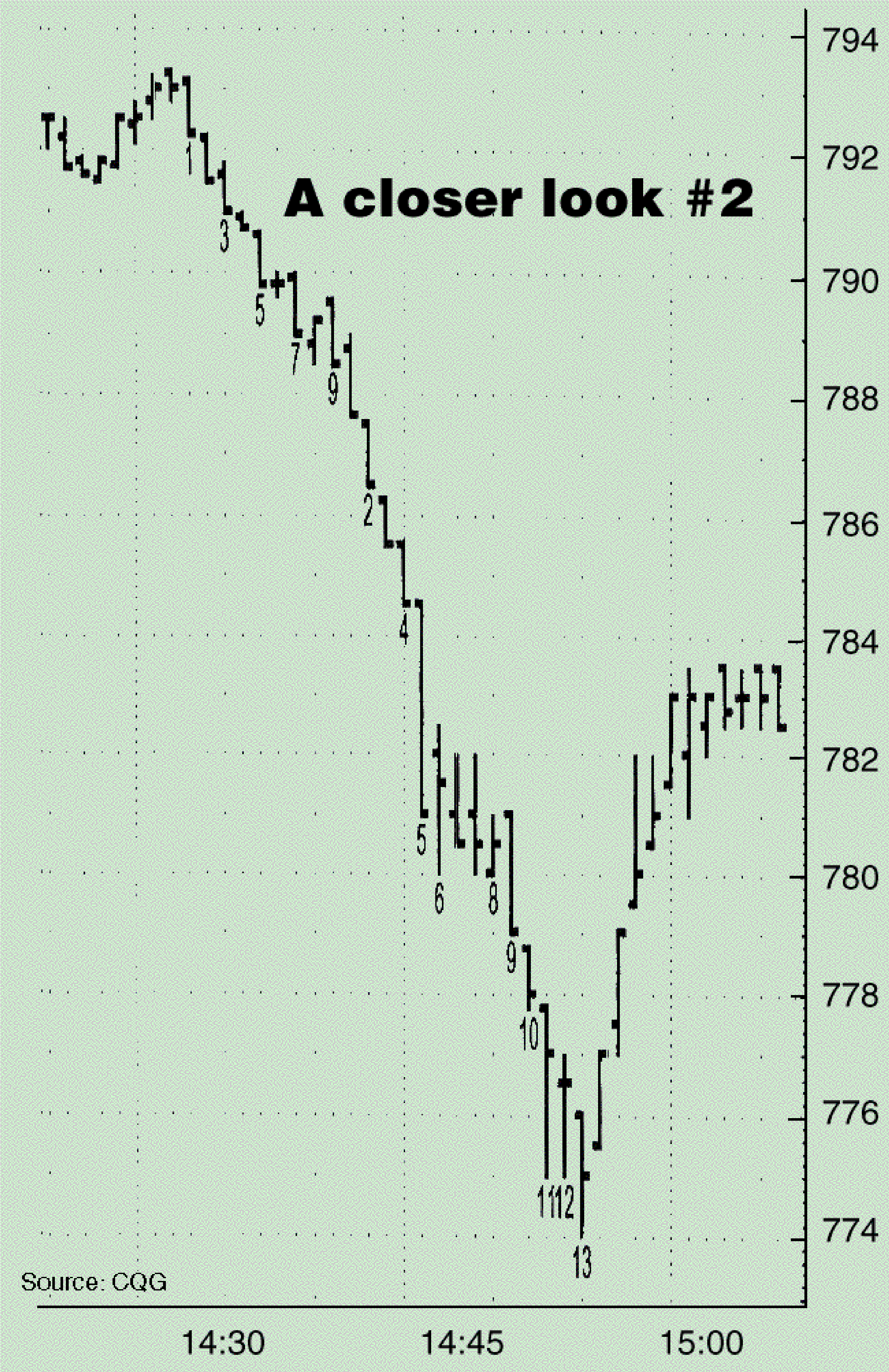

The buy setup and countdown, bottoming at 13.

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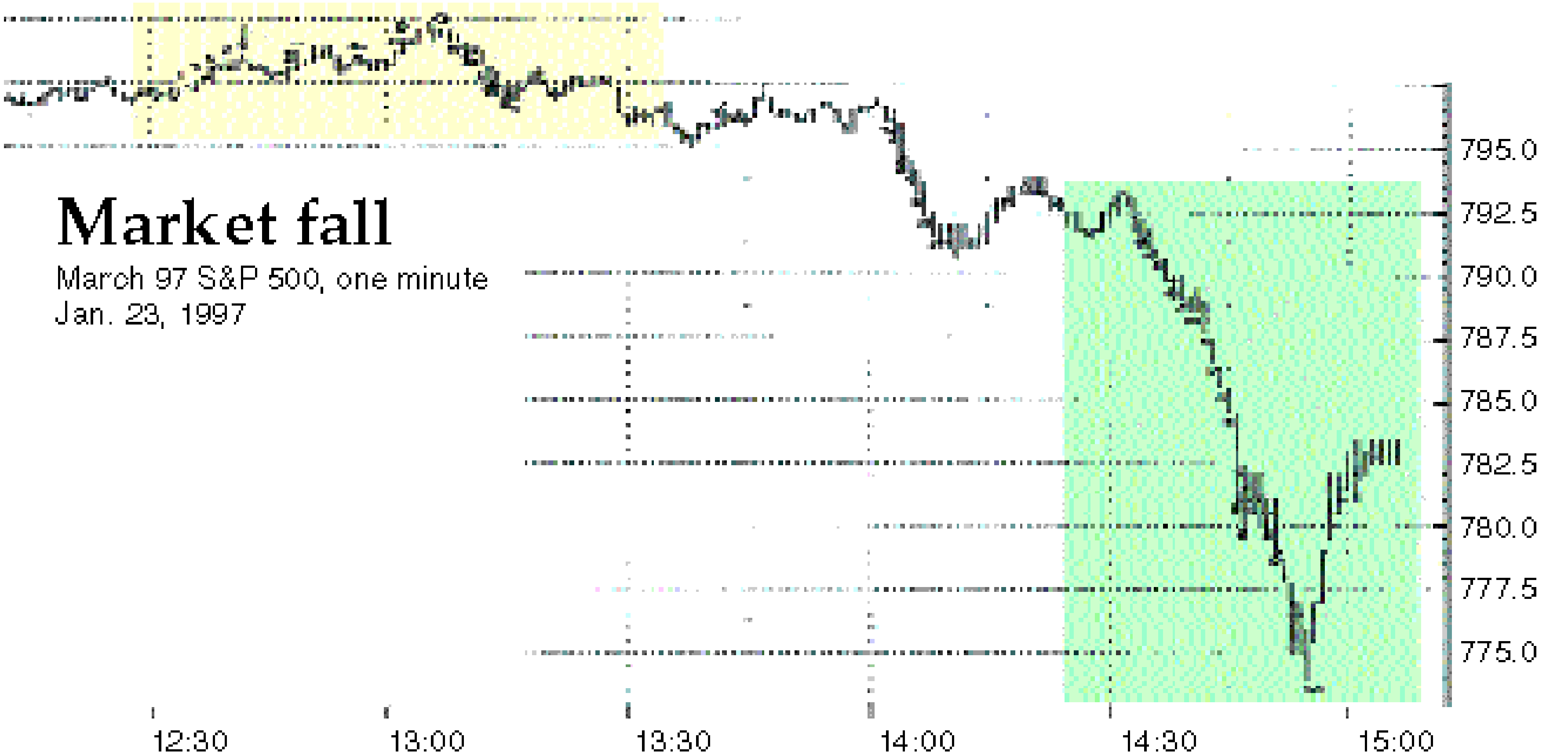

A 27-point plunge in less than two hours on a one-minute bar chart.

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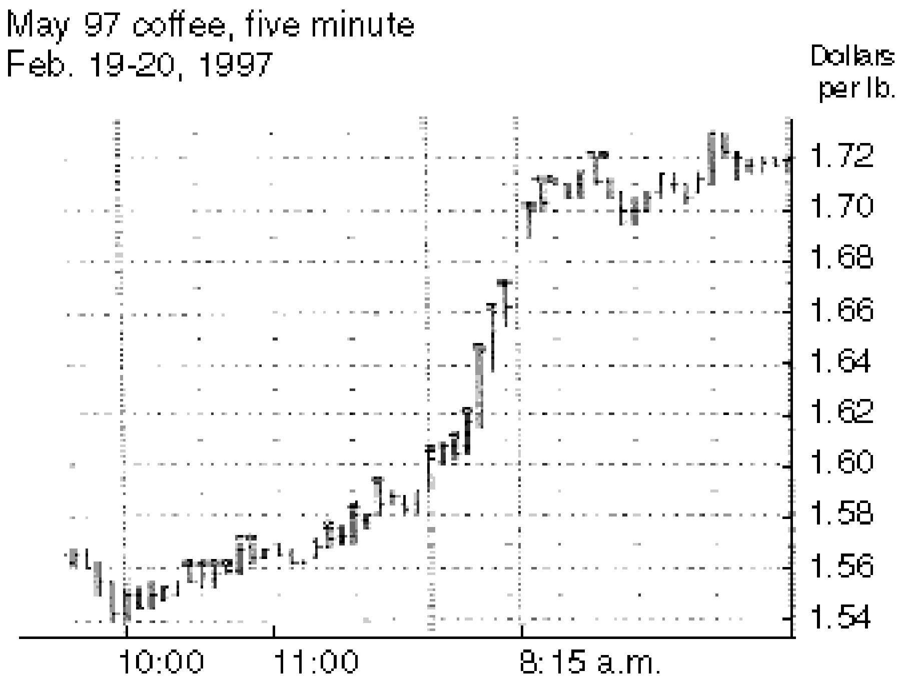
Coffee TD Sequential



Stretching TD Sequential to a five-minute chart.

Longer count

Stretching TD Sequential to a 10-minute chart.

Source: Both charts, CQG

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Taking advantage of the big event

Day-trading takes more finesse than most techniques. Here is a way to take advantage of market reports, etc. without being taken out before the market moves.

By Mitchell Holland

The bottom line for any trading technique or system is its practical application in the real world, regardless of the lovely theories that may have been used in back-testing its strategies.

How reproducible our trading results are often stems not from the right execution technique but from how close the current conditions are to a previous time when a similar trading opportunity last arose and how well we are able to identify these certain conditions -- in other words, the right execution needs the right conditions to be successful.

Like scientists, many trading systems are forced to focus on a narrow set of parameters in this regard because the broader the parameters are, the harder it becomes to reproduce the result. Time also is a factor: The more time that goes by following the last set of results, the less likely it becomes that similar trading conditions still exist.

Some factors that allow you to make a simple execution technique work are:

1) A set of conditions to track.

2) A technique that applies itself to the conditions so you can choose appropriate entry and exit points.

3) A set of results following the use of the technique to see if it works when tested in real time.

Here are the terms and defined parameters for a day-trading approach:

Market selection Market selection primarily is based upon one factor: market efficiency. Because you are looking at a short-term trade, the market must be efficient and respond optimally to your orders. Several factors make markets efficient, the most obvious, of course, is liquidity.

Your association with the trading floors also is key. If the trader on the floor will not or is unable to execute the trades quickly, you lose! Because the bracket trading technique places orders before the markets open, direct floor access is less important than it would be in an intraday technique. But your ability to get filled when the market starts moving is key with this technique.

Perhaps the most important factor to the day-trader is the ability of these markets to process information quickly. Again, experience being the great teacher it is, you can see clearly in a short time whether a market is responding in a timely fashion to changes in important information regarding that market.

Based on these considerations, the Chicago Board of Trade's 30-year Treasury bond market is a good market because it has great liquidity and is perhaps the most efficient of all markets. Not only is information processed quickly, but the ability to get immediate price information and excellent trade execution also makes this a prime candidate for this day-trading technique.

The event Event-based trading means taking advantage of an important upcoming event with the hope it will create an impetus to increase market volatility dramatically.

Events are plentiful in the bigger and more-liquid markets. The art of using this information is assigning some form of a priority to the events that will occur in the near future. Use the dates of important information releases that are bound to cause market moves as a primary basis for timing these trades. In the bond market, these are plentiful and, in many cases, will create the market follow-through you are seeking.

Some important events for interest rate markets, placed roughly in order of significance, include:

1) Federal Reserve Bank meetings and announcements

2) Economic reports, especially critical when released on Fridays before holiday weekends (U.S. employment reports, jobless claims, etc.)

3) Options expirations

4) Currency policy meetings or G7 summits

5) Political announcements

6) Intermarket relationships (historic sell-off in stocks, large oil price changes, etc.)

When the markets appear to become indecisive and choppy, many traders look for confirmation regarding future direction of the market, and the influence of these events rises dramatically. It is your job to determine the event's significance by paying attention to the general mood of the markets.

Volatility The basis behind the bracket technique is to take advantage of contractions in market volatility to create ideal entry points, which act as springboards when the market regains its volatility and breaks out. These contractions frequently are referred to as a "volatility squeeze" -- markets are strongly volatile but experience a day with a small trading range in anticipation of the following day's report or event.

This trade depends upon volatility contractions to execute entries and expansions to execute exits. The conditions that make the trade work solely rely upon your ability to note when it's likely the market will move in your favor but not with the kind of volatility that makes successful entry points impossible.

Caveats This technique also allows for stop outs, which is when your stop is taken out by the trading floor just before the market moves in your favor. These are minimized by proper stop placement and also by the use of a volatility contraction to mark your entrances.

Negative signals Avoiding the trading days when the best conditions don't exist is an important skill that improves the bottom line. After many years as a professional trader, I've had chances to trade futures in many different time periods. Day-trading of any market likely is the most challenging time period to trade. For that reason I more carefully pick my battles when day-trading than I would when trading within another time frame.

The technique After giving all this attention to determining that the conditions are "right," now we come to the technique -- a simple T-bond bracket trade. The trade is done by placing two orders into the market before the open, one to buy and one to sell. The buy is placed above the sell so when one is filled, the other is left in place to become the stop loss.

A short profit target is chosen, and the trade is exited with any profits at the end of the day (regardless of size), or the trade is carried over to the next trading session if it is in drawdown but not stopped out.

The mechanics of this trade are simple. Assuming you have followed the market over the course of several days or weeks, you notice the market appears to be exhibiting a volatility contraction on a day before an important report or announcement is expected. When both the volatility contraction and the appearance of an event of significance are present, you are ready to place your day-trade order for the beginning of trading the following morning.

The orders Two day orders are placed simultaneously for the opening of the following day's trading:

1) Buy the market several ticks above the previous close.

2) Sell the market several ticks below the previous close.

The nearest support or resistance level is used as a basis for the closest order.

The two orders should be placed strategically to allow entry only if the market moves through one of them. At the same time, the order should not be placed any further than you are willing to risk on a single trade (never more than 16 ticks in bonds). This is the critical step but becomes easy when the trading range is contracted enough to allow a low-risk entry with the buy order above the previous day's high and the sell order below the previous day's low.

Let the market enter you into a position. Don't try to double guess or pick direction. If you aren't filled, the orders are canceled at the end of the day.

You exit under any of these conditions:

1) If the market moves more than 16 ticks with you at any time, take profits.

2) If you get stopped out.

3) If the market appears to be ending the day with any profits, exit on the close.

Tale of the tape Some examples over the last few months illustrate where this trade has worked or not worked and the risk or reward associated with the trades on an after-the-fact basis. These are real trades that were executed.

Feb. 7, 1997

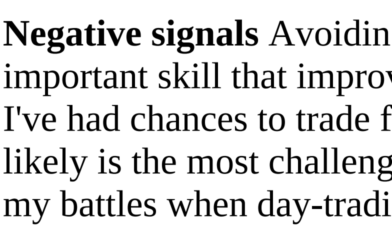
Two orders were placed the evening of Thursday, Feb. 6, prior to the next morning's U.S. employment report release:

1) Buy March T-bonds at 112-06.

2) Sell March T-bonds at 111-19.

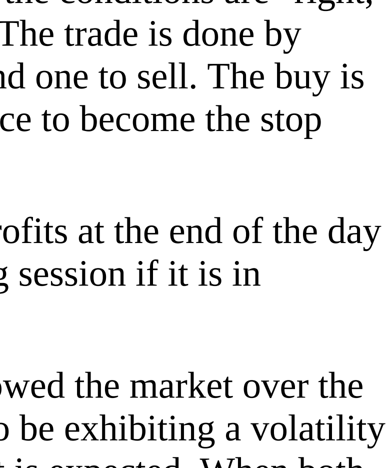
This trade risked 19 ticks ($594) and had a good potential to return between $500 and $2,000 by day's end.

The relief of inflationary pressure from the employment numbers released Feb. 7 and the drop in oil prices took the lid off the bond market for the near term. The only saving grace was a declining Nikkei, which encouraged the Japanese to continue their strong U.S. bond sales.



The employment report at 7:30 a.m. (CST) Feb. 7 got me long with a buy stop in March T-bonds at 112-06 as the market skyrocketed up to 113-00 (see "Employment perks," left). When it hit 112-30, I got out with a 24-tick instant profit of $750. The stop at 111-19 never came close to being triggered, and if anyone got stuck waiting until the close, the trade still pocketed 10 points or $312 profit.

Nov. 1, 1996



After a sharp move up earlier in the week, the market consolidated as I expected (see "Election results," right), and Friday, Nov. 1, looked like a great day to put on a bracket day-trade: There was a Federal Reserve announcement, and the Presidential election was looming heavily on the markets. Two orders were placed for the Nov. 1 open.

1) Buy December T-bonds at 113-05.

2) Sell December T-bonds at 112-26.

If one was filled, the other became the stop. The difference between them was only 11 ticks ($344). One of my rules is I'll take profits if I'm up six ticks at any point after my fill or if I have any profit at the end of the day.

This day-trade in December T-bonds worked like a charm. I was filled long on the open at 113-10 and exited at 113-18 for a quick eight-tick gain ($250 minus commissions per contract). After that, I stayed out and let the market go nuts without me.

Aug. 23, 1996

This trade was interesting because there was a lag time of one day between the volatility contraction on Aug. 21 and event day (an employment report) on Aug. 23 (see "Short and quick,"). Two orders were placed for Friday's opening, using the Aug. 21 range as a guide:

1) Buy December T-bonds at 110-11.

2) Sell December T-bonds at 109-28.

The difference between them is only 15 ticks ($468), which is the size of the stop.

I was filled short 10 minutes after the open at 109-26 and exited at 109-10 for a quick 16-tick gain. The profit was $500 per contract minus commissions.

Summary of results Over five months, I made 14 of these trades; 11 were profitable and only three were losers. Of the three that lost, the amount lost was roughly equal to the gain on any one winner, so the ratio of winners to losers becomes the most important statistic in this case. For this reason, the effect of the commissions and slippage were incidental to the result of this trading technique.

As with any technique or system, this bracketing day-trading concept will work when the conditions are right for the entry or exit points you are seeing. But over time, I've come to realize one key aspect to my success is "if the odds of success don't weigh in my favor, stand aside."

In other words, the key to successful day-trading is not developing entry points; it is knowing when not to trade. Having mixed technical and fundamental indicators may be enough reason to persuade me to stand aside. On the other hand, a small range day right before the release of an important report is enough reason for me to climb aboard.

Mitchell Holland is a full-time trader, futures educator and author of the recent book, The Master Trader. *He resides in San Diego. E-mail: trader@trillions.com.*

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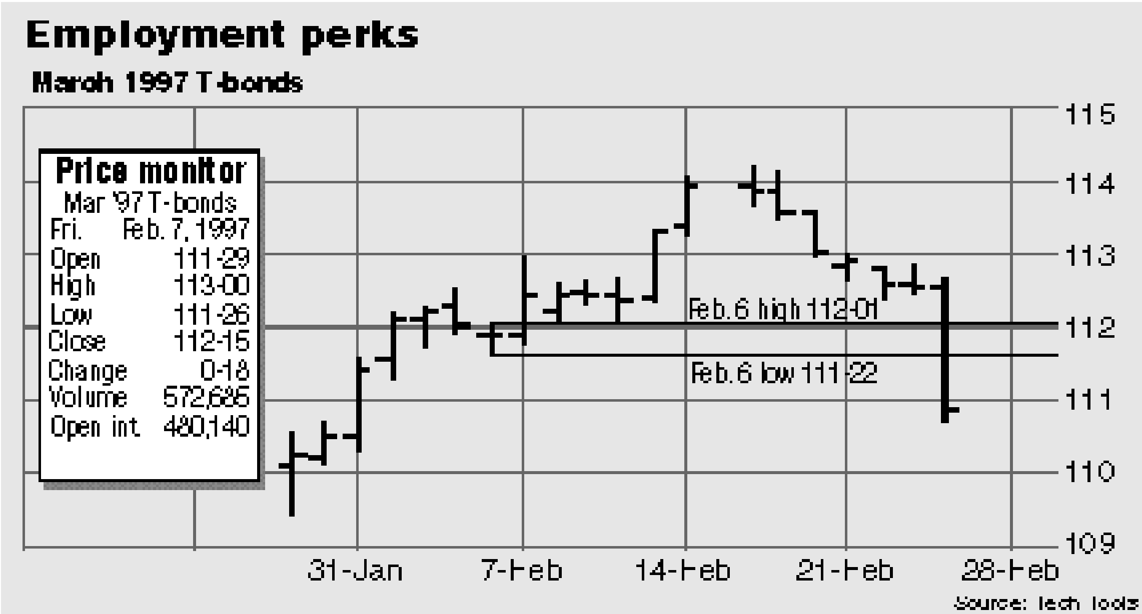
Employment perks
March 1997 T-bonds
Price monitor
Mar '97 T-bonds
Fri. Feb. 7, 1997
Open 111-29
High 113-00
Low 111-26
Close 112-15
Change 0-18
Volume 572,686
Open int 480,140
Feb. 6 high 112-01
Feb. 6 low 111-22
115
114
113
112
111
110
109
31-Jan
7-Feb
14-Feb
21-Feb
28-Feb
Source: Tech Tools

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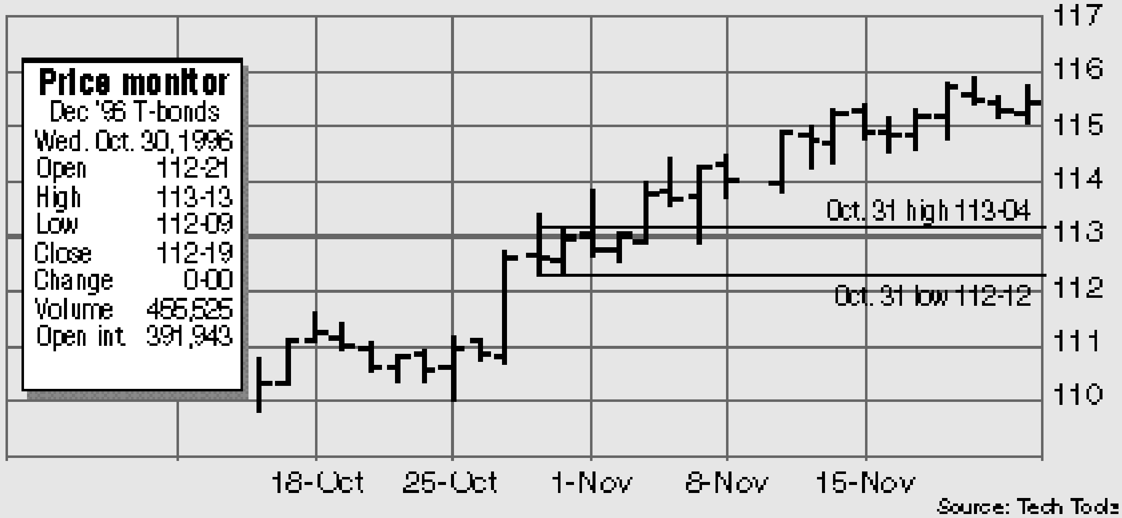
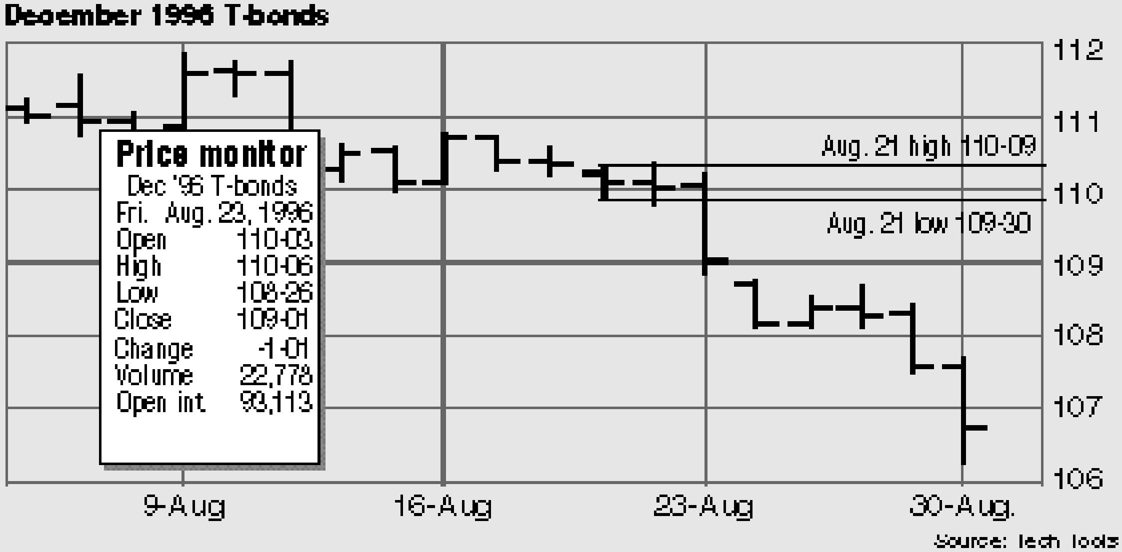
Election results

December 1996 T-bonds



Short and quick

December 1996 T-bonds



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When a professional options trader prepares for the day's market, he looks at much more than technical indicators. Here's a personal account of what it takes to be prepared for the day.

By Jon Najarian

Get ready: How an options specialist prepares for the market opening

At 6:45 a.m. the traffic already is building on the expressways that feed into downtown Chicago.

From inside your car, the only real difference between winter and summer at this time of day is that in summer the sun is already up. In the dead of winter, traders only see the sunshine on vacation. When we drive to work, it's dark; when we're through for the day, it's dark again. But just like the screaming and shoving down in the pits, you get used to it.

I've been trading upstairs and in the pits of Chicago for the last 15 years. Getting up early never bothered me as much as how cold it gets in January -- ungodly cold. But I suppose that's just one more thing that separates the players from the pretenders in this high-stakes game we play.

While I came to Chicago to play football for the Chicago Bears, all I really have to show for that is four pre-season games and a few great friendships. I took my agent's advice and traded a career as a backup football player for a job on the floor of the Chicago Board Options Exchange (CBOE) -- probably the best trade of my career.

While the trading floor immediately was intensely exciting, options trading didn't come easy. My college studies prepared me for a job in advertising or design, not sophisticated financial instruments like options and futures. However, hard work and mentors such as Tom Haugh, general securities principal at PTI Securities & Futures, helped me see the light at the end of the tunnel.

Although I've traded everything from equity and index options to futures and warrants, I've never stopped learning. If you ever think your education is complete, somebody else who's hungrier will figure out a better way and take your edge away.

Morning prep When I get into our offices at 7 a.m., our clerks already have been at work for about an hour. As we trade tens of thousands of options and 1-2 million shares of stock every trading day, it's extremely important to check our options and stock confirmations vs. what our computers say we've traded the pervious day. Mistakes in clearing of either stock or options could cost us thousands of dollars fast, so this trade-checking session is essential for us to start each day with the correct position.

Our main trading room -- the so-called war room -- is an octagon shaped room with 30 running feet of trading desk on the west wall and a 12-foot-by-12-foot conference table in the middle.

The room gets more boisterous and energized with each tick of the clock. Our head of research will hand me the critical overnight news stories that will affect our trading that day. By 7 a.m. he will have run several search programs on a host of computers that incorporate fuzzy and Boolean logic to hunt for key words in news stories that he feels will influence the markets.

The computers assemble and search through news feeds from more than 20 news services such as Dow Jones, Bloomberg and Reuters. These feeds cost us more than $5,000 per month; such is the value of information. However, it's only slightly less important to get that information to our traders as fast as possible. That's why the computers are networked throughout our offices and down to our traders on the floor.

My $1 rule If a story is compelling enough, my next step is to find the average trading range for the stock. If the range between the high and the low is less than $1, I usually take a pass. There simply isn't enough edge for me to jump in and trade when the average daily range of the stock is so small.

Just like most traders, when I have to buy, I pay the offer; when I have to sell, I hit the bid. Therefore, if the stock trades an eighth wide between the bid and the offer, I give away a quarter point to trade in and out. With an average daily range of less than $1, an extraordinary percentage of my trades would have to be right to make any money. Hence, my $1 rule.

Liquidity My next step is to check the average daily volume the stock trades. I can't step in and buy 1,000 shares of some off-the-wall stock without knowing how much trades each day. In some of these stocks, 1,000 shares could represent nearly 20% of the average daily volume. So knowing there usually is enough volume to get in and out without impacting price helps me avoid the dogs.

Timeliness I view the news that is out before the opening in a different way than the news that comes out during the trading day because all option models are forced to make some assumptions as they seek to tell us the correct value of a call or put.

One obvious mistaken assumption is that there is continuous pricing of a given stock or future. Only foreign currencies come close to living up to that presumption. Stocks and most futures have specific trading hours and are closed for several hours of each 24-hour day and over weekends. Therefore, the likelihood of news causing a rapid ascent or descent of a stock or futures contract is greatest before the opening.

CNBC and CNNfn are likely to have many of the 20 different news sources we have, but clearly the more expensive sources have fewer eyes watching for market-moving information and are, thus, all the more valuable. If a story we deem a market-mover comes out on the Dow Jones news wire, for instance, the world will know about it within minutes. If a similar story comes out from some other vendor, however, that information might not be widely disseminated for several hours.

Obviously, the search for market-moving news continues from the beginning of our day straight through until the last trader locks the door. To make sure we stay on top of the stories, we have audio, visual and printed alerts that flash, beep and print throughout the day.

Strategy planning Armed with the news of the day, our traders take turns sitting around our conference table going over our stock and option positions and plotting strategies for the day. We begin with our Chicago Designated Primary Market Maker (DPM) group, go through the rest of our specialist books and finish with our independent floor traders. The DPM unit carries our largest positions in about 30 option classes and, consequently, requires the greatest amount of time to complete the daily review and tactics planning.

Just as it is important for us to know the average daily range of the stock, we have to know the range of volatility for a given security or future. For instance, if a stock such as Micron (MU) has traded in a range in volatility from 45% to 80%, we would be aggressive buyers of call and put options on the lower end of that scale and an aggressive seller of both if the volatility were on the high end of the range.

As we go over the MU positions, for example, we discuss the overnight news that will affect MU. If our position is long gamma (that is, one in which we own option premiums vs. short gamma in which we are net short option premium), and the overnight news is positive, we would plan which calls and puts to price attractively to draw buyers into the market. Conversely, if we were short gamma with the same news overnight, we would bid calls and puts such that we would attract option sellers into the markets.

If there were known news events occurring during the day or after the close (such as new product announcements or earnings), we would keep the options bid higher until the news broke and then sell as aggressively as possible.

By knowing the dates of the news events (government releases, stock dividends, earnings reports, etc.), we can plan to carry long gamma into those situations. If, however, someone is willing to bet that the news will be either so good -- or so bad -- that it will move the stock outside the expected range, we will sell them options and take the risk of going into the news event short gamma. If we've done our homework, the odds will be solidly on our side.

We follow the same procedure for each position each trader has. Between traders in Chicago, Philadelphia and New York, we go through a little more than 100 such positions every morning. By 8:15 a.m. everyone is heading to the trading floor, and I'm sitting in front of the 20 monitors, watching S&P's, T-bonds and CNBC.

Just 15 minutes to showtime.

Jon Najarian is president of Chicago-based Mercury Trading Co., an options specialist. He has traded on the CBOE since 1981, both on and off the floor. Web page: www.DrJsPlanet.com.

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There's more than just knowing how to day-trade. You must know where to day-trade. Good day-tradable markets have certain attributes. Knowing these, and which markets have them, at least puts you in the right arena.

By James T. Holter

Day-trader's paradise

Most traders have their favorite markets. In many cases, though, the same markets you excel in with interday trading, you may perish in with intraday trading. It's vital, then, to know how to pick good markets for your day-trading strategies.

But one market can't be a panacea for all day-trading problems. It's still important to know what you trade, warns William Darby, president and chief executive officer of Darby Trading Consultants in White Plains, N.Y. "Professional traders often find they have a special knack for some markets, whether it's from past job experience, training, whatever. Some people just perform better in certain markets."

Still, if a market doesn't have a wide price range as well as considerable volatility, liquidity and consistency Darby says, it can be a bust for day-trading no matter how well you know it.

Range of opportunity Barring options, it's hard to make money trading a flat market. This stands for any type of trader -- short term, long term, etc. -- but it's particularly true for day-traders. By definition, day-traders liquidate any open positions at the close; they don't have the luxury of waiting to see if tomorrow brings the expected price move. (They also avoid any adverse overnight moves.) So if a market doesn't exhibit a healthy range of daily prices, forget about day-trading it.

"One of the necessities in day-trading is having markets that move enough. If there's no range, then the prospects for day-trading are just terrible," says Ralph Greenberg, president of Exel Inc., a system designer in New York.

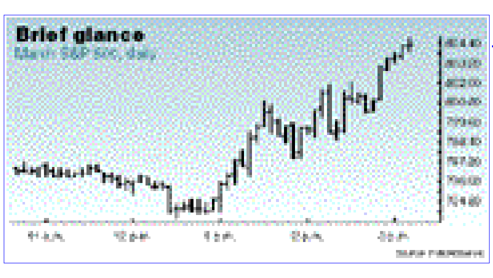
Market menu

It's even better to trade markets with wide ranges within a longer-trending market, he says. Trading when ranges widen, particularly in the direction of an intraday trend, can improve a day-trader's chances. Greenberg likens this to a surfer catching a much better wave if the wave is going with the tide rather than against it.

How large the daily range must be depends on your profit objectives. One guide is using the average daily costs of trading as an absolute minimum. But many markets are tradable using this bottom-line criterion. So you should look for the market that has the largest price range; it should be the best candidate for day-trading.

To compare the typical daily price ranges of markets, you need to standardize their ranges. To do this, find each market's average point range and multiply that by the dollar value of each point.

For example, from Jan. 1, 1997, to Feb. 28, 1997, June S&P 500 futures had an average daily range of 1,098 basis points. At $5 per point, that's an average daily dollar range of $5,490. (See "Brief glance," below, for a particularly strong move in the S&P 500.) The S&P 500 obviously has a considerable amount of profit potential -- or loss potential, as Greenberg points out -- for the day-trader.



Brief glance

Near the other end of the profit scale are Eurodollar futures. From Jan. 1, 1997, to Feb. 28, 1997, the June contract had a daily range of six basis points. With each one-point move worth $25, the average daily dollar range of Eurodollars is $150.

But average daily range merely represents the maximum profit potential of an average day making two trades -- buying at the top, selling at the bottom, not always a realistic scenario. But there's more to consider, which can improve a market's prospects, than just average daily range.

Specifically, there's the simple fact traders can make more than two trades a day. Knowing that, it's obvious volatility, as well as daily range, is an important consideration for day-traders.

Widening the window If a market is volatile, it may be a good candidate for day-trading even if its daily range is lacking.

Consider a market with a daily price range of only $500: If it hits each barrier six times, that's still more profit potential than a market with double the price range that only makes a straight shot from bottom to top (or vice versa).

Buying soybeans at $7 per bu. and selling at $7.09 1/2 earns you a net profit of $475. But selling corn at $2.54 3/4, buying at $2.50, buying again at $2.50 1/4, selling at $2.55, going short one more time at $2.54 and finishing the day getting out at $2.49 1/4 earns you a net profit of $712.50.

But when volatility increases, so does slippage, which means lost opportunity. Darby points to the coffee market in early March 1997: "You would see 50 to 100 points between ticks. That's $375. You're looking at about $700 just to get in and out of a position."

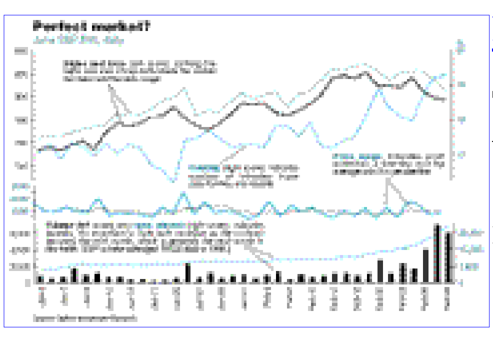
Volatility also is difficult to predict: "Some markets will just go dead," Darby says.

Troy Pugh, a broker with Allendale, adds that also means typically dead markets can suddenly come alive: "Government reports and various seasons can cause an otherwise flat market to move considerably," such as spring for grains and during cattle-on-feed reports for live cattle.

Another strike against volatility is that to take advantage of it, you must make more trades. And that means paying more commissions, Greenberg says. "Commissions are a very large part of the day-trading equation. You don't want to nickel and dime yourself to death," he says.

But despite the risks of slippage and commissions, market professionals agree volatility definitely is a plus for the day-trader.

As Dave Eberhart, analyst with the market research firm Optima Investment Research in Chicago, points out: "Typically, the more volatile, the better. There's more opportunity where there's volatility."



Perfect market?

Take my trade...please Liquidity is the most difficult variable to measure, traders and analysts say. Volume and open interest are quantifiable aspects of a market that measure its activity and level of participation, but other aspects, such as activity of the locals and the intraday amount of commercial participation, are hard to put a finger on, particularly for the upstairs trader.

Some traders contend certain markets, such as energies, precious metals and some softs, are dominated by groups of floor traders who make it difficult for upstairs traders to get decent fills intraday. Floor traders, of course, don't have a vendetta against off-floor traders, they simply are looking out for their own interests. Other attributes of such markets, (for example, low open interest and choppy volume) compound the problem of getting good fills.

"A thinly traded market can be put out of whack by big locals on the floor [or] by large commercial orders coming in," Eberhart says.

Pugh says day-trading only the markets and contract months with the highest open interest is vital "to get the best liquidity." Volume, of course, also is important. When volume is steadily rising and is high relative to its average, it indicates a market may be ripe for day-trading. But also be aware of markets where volume spikes suddenly. Tomorrow may not be as liquid because such spikes often are do to some short-term fundamental factor, Pugh says.

Another factor that often overrides most measures of liquidity is your broker. The point of liquidity is to get good fills, and your broker often has more to do with this than the market.

"Your trading system doesn't have a whole lot of value if you can't get your order down to the floor fast enough," Eberhart says.

Greenberg says short of trial and error in picking the most efficient broker, the day-trader can be sure he calls his order directly to the floor instead of to an order desk.

"Most houses take the order at an order desk," Greenberg says. "First you have to wait for them to answer the phone, then take your account number, then repeat the order back to you, then send the order down to the floor, which prints out and must be ran to the ring [pit]."

No surprises Day-traders can expect most markets that are good day-trading prospects over time to continue to be good prospects into the future. Using the past to predict a market's future intraday profit potential works great, Darby says, unless yesterday's potential was the result of a market shock.

"News events can cause nice, wide ranges," Darby says. "But you can't necessarily expect those same ranges the following day."

In the absence of news events and market shocks, though, daily price range, volume, open interest and price movement generally are stable.

Eberhart, who works a great deal measuring and assessing volatility, points out: "If you have a market where volatility is trending higher, chances are the next day will be more volatile as well."

So once you've found a day-tradable market, you can expect the track to be stable, Eberhart says. It's up to each trader to figure out which way prices will run.

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Market menu

Market	Daily range	Volatility	Liquidity	Consistency
S&P 500	Several thousand dollar daily range	Approaching historical highs	Very active, but costly slippage	Even slow days have potential
T-bonds	Relatively small, but varies	Varies; best during gov't reports	High volume; low slippage	Gov't reports impact range and volatility most
Energies	Depends on fundamentals	Season main factor (e.g., heating oil in winter)	Crude very liquid; heating oil lacking	Only day-tradable at times
Meats	Cattle contracts typically best	Increases with gov't reports	Seasonal; depends on commercials	Also relative
Currencies	Yen and D-mark most active	Market driven; gov'ts play role	Very liquid	Consistency a strong point

Some markets day-trade better than others.

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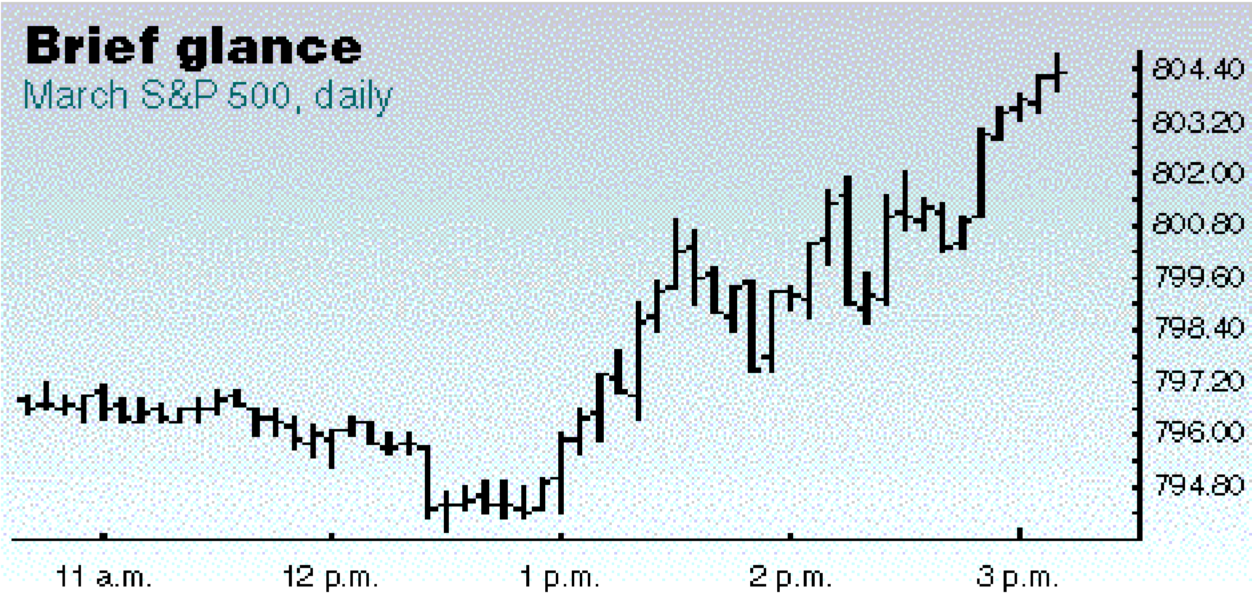

Source: FutureSource

The front month S&P 500 futures contract jumped 1,020 basis points the afternoon of March 5, 1997. This 2 1/2 hour move earned longs a net $5,100.

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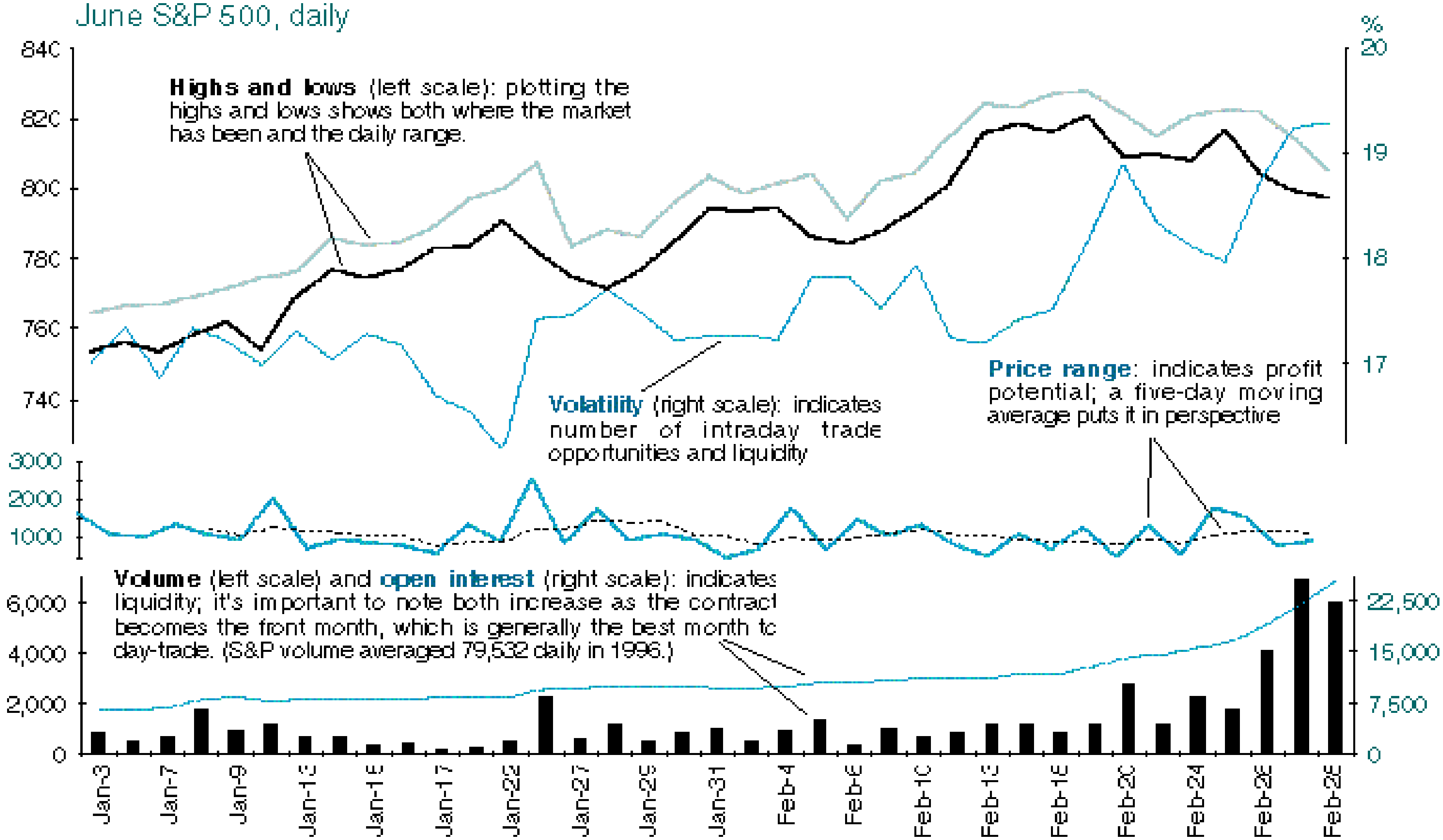
Perfect market?

June S&P 500, daily



Source: Optima Investment Research

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Why day-trade? It's a good way to control risk, for one thing. But it's also a unique game. We'll give you some ideas on how to make the most of the advantages and avoid the pitfalls of day-trading.

By Mark Etzkorn

All in a day's work

The small trader sometimes seems like a candidate for the endangered species list. The flood of institutional money combined with increasingly competitive and volatile markets effectively has squeezed out many smaller-scale speculators, leaving a perception that few opportunities remain for the off-floor commodities trader who does not have Paul Tudor Jones-size pockets.

Fortunately, this is not entirely true. While futures trading certainly is not a game for the uninformed or under-financed, there still are ways for the smaller or more conservative trader to participate in the markets.

One way is through day-trading. Although it has inherent qualities that attract naturally cautious traders, day-trading is not reserved exclusively for the small fry. Many large traders and money managers who handle millions of dollars are drawn to the "clean slate" aspect of day-trading as well.

The upside The benefit of day-trading can be summed up with one word: control. The name of the game in futures trading is risk control, and day-trading provides one of the best methods for limiting market exposure by allowing you to sidestep two potential obstacles: heavy margins and overnight risk.

Margin rates initially are set by exchanges. Clearing firms generally margin customers at a rate in line with the exchange figures -- sometimes more, but never less, because the firms themselves are margined by the exchange. (Rates range from less than $100 per contract to more than $15,000 for contracts like the S&P 500.) If a market moves against a trader, the clearing firm may issue a margin call, instructing the trader to deposit more margin money into his account to cover potential losses.

However, if you only trade on an intraday basis, offsetting all positions by the close, you will avoid expensive margins that might otherwise prevent you from trading. If you have $7,500 in your trading account, you can theoretically buy and sell an S&P 500 contract during one trading session and take your profit (or loss). If you wanted to hold an S&P 500 position over a number of days or weeks, you would have to have at least the minimum margin requirement in your account at all times. If you didn't, you might have to come up with more margin money immediately or risk having your position liquidated. It's important to remember, though, that your system will ultimately dictate the capital you need to trade responsibly; there's a direct correlation between available capital and the probability of success.

Intraday trading also protects you from the adverse effects of events that occur while the markets are closed, resulting in large gap openings. Although some electronic overnight markets now exist, the 24-hour global trading village still is a long way from reality, and you have no control over world events that may turn a market against you while you sleep, whether it's a government affecting your currency position, a war affecting your oil position or a monsoon affecting your rice position.

The catch The other half of the equation, as you might expect, is that day-trading limits your options in other ways; it shuts certain doors while it opens others. The day-trader must adjust profit objectives to the shortened time horizon.

Day-trading rarely will give you the big trade you've been waiting for your whole life, but on the other hand, you might sleep better at night without having to worry about the market opening 10 points against you in the morning. Every day starts with a clean slate. In football terms, day-trading might be considered the grind-it-out ground game vs. the flashy passing game. Ball control vs. big play. You give up throwing the bomb but at the same time remove the chance of the devastating interception.

Laying the foundation Most technical analysis that can be applied to monthly, weekly or daily data will work on an intraday scale, at least to an extent. Indicators that are too noise-sensitive or have a tendency to lag might give a distorted view of a market and lack practical applications.

It's also important not to trade in a vacuum: Don't treat each day as an independent entity; look at the longer-term picture to determine if you're operating in a larger uptrend or downtrend, etc., so you have a better idea of what to expect.

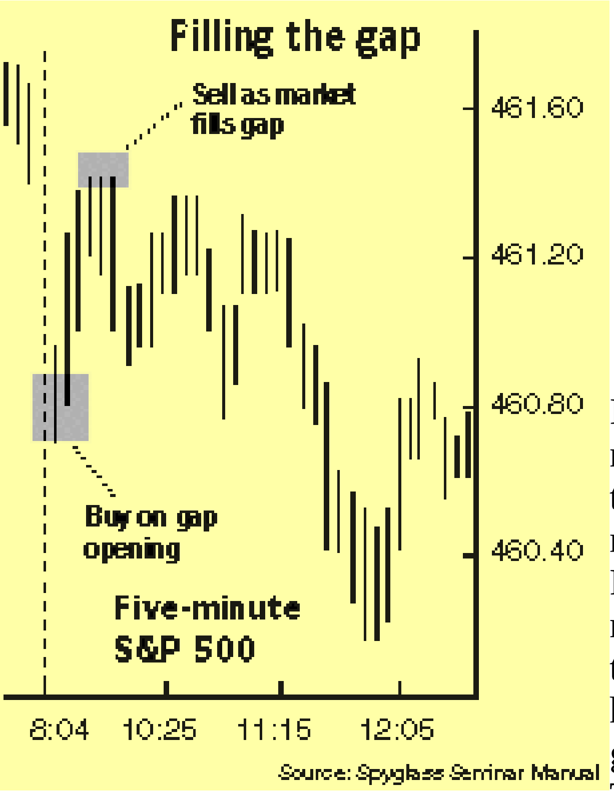
You also must focus on contracts with enough liquidity to get good fills and enough volatility for decent size price moves. Thinly traded contracts with narrow ranges can be exercises in futility and frustration (see "A trader's paradise,").

Opening bell One decision every day-trader has to make is whether or not to trade on the opening. Many on- and off-floor day-traders establish positions on the opening for two reasons. First, the open usually is a heavy volume period. Second, the open usually is one of the most volatile periods, as the market seeks to establish a trend or stable price level.

The opening often will introduce a short-term trend that may either indicate the direction for the day, or give a false signal, in which case the day-trader can "fade" the early trend, that is, buy or sell against it in anticipation of a reversal.

Day-trader, author and system designer George Angell lectures on day-trading the S&P 500 and offers food for thought: One extreme of the day's range usually is contained in the first 30 minutes of trading.

Mind the gap Every trader has heard something along the lines of "gaps were meant to be filled." Like many old sayings, this one has more than a kernel of truth in it. Markets often exhibit a strong tendency to fill price gaps. The gap functions like a magnet, drawing prices back before they can take off again.



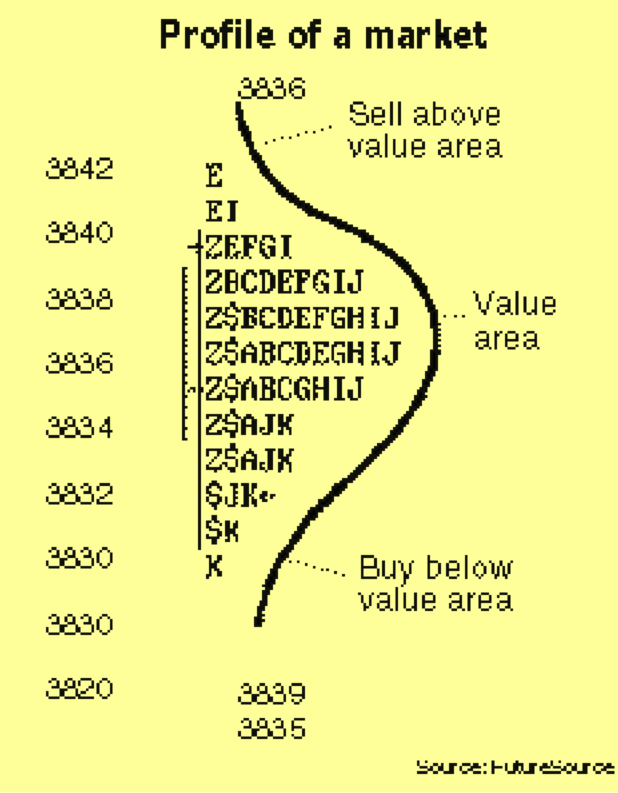
The market gaps lower on the opening but soon rises to fill the gap. Traders had the opportunity to buy the opening and sell as the market rose to fill the gap, or sell the gap and wait for the downtrend to resume.

If you look at an intraday bar chart, you will notice that on gap openings the market often trades away from the gap for the first few minutes, then quickly reverses and "fills" the gap. For example, a market that gaps lower initially may trend downward, leading everyone to believe that a downtrend is in effect. After five minutes, however, the price shoots to the upside, closes the gap and reverses again, trading lower on the day. This scenario presents two options: You could buy the opening and then sell when the market rises back to the gap; or sell as the price fills the gap, expecting the downtrend to resume (see "Filling the gap," left). If the opening gap is not filled within five or 10 minutes, there is a strong possibility the early trend may be the dominant trend of the day.

One advantage to trading the opening: If you hit the market correctly, you can take your profits and go home early. If you're wrong, you still have the rest of the day to look for trading opportunities. But the characteristics of the opening period (high volatility and liquidity) that make it such a potentially lucrative time to trade also make it risky. Unfortunately, day-traders do not have a surplus of time to design strategies and make decisions -- the average exchange trading session lasts six hours.

The flip side of this coin is presented by John Hill Sr., a trader, CTA and publisher of *Futures Truth* newsletter. He thinks the early morning gives too many "false signals" and suggests waiting for the second or third hour of trading to put on positions because the primary trend for the day often establishes itself at that time. This method allows a trader to avoid the uncertainty of trading volatile openings.

Market profile Another popular technique for gaining insight into intra-day price action is the Market Profile, a method designed by J. Peter Steidlmayer and developed in cooperation with the Chicago Board of Trade. In "Profile of a market" (below), the letter designation of each time bracket is placed next to every price that traded within that time bracket. The resulting "profile" shows the distribution of prices over the trading day.



This day's profile exhibits the common bell-shaped curve of the "normal day" profile. The value area represents the range to which price keeps returning.

The main idea behind Market Profile is that market profiles have three basic variations: the normal day profile, the trending day profile and the non-trending day profile. The idealized normal day profile forms the familiar bell-shaped curve, with most of the trading falling in the fatter middle range (the "value area"), with a smaller amount of activity at the extremes of the day's range (70% of profiles fall into this category). In the trending day, the value area will appear at one end of the range. Non-trending days do not exhibit a predominant value area.

When a trader sees a normal day profile forming, for example, he can sell when price moves above the value area and buy when price dips below it. Market Profile is useful in determining the perceived value of a market on a given day and gives the day-trader a method to evaluate the trading landscape he is in.

Another idea is to look at inter-market relationships. Floor traders especially look at tick-by-tick movements in cash and correlated markets, buying or selling when they feel price is out of line with these barometers. The influence of each tick in the T-bonds on the S&P 500 can be very strong on a short-term basis.

Risk control, money management principles and common-sense trading are just as important for day-traders as they are for large-position traders. Take your losses, don't average trades, don't add on to losers and don't overtrade. Just because you're a day-trader doesn't mean you have to trade every day. Wait for good opportunities. Tomorrow's another day.

Pivot profits

William Greenspan is a day-trader who practices what he preaches. In addition to trading, he runs a day-trading strategy school called Commodity Traders Boot Camp Ltd. in Chicago. One of his cardinal rules: "Make 10 points on a million trades -- not a million points on 10 trades." One method he uses successfully is called the pivot technique.

The basic pivot approach involves trading with support and resistance levels derived from the previous day's high, low and closing prices. The idea is to sell when price violates these levels in a break and buy when price pushes through them on the upside. Here are the formulas:

1. (H + L + C) / 3 = P	**Where:**
2. 2P - L = R1	**P = Pivot, H = High,**
3. 2P - H = S1	**L = Low, C = Close**
4. (P - S1) + R1 = R2	**R1 = Resistance level 1**
5. P - (R1 - S1) = S2	**S1 = Support level 1**
	R2 = Resistance level 2
	S2 = Support level 2

Because former resistance becomes future support and vice versa, these levels provide key stop-loss levels. For example, if you sold when the market broke through support level 1, you immediately would place your stop at or just above the support level 1 price. If the market reverses, you're out quickly with a small loss. If price continues to drop, you can follow the market with a trailing stop.

Pivot points

Although these levels sometimes will provide valid support and resistance levels throughout a trading day, their significance diminishes as they are repeatedly violated. The first penetration is the most important.

You also can use the opening range prices and the weekly highs and lows as support and resistance levels.

Mark Etzkorn is a Chicago-based financial writer, researcher and trader.

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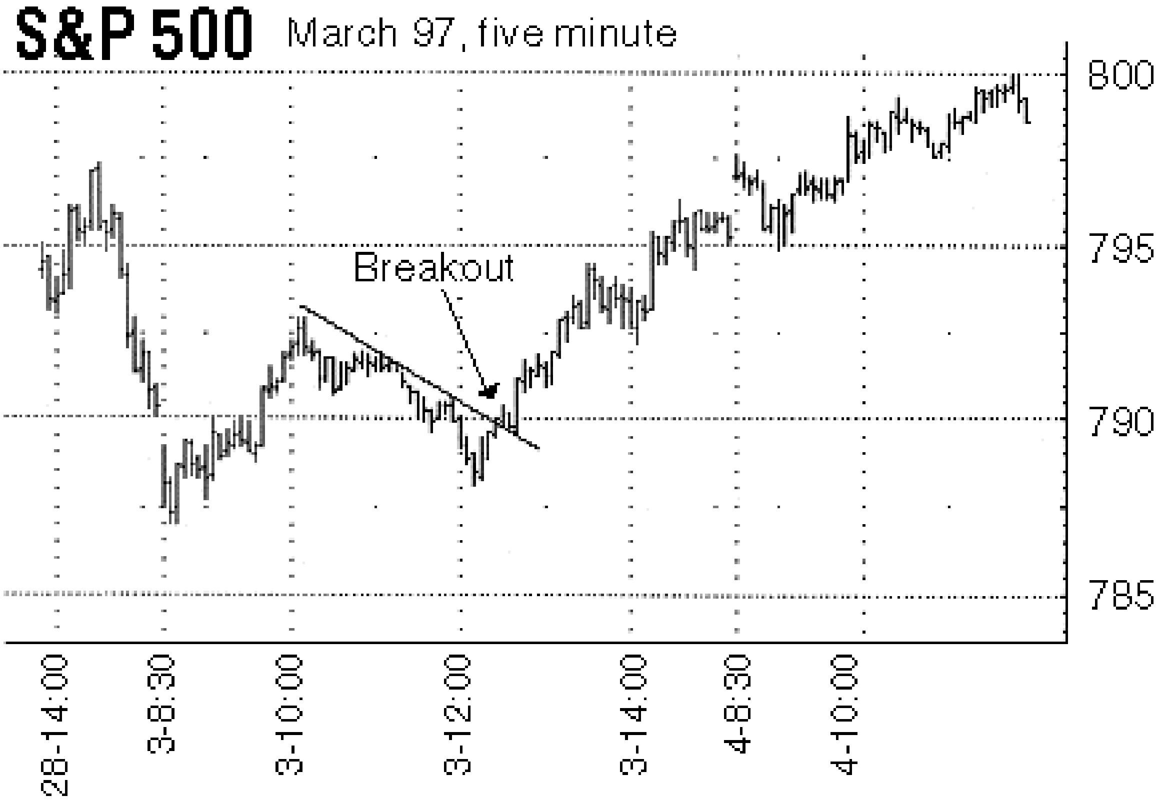
S&P 500 March 97, five minute
Breakout
800
795
790
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28-14:00
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What you need for day-trading speed

Before you can put even stellar day-trading ideas to work, you must have a way to get price data to you and your order to the floor. Here's what the prospective day-trader needs to set up shop.

By Darrell Jobman

Day-traders aren't much different from position traders in what they need to do their business well -- information on which to base a decision, price quotes to determine when to act, a way to analyze this data to turn it into a trading plan and a broker to put that plan into action.

Day-traders just need more of it; they need it faster; they need it more reliably. The magnitude of fluctuations in markets viable for day-trading requires that day-traders deal with changes quickly if they hope to survive.

Unless you're a floor trader, you will need at least a 486/66 MHz PC with 16MB of RAM running a Windows operating system, but most recommend a Pentium with 32MB of RAM and a one-gigabyte hard drive. Macintosh owners will find the field of real-time products to be pretty slim.

From there you have a number of choices for getting real-time prices, information and analysis. You can buy comprehensive turnkey packages or combine programs specializing in certain features. You also must decide which features you need, such as news, specific trading ideas or stocks and options data in addition to futures. At a minimum, you probably will pay for three things:

*** Data feed --** Price quotes must be fast, accurate and reliable. Keep in mind you will make two payments for real-time data: exchange fees and vendor charges. Depending on your situation, delivery can be by dedicated phone line, satellite dish or cable. The number of exchanges or means of delivery will affect your data costs.

*** Analysis --** Whether you want to analyze markets yourself or take trading recommendations from another, you will be paying someone who has programmed the analytical studies or the trading system or has made it possible for you to develop your own.

*** Information --** News services are included in some real-time packages, or news or advisory services may be available as add-on features. While price data and some means to analyze it may be more essential for the day-trader, it's nice to have event news and insights, too, unless you have trading system software that does everything for you.

Futures' 1997 SourceBook lists 154 firms as suppliers of electronic price quotes, 234 providers of charting or technical analysis software, nearly 300 trading system vendors, 45 news services and numerous advisory services or other information sources.

'The Internet is a potential goldmine for traders — if they can find the time to get the most out of it.'

The following is a sample of what is available from a few major providers of real-time products and services for day-traders. Readers also should refer to *Futures' 1996 Guide to Computerized Trading* for more information about real-time products.

For a larger list of firms in these categories and hot links to those with Web sites, check *Futures'* Web site (http://www.futuresmag.com/aboutfm/fosites3.html).

Data sources Signal from Data Broadcasting Corp. (http://www.dbc.com, 800-826-0098) is one example of a data vendor that offers real-time quotes on all futures, stocks, options, cash and international markets for traders interested in investment areas beyond futures.

Signal does not offer analytical studies, although company officials say many are coming with the next release. It does include DBC Newsroom, which gives news, commentary and analysis. Among programs that use the Signal data stream are TradeStation, MetaStock, Aspen Graphics and OptionVue.

The initial cost ranges from $195 to $495, depending on the type of installation. The monthly cost for real-time quotes is $220.

Other major real-time quote providers include BMI (Bonneville Market Information at http://www.bmiquotes.com, 801-532-3400) and Standard & Poor's ComStock (914-381-7000). FutureSource (see below), which covers futures and options on futures but not stocks, also is a data source for TradeStation for $195 a month.

Delayed and end-of-day data also are available, and may be sufficient for some, but most active day-traders will find real-time quotes a necessity.

Turnkey packages The trading packages that have everything in one box run the gamut -- and price range -- from the sophisticated terminals, such as those from Bloomberg Financial Markets, found on the desks of institutional traders, to the units that deliver only basic quotes and analysis and offer other services as add-ons.

FutureSource (http://www.futuresource.com, 800-621-2628) offers two futures versions with more than 50 technical studies plus the ability to add services such as Futures World News, BTU, Platt's Commodity News, Natural Gas Intelligence Daily and Weekly, Pro Farmer and Hightower News. FutureSource Expert, compatible with Windows 95, is $420 a month; FutureSource Technical is $370 a month.

CQG for Windows from CQG Inc. (http://www.cqg.com, 800-525-7082) covers futures and options on futures and requires a Pentium 166 MHz and Windows 95 (24MB RAM) or Windows NT (32MB RAM). CQG pioneered the computerization of Tom DeMark indicators and offers more than 60 studies. A special feature is a link to Excel for custom portfolio management. The monthly cost averages around $585 plus exchange fees.

Other products in this category include Dow Jones Telerate (http://www.telerate.com, 800-334-3813); MarketPro from Market Communications Group and Reuters America (800-810-0111); and DTNstant/Knight-Ridder as well as several other products from Data Transmission Network (800-397-7000).

Analytical software You can break down this area into several general categories:

*** Charting and analysis: Buy and analyze --** Stand-alone software programs can be purchased rather economically and used with live data feeds to produce charts and technical studies. Examples include ASCTrend Software from AbleSys Corp. (http://www.ablesys.com, 510-538-0926); LiveWire (805-646-0094); Candlestick Forecaster (real-time edition) from International Pacific Trading Co. (http://www.iptc.com, 800-444-9993); TradeWind from MarketSoft Research (800-495-7638); and one of the few products designed specifically for the Mac, Trendsetter (800-825-1852).

*** Charting and analysis: Lease and analyze --** Rather than purchase analytical software that will work on real-time data, you can lease it. An example is Aspen Graphics from Aspen Research Group (http://www.aspenres.com, 800-359-1121), which can use seven data feeds (ADP, Bridge, BMI, S&P ComStock, CMA, BisNews, DBC Signal), offers more than 50 studies plus DeMark indicators and costs $195 a month. You also can write your own studies with canned or user-defined formulas.

*** Charting and analysis plus: Buy, analyze, build and test systems --** A popular program in this area is TradeStation from Omega Research (http://www.omegaresearch.com, 800-497-8713). It not only has numerous built-in charting and technical analysis studies but allows day-traders to program and test almost any trading technique or concept they can express in words.

Real-time data formats supported include BMI, DBC Signal, FutureSource and S&P ComStock in addition to a number of end-of-day formats. TradeStation 4.0 currently is offered for about $2,400 (12 "easy" monthly payments of $199.95).

*** Trading system software --** Real-time trading system software also is available on a purchase or lease basis. Sometimes the day-trader has the choice of either, although the purchase price tends to be expensive.

Rather than a one-time purchase of a pricey system that may not turn out to be what you want, the argument for leasing is you always have the latest upgrade and better support at a lower price; if you don't like the system, you can walk away at a minimal cost.

Examples of this type of real-time software include %C-DT Trading System from Creative Breakthrough Inc. (http://www.futures-cbi.com/~creative, 561-776-0895) and Recurrence IV from Avco Financial Corp. (203-661-7381).

* **Options specialty products --** Options trading is becoming a mathematical game that is impossible for the day-trader to play without increasingly sophisticated and specialized computer assistance.

Examples of real-time software for the options trader include Option Station from Omega Research (see above); Orion from Optionomics (http://optionomics.com, 801-466-2111); OptionSource from The Options Co. (800-393-6442); and OptionVue IV from OptionVue Systems International (http://www.optionvue.com, 800-733-6610).

News services News services may be incorporated into packages such as those from Data Broadcasting Corp., FutureSource, Dow Jones, Reuters and others or may be an add-on feature. A broad range of advisory services, weather services and other specialized services are available.

This is an area where the day-trader has a great deal of flexibility in tailoring services to needs. If you have a blackbox real-time trading system, you may not need anything more. If your analysis is event-sensitive or if you are a trader who must have some explanation for why the market does what it does, you might find some type of information add-on service valuable.

Keep in mind a day-trader with a computer and access to the Internet already has access to a world of information. Government reports, exchange data and many other items are free, and the number of services offering data and information on a for-pay basis is growing. The Internet is a potential goldmine for traders -- if they can find the time to get the most out of it.

Darrell Jobman is a freelance writer in Chicago and a contributing editor to Futures *magazine.*

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From a 22-year veteran of day-trading, here are the rules for succeeding in this most difficult of time periods.

By Mark D. Cook

Day-trading: Not what you think

The day-trader is a cross between an extrovert and an introvert with both characteristics in balance.

The introvert aspect is depicted by the disciplined workaholic with a reclusive concentration. The extrovert aspect is depicted by an aggressive, competitive, self-motivated individual striving to be the best in a selective profession.

If you think you have that Dr. Jekyll/Mr. Hyde personality, then you are invited to explore my world -- the world of the professional trader.

I am easy to describe. I have an insane personality that is intermittently interrupted by craziness. Why else would anyone set up a multi-million dollar trading business in a rural surrounding in his great-grandfather's farm house, working five 12-hour days a week as well as a partial six-hour day thrown in on Saturday?

The intermittent craziness occurs when I try to find ways to spend the money. A true test of your success is to make more money than your kids can spend with constant spending influences of a "Honey, can I..." wife -- which always means get out the checkbook.

Why do I do it? It's one of the last bastions of pure capitalism. It gives the same opportunity to a hillbilly farm boy in bib overalls living in East Sparta, Ohio, as it does to an Ivy League university graduate in a tailor-made suit on Wall Street.

Each day I am a creature of habit, going through a daily ritual before the markets open. I outline in detail all three possible scenarios for that day: up, down or sideways. I assign a probability to that scenario and make a written strategy plan, which has been incorporated into a trading fax service that is devoted to teaching people how to trade. Thus, a disciplined trading plan is imposed on me.

Every successful trader must be flexible, alert and feisty. The flexibility must be used to shift from being long to being short literally within seconds. The alertness is used for observing price movements that are an aberration from the norm. Feistiness is the savvy aggressiveness to fight back with a vengeance to regain money you lost. I don't know how many times I've seen people lose money in the morning and quit. My most profitable days are when I lose money in the morning and stay in because I want to get it back.

Once the trading day begins, all of my focus is on my quote screen and three markets: S&P 500 Stock Index futures, 30-year T-bond futures and the S&P 100 Index options (OEX).

All day long I record a diary of the trading patterns for that day. This is a ritual I've done for 12 years, and the diaries have been priceless. Recurring patterns are much more frequent than people realize, and referring to the diaries has reinforced the adage, "If you don't know history, you are doomed to repeat it." The diaries clearly show that trading is actually a composite of many ebbs and flows at different times of the day. They have helped me develop the following set of daily trading rules:

'It's one of the last bastions of pure capitalism. It gives the same opportunity to a hillbilly farm boy in bib overalls living in East Sparta, Ohio, as it does to an Ivy League university graduate in a tailor-made suit on Wall Street.'

1) Do not trade the last hour of the day in the S&P futures market.

The probabilities of a successful trade diminish in this time frame due to the impulsive and reckless buying and selling by institutions just because they didn't get their trading done earlier.

2) If you don't like the trade you're holding, get out.

This is where my emotions do come to the forefront because I hate to lose. Not liking a trade comes simply from analyzing in my mind that this "hated" position has more probability to separate me from my objective of making money and must be eliminated. Have you ever had a feeling of relief after exiting a bad trade just because you were out of a mess? Losing trades use more mental energy than winning ones.

A day-trader must become very mechanical, almost robotic. Many people who have come to the office to observe my trading style have commented that I appear almost emotionless. I believe to show emotion is to show fear: When your hand is shaking so much you can't pick up the phone, the market senses a victim is about to be slain and goes out for blood. This rule has evolved out of this fear factor.

3) After two hours of trading, ask yourself, "Do I feel good about my trading today?"

Once two hours have passed in the trading day, you should have made at least two, or perhaps more, trades but enough to evaluate what you have done. If you can answer "yes" to the question, continue trading. If your answer is "no," stop trading. You can't bring happiness to a "blue" day by trading. Your emotions won't allow it, and a big losing day is likely to be the result.

September 1995 is a true example for me of turning a bad family health situation into a bad financial situation. My father suffered a heart attack. He always was the pillar of strength to me, and to see him in intensive care was just too difficult.

Some people drown their problems with alcohol. My escape is trading, but during that time, my heart wasn't in it: My focus was gone; my energy level was low; my enthusiasm was non-existent. It turned out to be the worst trading month I had had in seven years.

The person who knows you best is yourself. Listen to yourself.

4) All cylinders of the engine must be running efficiently.

Keep in mind, as your trading day progresses, what money you have made or lost. It is much like knowing the score of a basketball game when you are the coach. Day-trading is a job, and your paycheck is determined by your ability. You only can maximize your ability if you have all the information you need to make trading decisions.

If your phone, quote machine or any other mechanical function of your daily routine is out of whack, stop trading. Frustration is the best friend of a losing day. The more frustrated you are, the less efficient your trading decisions will be, lowering the probability of a winning day. Don't fight a losing battle; there is always another day with opportunities.

5) Have complete faith in your indicators.

This is a must for success. Many times your indicators give a buy or a sell signal, and you don't follow it because you just don't have the confidence the signal is right this time. Successful day-traders believe in their indicators but also are aware that nothing is 100% foolproof.

Not taking a trade that is set up using indicators you have developed is calling yourself a liar.

The indicator is a product of you telling yourself to do a trade. When you reject it, you are responding by saying, "Indicator, you are not giving me a true signal." Grade yourself with a big red "F," and go sit in the corner.

6) To anyone who aspires to become a day-trader, observe those who are successful.

Any information you can procure on the trading philosophies, mechanics and techniques of the professionals is well worth your while. If learning from those who have experience cuts down your learning curve time, isn't it worth it?

I've heard people say they were going to learn by themselves. Learning for yourself will work if you have the time and financial resources. Stubbornness and pride can be hazardous to your wealth.

If you do pursue learning from the "masters," do not be surprised to find that there are many different ways to day-trade profitably. Do not try to clone another individual, because your personality is never exactly the same as his. Observe, learn and test the waters to arrive at the confidence level you will need to achieve consistent success.

7) Day-trading is a long-term commitment.

I fervently believe it takes several years to become a true professional. Each year you should become more consistent in your profits and enjoy more confidence in your indicators. My final daily rule means taking every trade and dissecting it. This will provide a roadmap for success by showing you where you have been, which mistakes you can learn from and which situations to avoid.

Day-trading is not easy, but as a business, it can provide the American dream -- financial independence.

Mark D. Cook is a professional trader in East Sparta, Ohio. He has been trading for 22 years and won the 1992 U.S. Investment Championship with a 563% return. Cook offers a fax advisory service, Mark D. Cook's Trader Fax, www.markcook.com, on S&P and T-bond futures and OEX options that is structured specifically to teach people to trade better.

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Day-trading's time has come with the advent of intraday quotes and software availability. Still, some technical analysis transcends time. Here an old pro provides the strengths and weaknesses of applying those to day-trading.

By Jake Bernstein

Day-trading overview

Day-trading, which was once the exclusive domain of the floor trader, is now fair game for all speculators. Inspired in part by large intraday price swings, instant availability of quotes, affordable high-powered computers and competitive commissions, the new wave of day-trading methods and systems has attracted thousands of traders in recent years. The undeniable thrill of trading within the time span of one day is, however, a double-edged sword: one that can hurt as well as heal. To be successful, a day-trader must have the discipline of a machine, the instincts of a fox, the emotions of a rock, the skills of a surgeon and the patience of a saint. (And a little luck wouldn't hurt either.)

What is it about day-trading that attracts so many speculators to the markets? Are there effective methods for day-trading? Is successful day-trading more luck than skill? Is day-trading the proverbial "crap shoot?" Can day-trading be learned? Is the successful day-trader a different breed of "cat" than the successful position trader? Does day-trading offer advantages above and beyond position trading? Read on for the answers.

Day-trading defined In the summer of 1968, after making my first few trades in the commodity market (as it was called then), I learned quickly that floor traders clearly had the "edge" over the public. Floor traders were in the pits where the action was. They knew prices before the rest of us did. They traded for minimum commissions, and they seemed to know the news that affected prices before the rest of us. During one of my visits to the Chicago Mercantile Exchange, I was chatting with a retired floor trader in the visitors' balcony, and he asked what my trading interests were. I told him I was there to learn, that a broker was handling my account and that my knowledge of trading was very limited. He asked me if I was a "position trader" or a "day-trader." I confessed I hadn't heard either of those terms before. He offered the following definitions: A day-trader trades within the time frame of one day, entering and exiting positions within the day but always closing out trades by the end of the day, win, lose or draw.

This definition seemed logical enough to me. But the "old timers'" definition of position trading gave me cause to stop and ponder momentarily. He defined the position trade as a day-trade that ends the day at a loss.

After a few moments the definition struck home, and I laughed. But under the surface of my apparent amusement was an inherent market truth that has not left my mind since that day. Clearly, the ability to take a loss by the end of the day likely may be the salvation of many traders because the vast majority cannot take their losses when required to do so by their system(s), assuming, of course, they even have a system!

Giving up old ideas While many traders strongly oppose day-trading, I disagree. The long-standing "bad press" that has been given to day-trading and day-traders needs to be re-evaluated and abandoned. As I noted previously, computer technology and competitive commissions have changed day-trading forever. In fact, when examined logically in terms of the assets and liabilities of day-trading in comparison to position trading, the balance tilts clearly in favor of day-trading. Here is my list:

Day-trading pros and cons

Pros	Cons
1. No concerns about overnight news	1. Intraday volatility can be significant, increasing risk
2. More effective use of margin	2. Requires close attention
3. Forced exit eliminates riding losses	3. Misses the large "secular" trends
4. Can capture large price swings	4. Often requires live, costly, immediate quotes
5. Takes advantage of emotion based on moves	5. Cuts profits short as well as losses
6. Limited to active markets only	6. Requires active trading, which increases costs
7. Immediate feedback of results	7. Requires "iron" discipline (which most traders lack)

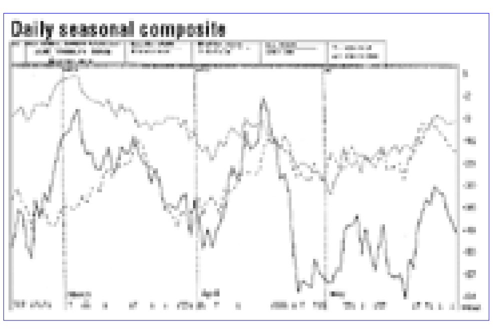
And there may be many other pros and cons as well. Of the above, the most significant pros are (1) forced to exit losses and (2) immediate feedback of results. Think at length about these two cogent benefits of day-trading, and I suspect you will agree with my assessment. But enough of philosophy and psychology -- let's get on with techniques and methods.

Technical day-trader Note that I consider the day-trader to be the ultimate technical trader as opposed to a fundamentalist. While fundamentals may rule a market in the long run, they are not nearly as important within the time frame of a day, other than, perhaps, to result in price swings based on news. The effective day-trader has methods for capturing moves based on the emotional response to fundamentally based news.

In my book, *The Compleat Day Trader* (McGraw-Hill, 1995), I distinguish between four basic approaches to day-trading: trend following and support/resistance trading. All are viable methods, which, alone, mimic what I consider to be the four basic technical methods of position trading. Here is a brief overview of each method as well as its assets and liabilities:

*** Trend breakouts and trend following --** Of all the trading methods, following new trends or buying on breakouts to the upside and selling on breakouts to the downside ultimately may prove to be the most effective. In so doing, a trader follows prices higher or lower, taking stock in the belief that "new highs beget new highs" and "new lows beget new lows." Breakout systems date back to the excellent work of Keltner in the 1960s who pioneered various methods for taking advantage of price highs and lows for a given time frame. "S&P 500" (right) shows the ideal situation for a day-trader who buys a "breakout" of resistance. The good news here is although buying breakouts to the upside or selling breakouts to the downside tends to work well, it is psychologically difficult for most traders to do, and it requires traders to reverse positions when wrong. There are numerous methods for finding, validating and managing the risk in breakout systems.

*** Support and resistance trading --** This approach appears to make the most sense to traders. It involves two aspects: First, a trader must determine the underlying trend of the day and second, once the trend has been determined, a trader must determine the technical support level in an uptrend and the technical resistance level in a downtrend. When the trend is defined as up, a trader will buy at support levels, and when the trend is defined as down, a trader will sell at resistance levels. Profit taking and risk management strategies accompany this approach. While you may think this approach is obvious and self-evident, few traders actually can define the above terms operationally.



*** Daily seasonal trading --** Very few traders use this approach, yet I think it is a viable and worthwhile method. The pioneering work of Art Merrill in his classic book, *The Behavior of Prices on Wall Street*, clearly demonstrates the statistical reliability of pre-holiday behavior in the Dow Jones Industrial Average. Merrill showed that the odds of a higher-price close on the day before major U.S. holidays were not only very high but also statistically significant. Yale Hirsch in his outstanding book, *Don't Sell Stock on Monday*, demonstrated the value of using day-of-week statistics for market timing and trading. I have extrapolated from both of these works to determine the percentage of time the various futures markets have closed the day higher or lower than the previous daily close. Naturally the reliability of such data is a function of the data history. "Daily seasonal composite" (above) shows a portion of the daily seasonal futures charts I have developed for this purpose.

*** Daily sentiment trading --** The pioneering work of R.E. Hadaday in developing his Bullish Consensus indicator was instrumental in my development of the Daily Sentiment Index. The index provides a measure of public sentiment on a daily basis. This allows day-traders who follow a contrary opinion approach to fade the public sentiment when it reaches to levels that are too high or too low. The theory is that when daily sentiment is at 90% bullish or more, the public will be wrong, and hence, the day-trader will look for timing signals to trigger short-side entry and vice versa when the sentiment is 10% or lower.

Risk endures These are the major technical, philosophical and psychological issues the day-trader faces. They don't differ significantly from the issues that face the position trader. The only major difference is the time frame.

Because our world is growing rapidly smaller, and because market moves tend to be larger now within the smaller time frames than ever before, day-trading is not only viable and manageable but also preferable in many cases for the reasons cited previously. Of course, the viability of day-trading methods does not negate the risk of trading. Risk always lurks under the surface. No trading method is complete without an accompanying method for managing risk and dealing with the reality of losses, commissions and the cost of quotes, equipment and time.

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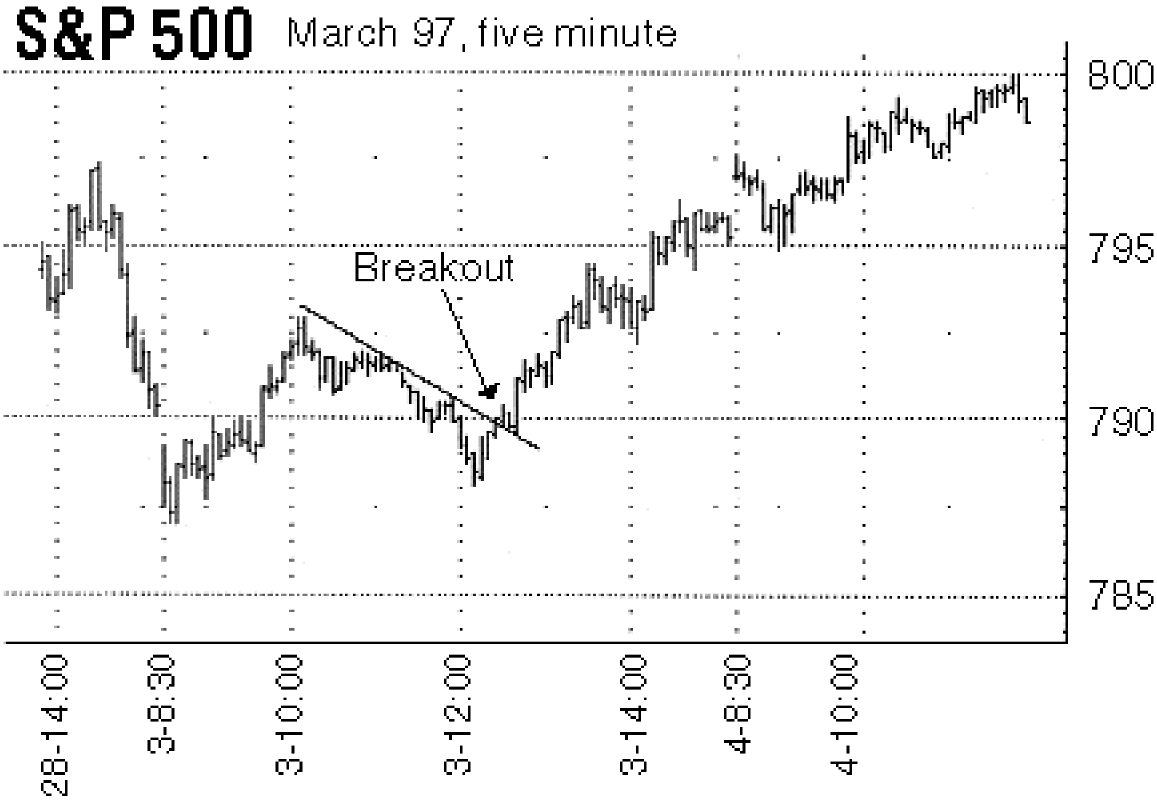
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800
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28-14:00
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3-12:00
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4-8:30
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More important for the day-trader than others is to have the proper 'team' in place. You especially need a good floor broker who can execute your trades in a heartbeat. But, you must pay him well.

By Chris McGinnis

Key to day-trading: Have your 'team' in place

Day-trading is a very serious business; if you don't have all the right ingredients in place before you begin trading, you're dead.

One of the most important aspects of the day-trading business is your "team:"

* Your broker
* Your trading advisor
* Your live quote feed
* Your trading software
* Your back office (clearing firm)

Best broker If you think you're going to be doing size -- 10-100 contracts -- then you must have a great relationship with your broker. The broker is just as valuable as the methodology.

Before the opening bell, I'm in contact with my floor broker to find out what has occurred in the overseas and night sessions and what information is coming out that could affect the markets. I never trade in the face of information. You shouldn't either unless you understand what could happen if you're wrong.

The broker is my eyes and ears on the floor -- after all, that is his job. I pay my broker well; however, I expect him to look after my best interests. *Never select a broker on the basis of cheapest commissions.*

I also expect excellent executions on my orders, and I get them. I picked my clearing firm because of its commitment to the client. My clearing firm also allows every client electronic order placement directly to the trading floor with the "ZAP" system, which is cutting-edge technology and the future of day-trading.

With the pace and stress involved in day-trading, it's essential to your style to trade within the capabilities of the broker and clearing firm so you can eliminate from your trading the worry of order placement and execution. For me, it's important for the brokerage firm to have great floor presence, offer 24-hour access to my account and have a fast back office.

When it comes to floor brokers, I use one who has years of experience in the pits and understands my needs, which fosters a special relationship because of his patience and concern for all of my clients. Friends like these in the pits are extremely important for an off-the-floor day-trader to be successful.

The trading way With a great team in place, next you add the trading methodology. Anyone trading the markets should learn and understand as much as he or she can about what to do before trading begins. It's an outrage to pay a vendor a steep price for a system when you don't know how or why it performs as it does.

The markets are based upon supply, demand and psychology. To trade, you must be aware of many different scenarios and factors that will occur every day.

The first item your methodology must have is a strict money management system. I don't care what you think about the market -- you need to know where you are getting out before you get in and what is the maximum loss you will sustain.

I do not go into the market, for example, unless certain psychological price levels, like 50s, hold twice. Understand that in the United States we are brought up to round numbers off. (If the cab ride is $4.30, we say, "Make it $5" and add another 50¢ for a tip.) Most of the time we round off to psychological numbers like 25, 50, 75, 100. The big ones are 50 and 100.

The same thing occurs in the markets every day. I challenge you to go over your charts -- you'll find that markets hold big psychological points every day.

When you begin to understand this, you'll start to see there are more desirable numbers off which to buy and sell. But the markets are funny; each day the same patterns occur and it is our job to react when this happens.

Every day the market goes up, down, up, etc, which is called backing and filling. The market backs and fills within a certain mathematical number every day (at least most of the time), similar to a Fibonacci parameter.

By knowing this occurs every day, I never want to get into the market unless I'm as certain as possible that it is finished backing and filling. In the methodology used by my company, if the market has backed and filled 1.45, held psychological points twice, and the pattern we are looking for has occurred, we are getting ready to execute a trade.

In many respects, day-trading is not much different than war -- if you are not totally prepared to react to something you've been waiting for, you should not be trading.

Let's assume you are ready to take a long position. When executing a trade, you need to know exactly where you're going to get out, both on the upside and downside. This should be done systematically through strict money management techniques.

The market does not know where your stops are unless you are doing size. When in the market, however, your broker should be aware of your trading strategies and understand exactly where to trail your stops the second you get into a position. You should not have to pester your broker with stops; if you do, you have no game plan.

Never trade without a game plan. Paying money for a computerized trading system and a live quote feed and waiting all day for the system to issue a signal is not a game plan; it's an insane way to trade. If that's the case, give your money to a professional to trade.

My methodology looks at two different time horizons. The first is a long-term, 90-minute time frame in which we get an idea for the trend. (Note: Only trade when you know the trend.) The second time frame is a shorter-term, 13-21-minute period to get our entry.

I use my long- and short-term charts, along with my brokers' assessments of the markets, to form the basis for my trade. I react only to the market; I never give my opinion.

My methodology uses anywhere from $325 to $1,500 stops. I like to use a bit larger stops when trading the S&P 500 Index futures. However, stops are a personal decision and one you will need to evaluate to determine the amount you can handle.

Finally, never hold trades overnight because the second you let your guard down and forget you are a day-trader, it's likely you'll get slaughtered.

Chris McGinnis is president of Tradingroom Inc. (TRI), a trading advisory service in New York that provides free daily updates via the Internet (www.tradingroom.com).

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