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HOW TO GET THE MOST OUT OF THIS BOOK

This book is designed for beginning, intermediate and advanced traders. The authors in this book are leading experts in trading options and stocks.

As you read this book, you will be exposed to multiple strategies that have high probabilities of success and/or high profit. Most of the strategies in this book are divided into three sections:

- **“The Game Plan”** – An introduction to a charting technique. The strategy is then thoroughly explained along with illustrations and examples.
- **“Special Offers”** – If you really like a strategy, you can follow the presenter and the strategy. There are thousands of dollars’ worth of trading tools, indicators, training and mentoring services, books and videos available at steeply discounted prices.

In short, you will have all of the information you need to trade your new favorite strategy tomorrow. Some of the things you will learn in this book are:

- How to Reliably Back-Test Any Options Strategy
- 5 Steps to Identify the Best Options to Trade
- How Warren Buffett Identifies Stocks He Wants to Buy
- How to Capitalize on Corporate Earnings Reports with Options
- How to Use Order Flow to Spot Unusual Options Activity

At www.TradingPub.com, it is our sincere hope that you take away several strategies that you can use when you are done reading this book. You will also learn about markets that you currently don’t trade, and you will find out if they are suited to your trading personality.

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READING ORDER FLOW FOR UNUSUAL OPTIONS ACTIVITY: WHAT ARE OPTIONS AND WHY IS READING ORDER FLOW IMPORTANT?

By James Ramelli, AlphaShark.com

An option is a contract between the buyer and the seller. There are two types of options: calls and puts.

Calls give the buyer the right, but not the obligation, to buy a specified stock or financial instrument (the “underlying”) at a specified price (the “strike price”) on or before a specific date (“expiration”). The buyer has the right to buy the underlying at the strike price, and the seller has the obligation, but not the right, to sell the underlying should these conditions be met.

Puts give the buyer the right, but not the obligation, to sell the underlying at the strike price on or before expiration. Put buyers have the right, but not the obligation, to sell the underlying stock (or other instrument) at the strike price on or prior to expiration. Alternatively, put sellers are obligated to buy the underlying at the strike price should a buyer choose to exercise these rights.

So what factors determine how these options are priced? Six factors, or price inputs, determine an option “premium:”

1. The stock price
2. The strike price of the options
3. The time remaining until expiration
4. Dividends

5. Interest rates

6. Implied volatility.

In general, the more a given stock fluctuates in price on a daily or weekly basis, the more expensive its options will be, and vice versa. Options usually tend to be more expensive prior to earnings reports and other major announcements but decrease in price sharply after the announcement, once the “uncertainty” has been removed. A good example of this is biotech stocks and drug announcements.

Options are traded for one of two reasons: as speculation, or to hedge against a stock position.

Options are bought as a speculation that a stock will move in a certain direction. Calls may be purchased because a trader believes the stock will move higher prior to expiration. Alternatively, puts may be purchased because a trader believes the stock will move lower prior to expiration.

The terms “in-the-money,” “at-the-money,” and “out-of-the-money” are used to describe the relationship of an option’s strike price to the price of the underlying stock. A call is in-the-money when the stock price is above the strike price. Alternatively, a call is out-of-the-money when the stock price is below the strike price. As you might guess, if a call is at-the-money, its strike price is equal to the stock price.

The inverse is true when looking at puts: if the stock price is above the strike price, a put is considered to be in-the-money. A put is out-of-the-money if the strike price is below the stock price, while the at-the-money definition is the same as for calls.

Options are also purchased to hedge against stock positions. Each day, I watch over 2,000 trades in real-time as they hit the tape. I always try to determine, are these orders a hedge against a stock position, or a speculative play? In the eleven years I spent trading on the floor, I learned how to “Read the Tape.”

Most certainly a combination of art and science, it is a skill I've honed over the years. A large part of my trading strategy is based on my ability to do this. By watching for big block option orders, dubbed "unusual options activity," I try to determine the positions of Paper. "Paper" is term originating from the trading floor, when orders were actually written on paper and run to traders in the pit by clerks. It is used to describe large institutions such as hedge funds, mutual funds, or large banks. In other words, institutions who have access to better information – even "insider" information – than your average trader or investor.

When trading off of unusual option activity, I only want to take trades based on orders I believe to be speculative plays. Given the sensitive, and even illegal, natures of their positions, hedge funds tend to be a secretive bunch. Thus determining if these trades are speculative or a hedge is like piecing together a puzzle.

Let's put it another way: what if you could have taken the same trades as Raj Rajatnam, or SAC Capital's Steve Cohen, the moment they were put on? I'd go to jail for insider trading, you might say? Not so fast.

The moment an order hits the tape, it becomes public information. I can trade off it, based on the fact that I believe someone placing such a large bet has access to insider information, and it is completely, 100% legal. This isn't a matter of debate, or speculation, ask any SEC lawyer you know. This is why I trade unusual options activity. *And this is why it works.*

THE UNUSUAL OPTIONS ACTIVITY TRADING PLAN

There is no secret to becoming a profitable trader, and you should be skeptical of anyone who tells you otherwise. That being said, the techniques I've outlined in this text served me very well in my trading career and without them I would not have made the money I did.

Reading order flow and watching unusual options activity continues to be one of my most profitable techniques, just like it was on the trading floor. I had two very profitable years in Apple stock when my net profits in AAPL were over a million dollars. Once a week for a year,

a Merrill Lynch broker would walk into the pit and sell AAPL put spreads. His acronym was “HES,” and whenever I would see him coming, I would know to get long and sell volatility. How did he know? No clue, but by watching him I made quite a few profitable trades.

By combining order flow with technical indicators like the Ichimoku cloud, I devised my OCRRBTT trading plan to trade profitably off of the floor.

THE OCRRBTT TRADING PLAN

Pronounced “Oak Ribbit,” this trading plan will give you a step-by-step method for breaking down unusual option activity. After evaluating unusual trades with this plan, you will be able to decide if you want to follow it or ignore the trade altogether. The letters in the acronym stand for:

- Open interest
- Chart
- Risk
- Reward
- Breakeven
- Time
- Target.

Here you will see the importance of each of these elements in the plan.

Open interest: The first thing you need to look at is if the trade volume is bigger than the current open interest in that line. If it is, this means that this is an opening position and is worth taking a look at. You don't want to buy an option on unusual activity if it is really just paper covering a short. Only consider trades where volume is greater than open interest

Chart: This is the second most important element of the plan. Once an unusual order is confirmed to be an opening order you must then look at the chart of the underlying stock. You need to ask questions. Is the stock in a strong bullish or bearish trend? Is there support or resistance at the strikes the institution is trading? Is it more likely they are speculating on more upside or downside or could they be hedging? The answers to these questions will help you determine if the trade is speculation or a hedge. This will keep you from trading against the institution when you actually want to trade with them.

Risk, Reward, and Breakeven: Once the direction of the trade is determined, you have to evaluate if the risk vs. reward profile of the trade the institution executed is in line with your risk tolerances. Some trades they take could be far too risky for the average retail trader. However, since you know the direction the institution is betting you can tailor a trade that has the right risk setup for you. The risk of each trade must also be measured against the potential reward. If the institution is risking \$5 to make \$1, this is a trade you would want to avoid. You should also always be aware of the breakeven of each trade. If there is significant support or resistance at the breakeven point, you may want to consider another strategy.

Time and target: Always be aware of potential catalyst events that might be near. You want to know if paper is playing the overall direction of the stock or if they are playing a near term catalyst event like earnings, drug announcements, or new product launches. This might factor into your decision to take the trade or not. Once you have your time horizon set you want to pick a profit target. Are you leaving this trade on to expiration? Taking off half at a double and letting the rest ride? Knowing the answers to these questions at the onset of the trade make it easier to manage going forward.

PUTTING THE PLAN TO WORK

Once a trade hits the tape, a trader must use the OCRRBTT trading plan to analyze the setup and determine if it represents an actionable trading opportunity. Let's look at the example below and determine if it is a trade setup that we actually want to take. This order hit the tape on June 16th 2015.

```
OptionHacker (08:49:38 AM):
SWEEP DETECTED:
>> BULLISH 5000 CAG Jul15 39.0 Calls $1.08 ASK MULTI 09:49:18 CBOE 837 x
$0.9 - $1.05 x 387 CBOE ABOVECLOUD Delta=44%, SWEEP /
OPENING OI=796 $38.29 Ref CHART
```

Before running this trade through the plan, we need to understand the information we have.



We are able to get a lot of information from order flow. We can see how many contracts this trader bought, that it was a \$540,000 bet and that the trader that bought these options paid through the market maker's offer to get filled. Although all of these things make this trade interesting, they still do not necessarily qualify it as an actionable setup.

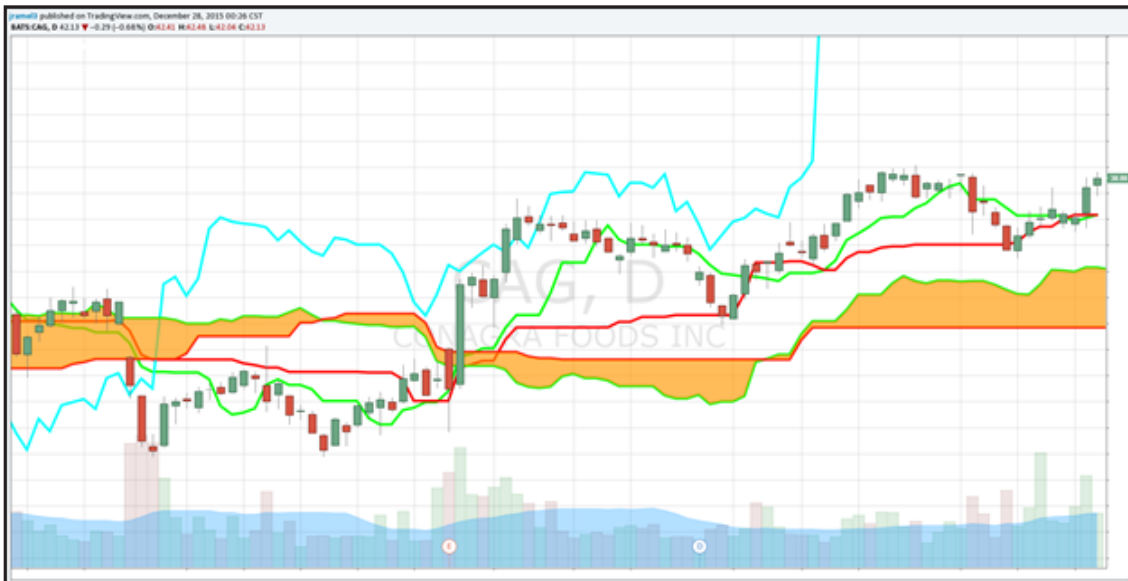
To make this determination we must evaluate this trade using the OCRRBTT trading plan.

Open Interest: Was this an opening position? This trade is labeled opening, so there is no doubt it was an opening position. If for some reason the trade was not labeled opening, we would still be able to confirm that it is because the volume of 5,000 contracts is greater than the current open interest in the line of only 796 contracts. With open interest smaller than volume, there are not enough open contracts in the line for this to be a closing trade. It is confirmed opening.

Chart: Does the chart indicate this trade is more likely to be a hedge or a speculative bet?

We need to confirm that the underlying trend of the stock supports this as a speculative bet. If it does not, the trade may be a hedge and it is less likely to be actionable. To do this, we will use an indicator called the Ichimoku Cloud. It may look intimidating, but for this purpose a trader only needs to know that anything trading above the shaded area on the chart is in firm bullish territory and anything below it is in bearish territory.

Here is the chart of CAG on the Ichimoku Cloud the day these calls hit the tape:



We can see that the stock is trading above the Ichimoku Cloud and is in an established bullish trend. This does not confirm with 100% certainty that this order was indeed a speculative bet, but it makes it far more likely that this is the case. With the trend supporting the idea of this trade as a speculative bet, we will move on to the next part of the analysis.

Risk and Reward: Does the potential reward justify the risk? This is a very large trade in what is generally a boring stock. ConAgra (CAG) doesn't usually get much unusual activity, so if the risk and reward setup makes sense it might be a trade that we want to take. This is an outright call buy, and a trader knows that they can never lose more than \$1.08 in this trade. This translates to \$108 in risk per one lot with what is a technically unlimited upside reward potential. This sets up for a good reward-to-risk setup, and a trader can take this trade.

Breakeven: Where is the breakeven point in this setup? These options are just out of the money and are being bought for \$1.08. At that strike price, this trader's upside breakeven is \$40.08, or about 4.6% higher than the stock's price at the time of the trade. This is only a 4.6% move to the upside. That is not an unreasonable move. With that in mind the setup becomes even more attractive.

Time and Target: What is the trader expecting? In this trade, they are looking for a move to the upside of at least 4.6% by July expiration. Since the trader bought the July \$39 calls, we will buy the same ones. A trader should never trade a different expiration or price target than the institutional trader. Remember, they have better information than us.

Everything about this trade sets up well. All of the evaluations in the OCRRBTT trading plan point to this being an actionable trade setup.

THE RESULT

This trade ended up being a fantastic winner. The trader's motivations behind this trade become much more clear three days later when news breaks of activist activity in CAG.

Look at how the stock responded to the news:



The stock gapped to the upside and these options exploded in value. Anyone looking at the reaction in the stock might be surprised by the huge move to the upside, but those paying attention to unusual options activity were alerted to this potential move three days before it actually happened.

The options that the institutional trader bought saw an enormous move to the upside, trading as high as \$6.20 before expiration. This means that at the highs, this trader would have profited \$2.56 million dollars at the highs. Look at a chart of the options below.



A retail trader who followed this trader with a 20 lot of these options would have profited \$10,240 at the highs. This is a perfect example of how a retail trader can harness the power of institutional order flow and trade more like the biggest and most successful hedge fund managers in the world.

HOW CAN ALPHASHARK TRADING HELP ME?

Since founding AlphaShark Trading in February 2012, I've been overwhelmed by the positive feedback and response I've received. Business is booming, which is great, because I love

helping traders improve their P&L through setting up better risk-versus-reward trades. Every day in the office, the other traders and I discuss strategies, options set-ups, and reasons why we did or didn't take certain trades. AlphaShark trading began as a blog, but I realized I wasn't just content with sharing my market commentary. After all the monetary success options brought me, I wanted to help others stop losing money at the very least.

To learn more about trading unusual options activity and how you can get unusual options activity alerts live and in real time, please check out our Gold Package here for a HUGE discount!

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ABOUT THE AUTHOR

James Ramelli is a trader and options educator at AlphaShark Trading, where he actively trades futures, equity options, currency pairs and commodities. As one of the moderators of the Live Trading Room, Ramelli educates members on strategies, trade setups, and risk management while trading his own capital.

Ramelli regularly appears on Bloomberg TV, BNN, and CBOE TV, in addition to writing a weekly column for Futures magazine and being featured in CME Group's OpenMarkets as a guest contributor.

Ramelli holds a B.S. in Finance with a concentration in Derivatives and Financial Engineering from the University of Illinois at Urbana-Champaign.

THE STRATEGY FOR A SCHEDULED OPTIONS PAYDAY EACH QUARTER

By Christopher Irvin, MarketTraders.com

Four times each year, stock and equity options traders' ears perk up.

Like clockwork, their gears start to turn and they type away at the keyboard, looking for the earnings season schedule of big-name companies like Google, Apple, Netflix, Tesla... The list goes on. It's like an appointment for profits.

Each earnings season, the stock market sees a spike in volatility, in profit potential, for traders with a weather eye on the horizon. As stock traders take to the charts, equity options traders do the same, looking to take advantage of stock movements for pennies on the dollar and get a little piece of the pie.

What if you could do the same?

What if each quarter, you set aside a handful of hours to execute a few options trades where you could potentially profit 25-30% overnight?

It happens, and more frequently than you might think. I've been trading for more than 15 years and I've not only seen it happen through my students' successes at Market Traders Institute, I've watched it happen in my own account too. The beauty of it is that no matter what time of year it is, you could be preparing for earnings season.

This is the precise strategy that I use each and every quarter...

What is the Earnings Season?

Earnings Season: The time around the beginning of each financial quarter when publicly-traded companies release earnings reports for the previous quarter.

The Catch

Despite what some traders will tell you, as an equity options trader, the actual earnings number is not the issue. I really don't even care if the company makes money or loses money. What counts is how investors react to the news.

What is the important part? ***The knee-jerk reaction of investors.***

Because investors assign a positive or negative emotion to those numbers, the stock can jump, or dump. These moves can make for great opportunity if you know how to play the move.

I focus on the reaction that the stock's price has to the earnings number.

That's what will drive the intrinsic value in my options, and therefore the profitability in the trade. The intrinsic value of an option is the component of the options price that is DIRECTLY affected by the movement of the underlying stock. If the stock goes up \$1.00, the intrinsic value goes up \$1.00. That is why we need the stock price to move big. **In order for a straddle to work, intrinsic value needs to take off.**

The other day, Netflix (NFLX) had its earnings announcement. The company made \$0.06 per share, but the bigger story to me was that the \$100.00 stock moved approximately \$17.00 the next day. That is the type of move that we are after. The total cost of the straddle in this situation was on \$12.80 per share. Since the underlying stock moved \$17.00, the intrinsic value boosted the trade to a profit. Like I said, I don't care about the \$0.06. I care about the \$17.00 and what that move will do for my options.

One of the great things about a straddle trade is that I really did not even care if the stock moved up \$17.00 or down \$17.00. I would profit either way. That is correct - I do not have to choose a direction. It's just one more way that this strategy takes the stress out of your trades.

THE 4-STEP EARNINGS SEASON PROFIT PLAN

The Straddle Trading Strategy

An options straddle blows some traders' minds. You don't pick the stock's direction. Truly, your only concern is that the stock moves. Period.

Not a bad strategy, right?

Volatility: The amount of market action. Also known as "the spread" in the market's waves or the price fluctuations a stock experiences.

Typically, if you're buying a call option, you're looking for the stock price to go up.

If you buy a put option, you are looking for the stock's price to move down.

In an options straddle, you buy a call and buy a put simultaneously.

When you place these orders, you just want the stock to react to the earnings announcement.

The bigger the reaction the better. Positive or negative does not matter, we just want it to move dramatically.

Options Straddle: When you buy a call option and buy a put option at the same time, you straddle the market price so that no matter which direction the stock moves, you could profit.

Why Trade In Both Directions?

So you might be thinking, if I'm trading in both directions, won't the trades cancel one another out? Or worse, won't that mean that the market will inevitably go against me?

Yes and no.

When the market moves big in one direction, one of your options, either the call or the put, will increase in value. The other decreases in value. You will be losing money in that negative trade, but the objective is to have the winning trade outweigh your losing side. This is where

you start to see profit. The profit of the winning trade should be much larger than the loss in the losing position. As a matter of fact, your loser may get crushed into oblivion. The good news is that when you buy options, your risk is limited to the cost of the option, and your reward is unlimited. So if your winner increases by more than the cost of the total loser, we have a winning straddle.

How it Works

The key is buying equal numbers of “at the money” calls and puts prior to the announcement. This is why having the announcement release date on your calendar is so critical. When you buy an equal number of at-the-money calls to puts, you are creating a “delta neutral” strategy. At-the-money call options will have deltas of .50, and At-the-money put options will have deltas of -.50. When these deltas are added together, we end up with a delta of “0”, or delta neutral.

Delta: Stemming from the Greek word diaphora which means “difference.” This number tells you how much you will profit based on a \$1.00 move of the stock; e.g., if a trader buys an option with a 0.75 delta, and the underlying stock moves \$1.00, the option will increase in value by \$0.75.

Delta Neutral: Puts always have a delta from -1 to 0 and calls from 0 to 1, so when you buy a put with a delta of -0.5 put and a call 0.5 delta, your deltas will cancel each other out and you will be left with a delta neutral position.

You are dealing with two deltas in this case.

Let's say that we get into a straddle trade where the call option has a delta of 0.50 and the Put option has a Delta of -0.50. The earnings are released and the stock gaps up in the pre-market. This causes the call options to increase in value and along the way the delta is ratcheting up. 0.50, to 0.55, to 0.60, to 0.65 eventually moving up to 0.85. This means that my call options is now making me \$0.85 every time the stock move up \$1.00. That is great! But what about the put positions? The put delta will start moving in the opposite direction;

-0.50, to -0.45, to, -0.40, eventually falling to -0.20. The put, being on the losing side of the trade, is actually losing money slower. In this case, at this level, the put option is losing \$0.20 for every \$1.00 the underlying stock price moves up. Here is the great thing about the current state of our hypothetical trade. We are making \$0.80, with our call option, for every \$1.00 move of the underlying stock, while we are losing \$0.20 for the same move with the put. The net result is a \$0.60 profit. That is why straddles work!

PRO TIP: The Ultimate Stock and Options Course teaches to buy options with deltas between 0.5 and -0.50 for straddle trades during earnings season. (The trade is not a straddle if you use options with deltas other than 0.50 and -0.50.)

When to Straddle the Market

It's simple really. The straddle strategy allows a trader to take advantage of a known event that has a high probability of causing the stock to move 10% to 15%, regardless of direction. This is why it's a perfect strategy to master when trading earnings announcements.

The Key to the Straddle

Understand this: a straddle is not an ideal strategy for every stock at earnings. The reason is that not every stock has the potential for the required move it will take to put the trade into a profitable position. For this reason, you will need to do your homework before placing a straddle.

Now, let's explain the top five ways to judge whether or not a particular trading opportunity is a good pick for an earnings season straddle trade.

5 STEPS TO SUCCESSFUL OPTIONS STRADDLES

Step 1: Stalk Your Prey

First and foremost, you'll need potential stock shares that you'll want to monitor.

All of the following steps require that you have particular companies in mind, access to their current share prices and, preferably, have an idea of when their earnings reports will be released for the coming quarter.

Step 2: Look to the Past to Profit in the Future

Now that you have several stocks in mind, you'll want to look back on the historical data for the stocks in question, be it Apple, Google, Netflix, Tesla, whichever stock you're looking to profit from.

To do this, you want to look back on the stock charts and identify the four most recent earnings report releases dates. Once you have found them, check out the price fluctuations in that company's stock price following each announcement.

You'll want to answer three questions:

1. What was the closing price prior to the announcement's release?
2. What was the opening price the day after the announcement's release?
3. What was the peak or valley before turn price - after the announcement's release?

Peak or Valley Before Turn Price: The price the stock hits, before its first reversal, after the report's release.

The measurements from close to open, and close to peak/valley can give you an indication as to whether the stock has moved substantially in the past at earnings announcements. If the cost of the straddle is less than the historical movement at earnings releases, you may have a potential straddle candidate.

Example:

Let's take a look at an older example of this for the sake of clarity.

Below are four consecutive earnings report numbers for Netflix (remember that you'll always want to pull the four MOST RECENT earnings numbers for judging your potential straddle trade):

Earnings Report from 1/20/15

Pre Earnings Close - \$349.40

Post Earnings Open - \$414.68 (**\$65.28 move or 18%**)

Post Earnings Peak - \$457.38 (**\$108.28 move or 30%**)

Earnings Report from 10/15/14

Pre Earnings Close - \$448.59

Post Earnings Open - \$332.73 (**\$115.86 move or 25%**)

Post Earnings Low - \$331.00 (**\$117.59 move or 26.2%**) immediate bounce

Earnings Report from 7/21/14

Pre Earnings Close - \$452.00

Post Earnings Open - \$442.98 (**\$9.02 move or 1.9%**)

Post Earnings Low - \$412.51 (**\$39.48 move or 8.7%**)

Earnings Report from 4/21/14

Pre Earnings Close - \$348.49

Post Earnings Open - \$376.63 (**\$28.14 move or 8%**)

Post Earnings Peak - \$380.88 (**\$32.39 move or 9.2%**) immediate drop

In these examples, you can see that the two most recent earnings releases caused the stock's price to move between 18% and 30%. If we were looking at a straddle that hypothetically cost 15% of the current cost of the stock's price, the trade would have potential.

What's the Magic Number?

Unfortunately, there is no magic number and there's no holy grail. In the past, I have looked

for stock price fluctuations between 12-15% minimum. That often creates enough movement to produce a profitable trade in a straddle situation. The only way to truly make a sound judgement is to determine the current price of the straddle and compare that price against the average price movement over the past four earnings releases. If the cost of the straddle is greater than the average move, the trade probably will not work. If the average move is greater than the cost of the straddle, the trade has a good chance of working.

Step 3: Let the Big Dogs Weigh In

Now, this is a dangerous one if you're not careful. While we want to consider what key analysts are projecting, we don't want to trade the news, we want to trade the moves. At the same time, once you have your stock picked out in Step 1, it's good to check in on the analysts' insights.

You want to focus in on the highest analyst price target. When the cost of the straddle is added to the current value of the stock, you arrive at a number that is less than the analyst target, indicating that your straddle has the potential of working out.

PRO TIP: Don't pay attention to the earnings estimates. Instead, look to see where the analysts have set their highest price targets for the stock. This is what they think that the stock is worth. Traders like to drive prices up to the analyst targets and stop, so if the straddle profit target is lower than the analyst price target, the straddle should be in good shape.

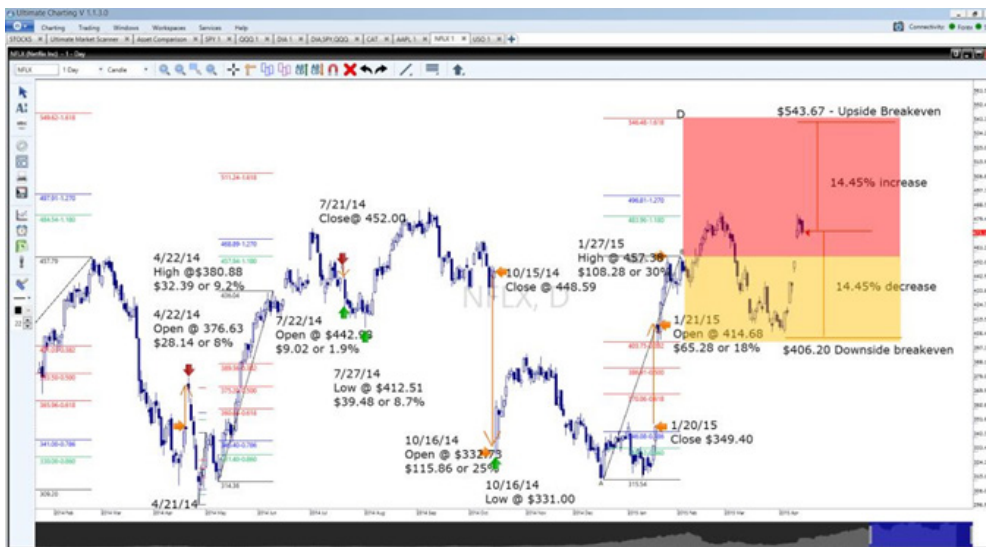
Step 4: Don't Forget the Fibs

The Fibonacci sequence is an old mathematical golden ratio you probably learned in some middle school or high school math class and quickly forgot about it, dismissing it as something you couldn't possibly, ever in a trillion years use... That is, until you began to trade the markets.

The next step (the decision-making process) for your trade is to draw out the Fibonacci.

In this instance, you want another point of confirmation. You're looking to be able to say that the stock has the potential to make the range of movement you're after within the current extension or retracement. If it is not, then your technicals do not match up with what you require to be profitable in your trade. While this may not be a 100%, sure-fire way to decide whether or not to avoid the trade, it is a critical component many traders take into consideration in passing up a trade.

See what the Fibs look like on the charts:



Step 5: Give the Volatility Charts a Vote

Have you ever seen a volatility chart? These charts help options traders determine whether an option is overpriced or underpriced. This is a wonderful gauge for seeing if the options are priced at a level that is just too expensive to place the straddle.

The chart is very visual, and simple to read. The chart will have two lines. One shows the historic volatility and the other represents the implied volatility. If the implied volatility line is higher than the historic volatility line, the options are thought to be expensive. If, on the other hand, historic volatility is higher than implied volatility, the options are thought to be inexpensive. What we really want to see is just how expensive our options are. What

you're looking for is the skew between the historic and implied volatility. The closer these two numbers are together, the smaller the skew. The smaller the skew, the less expensive the options and the better your chances will be of covering the cost of the straddle. The wider the skew, the more expensive the trade becomes and your chances of covering the straddle cost goes down.

Skew: A fancy math term for the difference or distance between two numbers.

Historic Volatility: Gauge of how much the stock's price has flopped around and moved based upon past data.

Implied Volatility: Representation of the average analyst sentiment as to what they believed the volatility will be in the future. (This directly ties into Step 2!)

CONCLUSION

Earnings season trading is as close to appointment-style trading as you can get. With just one strategy, the options straddle strategy, you could have a payday scheduled for every quarter.

Do you want to get more hands on experience with this strategy?

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Check out one of our live webinars. Your ticket is on me, just RSVP here -

www.TradingPub.com/LRHP2



ABOUT THE AUTHOR

Chris Irvin is a real trader. Over the past 15 years, he's traded stocks, options, futures and currencies. For him, trading is more than being your own boss; after all, he's been an entrepreneur since 1996. He knows that trading is a way to take control of your life. For him, being able to rely on himself is true freedom. Recognized for his trading skills in 2011 by Trade King and being an expert contributor in publications such as Invezz, Chris has put his trading knowledge to use in developing training materials and teaching traders across the globe since 2004. Now, after joining MTI in 2012, Chris continues to actively trade and teach others how to do the same without going through the school of hard knocks like he did.

HOW WITH PRICE ACTION YOU CAN CREATE A HIGHLY PROFITABLE TRADING EDGE OVER THE MARKET IN 5 SIMPLE STEPS

By Johnathon Fox, ForexSchoolOnline.com



Having an edge over the market is crucial to every trader's long-term success. Without an edge, all traders will be found out by the market eventually. Everyone can get lucky and go on winning streaks and on extended winning streaks. This often tricks people into thinking they are profitable or a good trader when, in fact, they are just lucky.

If the traders do not have an edge over the market, eventually they will start to lose and give back all the profits they have made during their winning streak. Because they don't actually have an edge, overall the edge is with the market and eventually that edge will play out in favor of the market, ensuring that traders lose.

It is just a matter of enough trades being traded. So, whilst every trader can get lucky, if they don't have an edge and the edge is on the side of the market, it is simply just a matter how many trades it takes before the edge plays out and the trader becomes a loser.

In this lesson, I am going to teach you just how crucial a profitable edge over the market really is. BUT, way more important than that, I'll teach you the five most important steps you need to start following right now to start creating your own edge over the market.

So that you can fast track your trading success, I have created a trading checklist for you listing the exact seven factors I check-off when hunting for and high probability trade setups.

These are the seven trading rules that I live by. You can use them to make your own trading checklist. You can get this seven-step trading checklist by clicking on the link I have supplied to you at the end of this chapter.

SO, WHAT EXACTLY IS AN EDGE OVER THE MARKET?

The best example of an edge at play is with casinos. The reason casinos make regular and consistent profits, even though they are gambling and playing games of chance is because they have an edge over the people who are playing the games. In other words, all the games, such as blackjack and the poker machines, etc., in the casino have the odds stacked in favor of the casino.

What is super important for you to note about this example is this; the casinos know they are going to lose and know they will go on large losing streaks. For example, someone may come to a blackjack table and get on a big roll and make a lot of money and the casinos know and understand that.

What the casinos also understand is that while they may lose here and there, they OVERALL, after many, many, many hands of blackjack, ALWAYS win. The casinos know that people are going to come in and win the jackpots on the poker machines, but OVERALL, the casinos will ALWAYS win.

This is the casinos edge and this is the exact same way you need to start thinking about your trading. A huge mistake many traders make is that they are short-term thinkers and they are

only thinking about their next trade, rather than thinking about trading within an overall edge.

You need to be trading a Forex business, and with an edge over the market. These next five steps are going to show you how exactly you use an edge with price action to become more successful.

1. FOCUS ON THE PRICE ACTION STORY

As a price action trader, your primary focus needs to be reading the price action. This would seem like a super obvious statement to make, right? Do a quick Google search or a search of any of the major forums and you will quickly find that a lot of the traders that think they are price action trading are; in fact, “pattern trading.”

Pattern trading is simply looking at the last one or two candles of the chart, and then making a trade based on this last candle. While the last one or two candles can be super important and we can use them as really great entry signals, they are only one or two candles on a price action chart that is full of many candles.

If you are to become a successful price action trader, you need to learn how to read the whole price action chart and learn how to put the whole price action story together. This is done by reading the live order flow, major support and resistance, and trends and trader behavior through the live price action.

2. PERFECT ONE PRICE ACTION TRIGGER AT A TIME

To make a really high probability A+ price action trade, we must first find a really solid price action story and a great area on the chart to enter from. As a price action trader, you would be asking: is there a strong trend? Also, is price rejecting support or resistance? Is there space for price to move into? Is this is a good area to make a trade from?

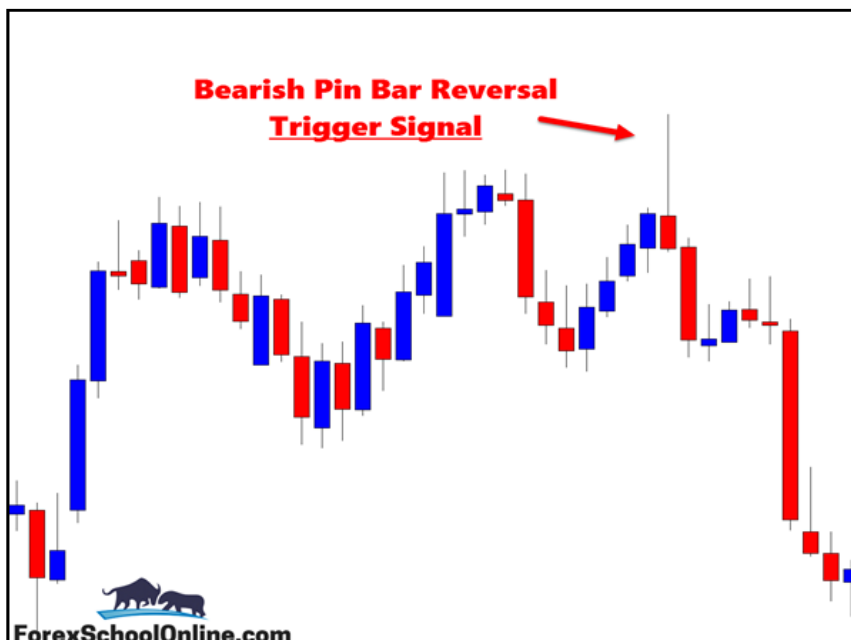
Once we find a really solid area to make a trade, we can then look for a price action trigger to make an entry. Price action trigger signals are candles, such as the pin bar reversal and the engulfing bar.

A mistake that a lot of traders make that slows down, rather than speeds up, their learning is that they try to learn and perfect all the price action triggers at once, rather than picking one that really suits them personally and that they like, and then making that trigger signal their own and perfecting it.

When a trader takes this route and decide to perfect just one trigger, instead of becoming okay at all setups, he or she can become a master of one at a time. If you perfect just one trigger at a time, you will be spending all your time with just that one trigger, learning everything about just that one trigger until your master it. There will be nothing else to take your concentration away.

Once you are happy that you have mastered it, you can then move on and repeat the process with the next trigger signal.

See the chart below for the pin bar reversal trigger signal.



3. BE A SNIPER BEHIND THE BUSHES, AND NOT A MACHINE GUNNER WIDE OUT IN THE OPEN WITH A SHOTGUN!

I was in the Australian Army before I moved to trading full-time, so the two things I know best are discipline and how to effectively blow things up. I often use my experiences in these two areas to use examples or explain trading situations and scenarios.

A great example of this is the biggest trap traders fall into: overtrading. This is without doubt the biggest trading account killer.

As a Forex trader, you want to be a sniper who hides in the bushes, well camouflaged, and when your trade comes up, you take just one single shot and make your profits. One shot and one kill. Precise trading. You sneak up to the great areas on the chart and then BAM! You pull the trigger on the trade.

YOU DO NOT want to be the machine gunner who stands out in the open or is standing on the back of a vehicle, spraying bullets everywhere. The machine gunner is rapid fire, laying down a lot of rounds and drawing a heck of a lot of heat, but hardly any of their rounds are actually hitting the target.



In the Forex market, more does not equal more. This is something that can often take a lot of traders a long time to come to grips with, but the sooner, the better because overtrading is the number one account killer without a doubt.

More trading does not always equal more profits. The mindset needed from trading is very different from the day-to-day mindset needed in everyday life. A common example of this in the markets is a trader who makes a trade when they probably shouldn't, just because they are wanting to make more trades. They lose this trade because it was a very average trade. Another trade then forms that is a very good trade. The trader also plays this trade and makes a profit.

The problem is that the trader is now only back to break even because while they have played two trades, the first average trade that they should not have played cost them money. Whereas, another trader who would have only traded just the one trade would now be in profits, but the first trader is sitting with zero profits at break even. This is a clear example of how more does not always equal more.

4. WORK DOWN THE TIME FRAMES - NOT THE OTHER WAY

This is super important, and so often done the opposite way. Often, traders come to trading and will go straight to the smallest time frame they can find, such as the five minutes or one minute charts. The massive problem with this is that price on the smaller time frame is moving quicker, is more erratic, has more false moves, and has a lot more support and resistance areas to deal with.

The higher the time frame, the easier reading price action becomes, and the more time you have to make decisions, the less choppy price is going to be. A major reason that a lot of traders are on the smaller time frames is because they think that the smaller the time frame, the more trading opportunities and whilst this is true to a degree, it is no good playing a heap of trades if you are losing money. Why look for more and more trades to lose more and more money?

Instead of working from the smallest time frame, you need to move to the daily chart and earn the right to be trading on the smaller time frame charts by being profitable. The daily

charts are by far the best time frame for you to not only learn on, but also, continue trading on for your lifestyle.

Daily charts can offer profits without needing to stare at charts all day whilst still having a lifestyle. They are also the best price action charts for you to have success on. Daily charts have the clearest support and resistance levels with the most defined trends.

The other major note of importance is that you can build discipline on daily charts that is going to hold you in great stead on all the other smaller time frames. The daily charts only close once per day, and so you have to learn the patience and discipline not to over-manage or fiddle with your trades. These are great skills to learn early on in your trading career.

Once you are profitable on the daily chart, you can move to the four hour charts and learn to become profitable on them. Once profitable on the four hour charts, you can then move to the next smaller time frame and become profitable and continue repeating the process as far down the time frames as you like.

A lot of traders never leave the daily charts simply because they love the stability of the profits that the daily charts give them and they love the lifestyle factors of being able to only look at charts for an hour or so per day, and then do other things with their lives.

5. HAVE A PRE-TRADE PLAN

This is HUGE! And, that is why I have left it until last, but definitely not least. Managing your trades and setting targets is where you are going to make your profits. This is the part of your trade that can literally decide whether the exact same trade is a winner or a loser.

A lot of traders have a very “fly by the seat of their pants” approach to managing their trades and they just wing it each trade. If you want consistent results from your trading business and you want to make consistent profits, then you need to manage your trades consistently and have the same rules with the same plan.

So, how is this done? With a pre-trade plan. A pre-trade plan is something that you write out before you enter your trade. It states exactly how you intend to manage your trade. The best time to make trade management decisions is before you enter a trade and before any real money is on the line.

The pre-trade plan should include things like your profits targets. If you have multiple profit targets, then include them all. Do you plan to move to break even? If so, include the price point you plan to move to break even. Where is your stop? Do you plan to use a trailing stop at any point? If so, how and what sort of trailing stop?

Are you starting to get the idea? Basically, you should be writing down this pre-trade plan, so that someone else who does not know your trading strategy could come along and read your pre-trade plan and manage your trade effectively just by reading your plan.

Making this pre-trade plan is going to stop a host of human errors. As humans, we don't make great traders, and by making and following this plan, we can prevent a lot of these errors from ever occurring.

RECAP ~ YOUR TRADING MACHINE

The key to your long-term success is with you being able to build a profitable edge over the market. With a profitable edge, it ensures that whilst you will have losses and losing streaks, after all is said and done; overall, the edge will come out on top and you will make a profit.

When you have this, you have a trading business and a trading machine, and it is just a matter then of finding as many trades as possible that meet your trading edge; thus, turning the machine over to churn out the profits.

Safe trading and all the success,

Johnathon Fox

THE SPECIAL OFFER

7-Step High Probability Trading Checklist

Learn the simple seven steps that will help you make high-probability and low-risk price action trades in many markets and time frames time and time again. Visit the following page to get your free 7 step checklist - www.TradingPub.com/LRHP3

THE MOVIES

Visit the page listed below to watch a video lesson on how you can trade the high-probability false break Pin Bar Reversal trigger signal trade setup - www.TradingPub.com/LRHP4

Learn how you can manage your trades using the price action story. Visit this page - www.TradingPub.com/LRHP5 to watch a video on how to use the Pin Bar Reversal to manage your trade setups.



ABOUT THE AUTHOR

Johnathon Fox is a professional Forex and futures trader who also acts as a mentor and coach to thousands of aspiring traders from countries around the world. Johnathon specializes in helping traders reach their full trading potential by helping them master the art of price action trading and correct money management techniques.

You can learn the exact same seven-step plan that Johnathon goes through every time he looks for a trade. To get your seven-step trade checklist to help spot high-probability trade setups in the markets, go his special offer above and download the FREE seven-step process checklist.

LOW-RISK/HIGH-PROBABILITY OPTIONS TRADING STRATEGIES

By Michael McNelis, DelphianTrading.com

As an options strategist at **Delphian**, I am always testing models for different strategies. Low-risk / high-probability trades are a favorite for many investors.

The **Delphian** platform empowers traders with institutional grade trade analytics, giving you the ability to test your trading strategies with historical options data. By backtesting your trading strategies, we can answer the question:

What if I had applied investment strategy X during period Y?

So what is low-risk / high-probability trading? As traders, we all have a different tolerance for risk. In general, low risk means we are not willing to risk more than a certain percent of our trading capital in any one trade. That percentage will be based on your risk tolerance. High probability trades are trades that have been proven statistically and have generated more wins, with an average win rate that is greater than average loss rate. With **Delphian**, the edge comes from applying money management with our proprietary State Modeling™.



Typically, low-risk trades equate to lower returns (such as bonds), while higher risk trades offer higher returns and, in turn, higher risk. Options give us the flexibility to be conservative or ultra-aggressive because we choose which option delta we purchase or sell.

Delta is one of the option Greeks you need to understand when options trading. An option delta calculates the change in the options price compared to the price change of the underlying stock. For example, if I were

buying an option with a .70 delta, for every \$1 move in the underlying stock, my option would move by \$.70.

If we are buying options, we can take a conservative approach and buy deep-in-the-money options with deltas greater than .70. Or perhaps we want to swing for the fences and buy options with a delta of .20. This gives us only a 20% chance of being correct...but when we are, it should be a home run.

When looking for low-risk / high-probability trading strategies, options give us a multitude of different investment possibilities. We can be a buyer of options, a seller of options or both a buyer and seller at the same time. Based on our view of the market at any given time, we can structure a trade to give us an edge. We can choose simple strategies, like buying long calls, or more complex strategies with multiple legs, like an Iron Condor. Each strategy has its time and place.

When volatility (the degree of variation of a trading price series over time, as measured by the standard deviation of returns) is low, it's preferable to be a buyer of options. Conversely, it's better to be a seller of options when volatility is high.

In stock trading, time is not as important a factor as in option buying. Theoretically, you can hold on to a stock forever. As an options buyer (in other words, someone who is long option), time decay is the number one enemy for our options trades.

With the Delphian program, we can historically look at similar markets and test which options trades create the lowest risk based on your tolerance for risk versus reward.

WHAT'S THE REAL DEAL?

Let's pretend that I said, "My system had a win percentage of 90%." Initially, you might be impressed, right? But to really analyze the results, we'd need to delve a little deeper.

That 90% win percentage might mean that I make \$10 for every win...but what if it doesn't account for the \$100 lost for every loss? In that case, I'd have a system that loses \$100 for every \$90 it wins.

No thank you!

Conversely, it might not sound as impressive for me to say I have a system that only has a 30% win percentage...but it could be highly profitable with a low drawdown.



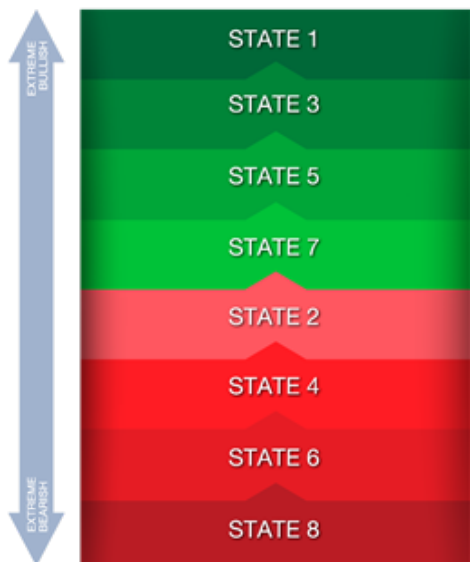
THE PROFIT FACTOR

When judging a strategy, I like to look at the profit factor, which is simply how many dollars I made, divided by the dollars I lost.

For example, if I had a system that gained \$1,000 and lost \$500, it would have a profit factor of 2. A profit factor of less than 1 is obviously undesirable as it loses money.



Proprietary State Modeling™



So now that we know what to look for, how do we find some low-risk / high-probability trades?

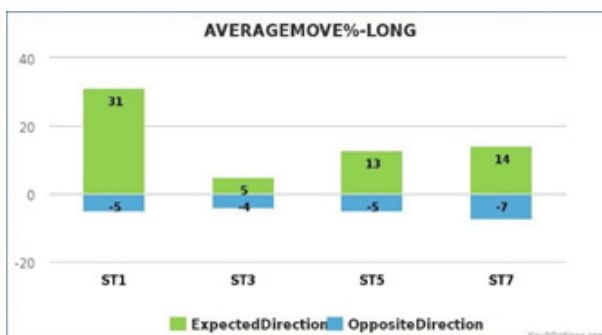
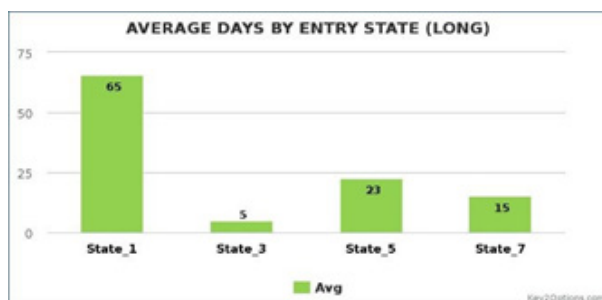
At Delphian, we use our proprietary State Modeling™ to help minimize risk and enter trades when probabilities are in our favor.

Each stock and index is categorized into one of eight states. States 1, 3, 5 and 7 are bullish. States 2, 4, 6, and 8 are bearish. States 1 and 8 are at the extremes.

Proprietary State Modeling™ gives you a detailed analysis of what state your stock is in, with information on Daily State Distribution, Average Days by State and the Average Move per State.

the Average Move per State.

The charts below are screen shots from the Delphian program that display information about Netflix (NFLX).



We can see that Netflix averaged 65 days in State 1, our most extremely bullish state. In a State 1 condition, it gained an average of 31%.

Using this data, we can then design and implement a trading strategy to take advantage of the time and price movement. This type of detailed analysis is necessary to lower risk and achieve maximum profitability.

BUY/SELL INDICATORS

Delphian is equipped with 20 different buy/sell indicators that can be used for modeling. You create your own buy/sell signals and give your model trade and money management parameters. You can even test different deltas to determine whether you should be buying in-the-money or out-of-the-money options.



As a general rule of thumb when buying options, the higher the delta the less risky your option trade is because it is already in the money and has a higher probability of ending profitable.

In the chart below, I have run a test on the S&P 500 index (SPX) from January 2007 to December 2014 to see how our proprietary trade filter can reduce risk and increase our probability of success.

TABLE-1

RUN	Trade Rule	Profit	Profit Factor	Win%	Num Win	Num Loss	Rejected
Run1	☰	\$26,106.00	1.34	43%	13	17	0

Running a test with a popular entry/exit system, a 10/30-day exponential moving average, we see that the system executed 30 trades with a win percentage of 43% and had a \$26,106.00 profit with a 1.34 profit factor.

In this case, I used a 100% profit target. When my trade made 100%, I closed out the position. I also used a stop loss at 50%, closing out any position when my trade reached a loss of 50%. I chose a delta of 52, which means the system will look for the nearest delta to 52 when looking for a trade.

Now, after adding our proprietary State 1 filter to the exact trade plan and running the same test, let's take a look at the results:

TABLE								
	RUN	Trade Rule	Profit	Profit Factor	Win%	Num Win	Num Loss	Rejected
<input type="checkbox"/>	Run2	☰	\$59,625.00	2.41	57%	12	9	9
<input type="checkbox"/>	Run1	☰	\$26,106.00	1.34	43%	13	17	0

The **Delphian** State 1 filter displays trades only when the SPX is in its most bullish state.

As a result, this reduced the amount of trades from 30 to 21 while increasing the win percentage by nearly 15%, the profit by over \$30K, and the profit factor from 1.34 to 2.41.

When proprietary State Modeling™ was used as a filter, some losing trades were rejected. It's also important to look at the consistency of trades. No one trade makes the majority of the profits.

TRADE	VIEW	SYMBOL	PROFIT	PROFIT(%)	RISK OPEN	RISK TRAN	ENTRY DATE	EXIT DATE	DAYS IN TRADE	DAYS TO ADJUST	MAX RUN UP	MAX DRAW DOWN	VOL %	PRICE %	PRICE DIFF	REASON
T1	View	SPX	(\$4,920.00)	-55.41	\$8,880.00	\$8,880.00	6/21/2007	6/26/2007	4	0	\$0.00	(\$4,920.00)	0	-0.02	(\$29.30)	SL_Cost_Close_Ar
T2	View	SPX	(\$4,980.00)	-56.08	\$8,880.00	\$8,880.00	9/19/2007	10/16/2007	20	0	\$2,460.00	(\$4,980.00)	0	0.01	\$9.50	SL_Cost_Close_Ar
T9	View	SPX	\$9,780.00	145.97	\$6,700.00	\$6,700.00	8/11/2009	9/16/2009	26	0	\$9,780.00	(\$1,670.00)	0	0.07	\$74.41	PT_PosProfit_Clo
T10	View	SPX	(\$5,265.00)	-55.1	\$9,555.00	\$9,555.00	11/13/2009	12/17/2009	24	0	\$2,580.00	(\$5,265.00)	0	0	\$2.60	SL_Cost_Close_Ar
T11	View	SPX	\$10,125.00	103.32	\$9,800.00	\$9,800.00	2/26/2010	3/5/2010	6	0	\$10,125.00	\$0.00	0	0.03	\$34.21	PT_PosProfit_Clo
T13	View	SPX	(\$4,695.00)	-51.14	\$9,180.00	\$9,180.00	8/10/2010	8/12/2010	3	0	\$0.00	(\$4,695.00)	0	-0.03	(\$37.45)	SL_Cost_Close_Ar
T14	View	SPX	\$9,795.00	126.8	\$7,725.00	\$7,725.00	9/17/2010	10/13/2010	19	0	\$9,795.00	(\$210.00)	0	0.05	\$52.51	PT_PosProfit_Clo
T15	View	SPX	\$11,190.00	124.33	\$9,000.00	\$9,000.00	12/3/2010	1/12/2011	28	0	\$11,190.00	(\$555.00)	0	0.05	\$61.25	PT_PosProfit_Clo
T16	View	SPX	(\$4,935.00)	-50.69	\$9,735.00	\$9,735.00	4/1/2011	4/14/2011	10	0	\$0.00	(\$4,935.00)	0	-0.01	(\$17.89)	SL_Cost_Close_Ar
T17	View	SPX	(\$4,845.00)	-54.47	\$8,895.00	\$8,895.00	7/5/2011	7/18/2011	10	0	\$3,120.00	(\$4,845.00)	0	-0.02	(\$32.44)	SL_Cost_Close_Ar

TRADE	VIEW	SYMBOL	PROFIT	PROFIT(%)	RISK OPEN	RISK TRAN	ENTRY DATE	EXIT DATE	DAYS IN TRADE	DAYS TO ADJUST	MAX RUN UP	MAX DRAW DOWN	VOL %	PRICE %	PRICE DIFF	REASON
T20	View	SPX	\$7,350.00	101.66	\$7,230.00	\$7,230.00	1/5/2012	2/7/2012	23	0	\$7,350.00	(\$550.00)	0	0.05	\$65.99	PT_PosProfit_Clos
T21	View	SPX	(\$4,950.00)	-56.12	\$8,820.00	\$8,820.00	7/3/2012	7/10/2012	5	0	\$0.00	(\$4,950.00)	0	-0.02	(\$32.55)	SL_Cost_Close_Act
T22	View	SPX	\$9,660.00	107.51	\$8,985.00	\$8,985.00	12/6/2012	1/10/2013	24	0	\$9,660.00	(\$2,805.00)	0	0.04	\$58.18	PT_PosProfit_Clos
T23	View	SPX	\$9,135.00	101.5	\$9,000.00	\$9,000.00	7/10/2013	8/1/2013	17	0	\$9,135.00	\$0.00	0	0.03	\$54.25	PT_PosProfit_Clos
T24	View	SPX	(\$4,830.00)	-56.1	\$8,610.00	\$8,610.00	9/16/2013	10/3/2013	14	0	\$5,235.00	(\$4,830.00)	0	-0.01	(\$18.94)	SL_Cost_Close_Act
T25	View	SPX	\$9,390.00	124.7	\$7,530.00	\$7,530.00	10/17/2013	11/13/2013	20	0	\$9,390.00	\$0.00	0	0.03	\$48.85	PT_PosProfit_Clos
T26	View	SPX	\$4,710.00	55.48	\$8,490.00	\$8,490.00	2/20/2014	3/21/2014	22	0	\$7,080.00	(\$975.00)	0	0.01	\$26.74	Exit_Dte
T27	View	SPX	\$8,480.00	111.43	\$7,610.00	\$7,610.00	4/28/2014	6/5/2014	28	0	\$8,480.00	(\$1,660.00)	0	0.04	\$71.03	PT_PosProfit_Clos
T28	View	SPX	\$3,660.00	37.42	\$9,780.00	\$9,780.00	8/22/2014	9/19/2014	20	0	\$3,660.00	(\$4,120.00)	0	0.01	\$22.01	Exit_Dte
T29	View	SPX	\$8,625.00	102.68	\$8,400.00	\$8,400.00	10/30/2014	11/17/2014	13	0	\$8,625.00	\$0.00	0	0.02	\$46.67	PT_PosProfit_Clos

11 - 20 of 21 items

TRADE	VIEW	SYMBOL	PROFIT	PROFIT(%)	RISK OPEN	RISK TRAN	ENTRY DATE	EXIT DATE	DAYS IN TRADE	DAYS TO ADJUST	MAX RUN UP	MAX DRAW DOWN	VOL %	PRICE %	PRICE DIFF	REASON
T30	View	SPX	(\$2,855.00)	-19.73	\$14,470.00	\$14,470.00	12/30/2014	1/12/2015	9	0	\$0.00	(\$3,855.00)	0	-0.03	(\$52.08)	Exit_Dte

21 - 21 of 21 items

THE FLEXIBILITY AND LEVERAGE OF OPTIONS

Options are a great investment choice because of their flexibility and leverage. You can hedge a long position or use the leverage for pure speculation. In either case, we can actually reduce risk by purchasing options. Although there is risk in trading options (because let's face it, there is even risk in keeping your money at the bank), the risk can be minimized and controlled.



The key to low-risk / high-probability trading is knowing when to trade, and understanding and quantifying your risk.

Delphian gives you the ability to analyze historical data and make informed decisions about your trading. Because risk is a relative statement, it lets you determine what your risk tolerance is by creating models to suit your investment objective. When combined with our state modeling, you can find low-risk / high-probability trades.

At Delphian, we believe you should [Plan Your Trade and Trade Your Plan!](#)

THE SPECIAL OFFER



Learn more about Delphian.

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ABOUT THE AUTHOR



Michael McNelis is an options strategist with Delphian. He began his career working for J.W. Investment Bankers, then co-founded Hatshack, a mall-based retail chain that eventually grew to 49 stores before being acquired by the publicly traded company Genesco.

Michael has been trading financial markets for over 20 years and has managed portfolios including equities, options and futures contracts. He has extensive use of options for income through covered call writing, hedging, and for capital appreciation, and has traded S&P, oil, natural gas, gold and U.S. dollar futures contracts.

PREDICTING MARKETS USING VOLUME AND PRICE

By Nigel Hawkes, HawkeyeTraders.com

Here are some normal volume attributes that add confirmation as to what price is doing:

1. Volume is highest just before going into congestion; e.g., channel, pennant, flag, triangle, etc.
2. Volume is lowest as it moves deeper into congestion.
3. Volume increases with a VALID breakout out of congestion and then SUBSIDES from this high volume level somewhat as the trend begins.
4. Volume increases in major reversals.
5. Volume goes with the overall trend and dries up on the counter trend; i.e., volume should move with the trend.
6. In 1-2-3 or double or triple top or bottom formations, you should see lower volume going into the second bottom/top. After the second top/bottom, if it is a reversal, you should see volume pick up in the new, reversed direction. If it goes into congestion, then it should slow down.

The following are unusual volume attributes which show a DIRECTION of price because volume isn't behaving like it should be as per above:

If heavier volume occurs at the LOWER price level of the congestion's formation, in the LATTER STAGE of the formation, this means that important buying support is being given and that the price will go up when it eventually breaks out of congestion's upper resistance level. If heavier volume occurs at a HIGHER price level in the LATTER

STAGE of the congestion's formation, then this means that there are more sellers than buyers and that price will eventually decline from the lower support level of the congestion pattern. Therefore, be on alert for price to move in the OPPOSITE direction to where the volume is highest in the congestion pattern, e.g., triangle, channel or flag. This also applies to Wyckoff's springboard, where you would see heavy volume coming into the lower edges of a protracted accumulation period (or after a lengthy period of price decline) where demand (buyers) is taking control or where you see higher volume coming into the higher edge of protracted distribution period (or after a lengthy period of price advance) where supply (sellers) is taking control.

1. Further to this, you should see volume on the direction of the breakout – this is normal, so if you don't see volume coming into the direction of the breakout, then the price will likely go in the opposite direction because not enough buyers (or sellers if going short) were present on that higher edge of the congestion to keep driving the price up (or down in the case of a short from the lower edge). Therefore, low volume on a breakout is predictive in that you should be looking to enter in the opposite direction. Therefore, if volume is initially light on the breakout, then it won't continue in the direction of the breakout.
2. It is expected on breakout that volume should increase, and it is also normal that once the breakout occurs, the volume should subside as the trend begins to form. But if the volume stays high after the breakout and prices move too strongly, this predicts that the breakout will NOT be valid and that price will move back into the congestion at least for a little while longer. If price retraces on high volume and bounces off of the outside edge of the congestion, and volume picks up again, then this is a valid breakout.
3. If volume is as high on the counter trend as it had been on the trend, then this tells you that price is about to reverse into the opposite direction from which

it had been going; i.e., the usual situation should show high volume on the trend but low on the countertrend.

4. Usually a wide bar, or multiple violent price swings along with this high volume, tells you that the price is going to reverse soon.
5. Always be on the lookout for countertrend volume to be higher than the trend's volume.
6. Top volume blow-offs usually happen quickly whereas bottom volume blow-offs are imagined and may take SEVERAL tests of a bottom before signaling the end of the bear market. Which means you don't necessarily see enormous volume spikes all at one time at a bottom.

Volume spikes – upside spikes are always followed by heavy downward price pressure because the buyers dry up. Downside price reversals in stocks usually go into congestion, whereas overall market crashes result in action similar to an upside spike; i.e., a reversal. If you are already in a trade, then you should be looking to exit on these spikes/crescendos because this is where price is going to reverse against you.

Remember that the large volume spikes at tops should ACCOMPANY very little upward price movement AT THE END OF A MOVE. This is what foretells the end of the advance. If you get volume spikes with large or commensurate price movement, then price could keep going. So the key is price hitting a resistance line or a small range bar(s) on high volume. The small range bar shows that there is resistance (or support in the case of large volume after a decline).

Circumstances of volume crescendos:

PRICE TREND	PRICE TREND	SUBSEQUENT PRICE
Before volume crescendo	While Volume Crescendo Builds	Direction
Rising	Up, Accelerating	Down
Rising	Breaking Down	Down
Flat or Congested	Breakout to Upside	Up
Flat or Congested	Breakout to Downside	Down
Falling	Accelerating Downward	Up
Falling	Reversing Up	Up

Lower Volume

1. Be on the lookout for volume to begin decreasing or slowing as the price continues in the later stages of a trend. This signals a possible reversal, pause or at least an exit point. Most likely this is a pause, which indicates a further continuation of the existing trend after the congestion/retracement. This is in contrast to observing high volume at the latter stages of a trend, which would be more indicative of a future reversal since this would indicate that participants were liquidating their holding. A decrease in volume entering congestion/retracement simply means participants are still holding on for the next leg in the same direction so you would want to hold on to your position or enter/add at this point.

2. A true (permanent) top or bottom formation's reversal should show high volume AFTER/ ON the reversal AS WELL AS the trend PRECEDING the reversal. If it shows light volume after/on the reversal, then this means that the original trend will resume and the trend is not going to reverse; i.e., it is simply a pause. This then is how you tell if it is a temporary or permanent top/bottom or merely a pause in the trend, by looking at the nature of the volume both BEFORE and AFTER/DURING the top/bottom formation. In other words, what is volume doing at the latter stages of the trend AND what is volume doing AS the price reverses? This before and after analysis determines whether price will temporarily retrace/

congest and continue in the direction of the original trend or whether it will permanently reverse into the opposite direction.

3. If, during the latter stages of a trend, volume dries up as price continues to rise – be careful of this since a reversal usually takes place the same as in a volume crescendo except that in this case there may or may not be a spike before the volume dries up. If you see advancing prices and declining volume, then you should short or exit longs. Remember, if prices are rising, volume should be rising if in an uptrend, and then volume should temporarily decline during a decline or consolidation in price. Similarly, be careful of low volume as prices continue to decline in a bear market as you should be expecting an upward rebound once buyers finally step back in and all the sellers have disappeared. This paragraph describes volume activity BEFORE/DURING the reversal (permanent) or retracement/congestion (temporary). It describes what might happen in the future AFTER/ON the top/bottom. Therefore, this is an early warning BUT not definitive. To really know for sure, you have to watch volume AFTER/ON the top/bottom as described in 2 above.

4. Low volume price advances (or declines) really say that the buyers and sellers are at equilibrium, which can't last for long before one side will dominate again...and it is in the opposite direction than the direction the previous trend was moving but again, the key appears to be what happens AFTER/ON the top/bottom as described above since low-volume, drying-up action could just be a temporary pause rather than a permanent reversal.

5. What the above is saying is that if you see the opposite to the way volume should be strongly or at least STEADY AND CONSISTENTLY acting DURING a trend, then beware of either a reversal or a pause. The general theme is that if you see lower volume at tops/bottoms as market price advances, then be on the lookout for some kind of change, be it temporary (retracement/congestion) or permanent (reversal). This is so because you should only see low volume on little or no price movement. Remember it like this: low volume = low price movement. If low volume accompanies price movement, then this can't be sustained for long and a correction will occur.

6. However, light volume doesn't necessarily guarantee a price retracement or reversal if price is only channeling or moving slightly because this is what light volume means (in other words, light volume reversals should only occur when price is accelerating in some direction, not when price is already languishing). Further, the bias is that if volume is light, then price will likely turn down, because fear is a more important motivator than greed so people watching light volume are more inclined to sell than buy. Hence the axiom that the market will fall from its own weight, whereas to advance it needs heavy buying pressure.

7. So the key is that if volume is declining and price is retracing or going into congestion AFTER the pivot, then the price will likely continue on its previous trend path. If price is retracing under high volume AFTER the pivot, then a new trend in the opposite direction is underway and the reversal is permanent since only minor corrections should occur under light volume. If volume and price are both advancing (but not extremely volatile) BEFORE a pivot, then price will continue in the direction of the existing trend and will only temporarily retrace/congest. If volume is declining and price continues to advance BEFORE the pivot, then expect a reversal or retracement in the future that might be permanent rather than a mere correction...again, look to AFTER the pivot for volume characteristics to confirm the price direction. But, if volume is extremely high in the direction of the prevailing trend BEFORE/ON the pivot, then a permanent reversal will occur; i.e., climax. *This paragraph is essentially a summary of volume characteristics.*

8. Wyckoff: *This paragraph describes volume patterns BEFORE price reverses*, in other words WHILE price is STILL running in a trend: At the later stages of a bullish move, you can have either buyers (demand) drying up or more sellers (supply) appear as the move ends. You can tell who is in control by the fact that as price continues to rise but is losing momentum (rounding off), and ranges continue to narrow.

Increasing volume means that more sellers are appearing.

- a. Decreasing volume means that buyers are not any longer available. Low volume leading up to the top pivot indicates that demand is drying up.

Both conditions indicate the trend is going to reverse. The important difference in these warnings is that if there are more sellers (supply), then this is more indicative of a price decline than of demand drying up. It indicates that the decline will be greater once the rally is over since the bears are taking over. This scenario is in contrast to demand drying up where the supply side is not in control. It only means that the buyers are less interested in higher prices AT THIS TIME. The drying up of demand as evidenced by small volume as price advances to a top therefore might only be a pause in price since these owners are not selling and no new fresh sellers are shorting. If the owners were selling, or there was a perceived top by the bears who would be shorting, then the volume would be high. The higher probability short would then be to watch for tops forming on higher volume as opposed to volume merely petering out. Remember that this action to be looked at is as the rally is still continuing; i.e., the 'before' detailed in 2 and 7. It is not on the reaction that follows the top (known as the 'after') in which case it follows the general rules. For example, if the reversal has high volume, then the trend will be down as compared to light volume on the reversal which would indicate a mere correction with the original bullish trend continuing.

The same scenario in reverse occurs in a downtrend. Specifically diminishing volume when price is contracting while still in the downtrend indicates that sellers are scarce and, if volume is increasing while price is rounding/ slowing towards a bottom, then demand is in control as the shares are gobbled up as evidenced by the high volume. Therefore, high volume during, or at the end of, a downtrend would provide higher probability of a significant reversal to begin a new bullish trend. Light volume at bottoms shows that supply is drying up and taking the pressure off of selling which likely will lead to more selling.

9. Wyckoff: This paragraph describes volume patterns AFTER price reverses. Wyckoff states that AFTER a significant decline or selling climax, if you see price jump up on light volume, this proves that the sellers are gone and a bullish trend will begin. He says that if you see this rally to #2 on light volume, then you probably will get a reaction on light volume back down to point #3 which won't take out the selling climax low #1 point. It is after this that you get the high volume coming in as the accumulation begins.

Similarly, at a top, light volume on the first decline says that the buyers are gone and that sellers are not pressuring the market but that the trend will turn bearish. The next rally on light volume should not take out the buying climax high. Then you should see heavy volume come in from the sellers to indicate the bearish trend is on its way. If heavy volume comes in immediately on the first reaction, then there probably won't be a 1-2-3 or double-top style of correction so you would have to move much quicker than if you see a light volume correction – same for bottom. So light volume AFTER a crescendo or climax tells you that a pause (double top/bottom, 1-2-3, congestion etc.) is likely to occur whereas heavy volume AFTER a crescendo/climax tells you that the market is going to reverse into an opposite trend immediately.

10. This volume matrix shows a price direction prediction when looking at volume at LATER stages of the trend shortly BEFORE the pivot into a retracement – matrix from Watford:

VOLUME at later stages of trend BEFORE pivot			
		Higher	Lower
PRICE Direction BEFORE Pivot	Up	Bull Count	Pause or maybe reverse
	Down	Bear Count	Pause or maybe reverse

11. This volume matrix shows a price direction prediction when looking at volume AFTER the pivot i.e. price is already going into congestion/retracement. This is essentially the same as the Cassidy matrix below since it shows that price movement and volume movement must go hand in hand - matrix from Watford:

VOLUME AFTER Pivot			
PRICE retrace/congest direction AFTER pivot		Higher	Lower
	Up	Bullish	Bearish
	Down	Bullish	Bearish

12. This matrix predicts the price direction when looking at volume WHILE the trend is still moving but going into a correction/congestion. The general notion is that volume should confirm the trend; i.e., that price should be retracing/congesting if volume is low and that higher volume should confirm price movement– taken from Cassidy:

VOLUME			
PRICE		Higher	Lower
	Up	Bullish	Bearish
	Down	Bullish	Bearish

13. Another distinction of when you are likely to see low volume reversals are when either or both of these conditions exist:

- a. After a slow or irregular price advance (or decline if the trend is down) on low volume.
- b. After a period of dullness where prices are channeling in low volume.

The fact that both occur under light volume indicates that market participants are impatient so one of two things may occur:

- a. The impatience of buyers holding stock begets selling as evidenced by higher volume or,
- b. Both demand and supply dry up so the market falls under its own weight as evidenced by light volume. This scenario usually doesn't result in a deep decline but more of a channeling dullness with light volume up and down within the channel until there is a decisive turn resultant from news, etc. breaking the indecision.

14. IMPORTANT: To determine whether a correction (or going into CONGESTION WITHOUT A CORRECTION) is a retracement or a reversal, not only do you look to see that volume is light, indicating support of the prior trend, you also want price to confirm it by having price breakout from the pivot that gave rise to the correction (i.e., the breaking above/below of the #1 pivot if it is only a retracement). If it is a reversal, then price should break above/below the #2 pivot of a 1-2-3 or double top/bottom. Many times in the ES you see an advance under volume, and then price simply channels sideways AFTER THE ADVANCE without a downward correction. When this channeling occurs, if you see little or no volume for several 540-tick bars, then expect the trend to continue on its original path. If you see the channeling under heavy volume, you have to try to determine if is going to break up or down – usually it reverses from the original trend. Dullness after a rally in price under steady volume usually means a resumption of the trend.

Big Buying Volume – Distribution by the strong hands. Without price increasing further AFTER PRICES HAVE BEEN RISING means that this is a resistance level and that price is going to decline because there are more sellers absorbing all the buying volume which eventually dries up the buyers, thus moving prices down. This might not be a reversal point, since price often declines into a consolidation and then eventually breaks price to the downside after the buyers become frustrated and stop trying to increase price. The key here is that if you

see heavy volume but price isn't increasing at the same rate, then beware that distribution is occurring and prices will decline. The big price increase (upthrust or spring – end of a top) on high volume is the other precursor.

Big Selling Volume – Accumulation by the strong hands. Without price decreasing further AFTER PRICES HAVE BEEN DECLINING means that this is a support level and that price is going to increase because the buyers are absorbing all of the sellers' shares which eventually dry up the sellers giving way to a price advance. Again, this is usually a consolidation phase which should lead eventually to an upside breakout when the sellers are frustrated, exhausted or simply not enough of them available. The key here is that if you see heavy volume but price isn't declining at the same rate, then beware that accumulation is occurring and prices will eventually rise. The big price decline (shakeout or selling climax – end of a decline) on high volume is the other precursor.

Other Price Patterns with Volume

1. Watch for greater than two times the standard deviation of volume on a narrow range bar where the close is less than the open after a large run-up, since this portends a reversal to the downside. Similarly, after a bear market and you have the close greater than the open, with large volume and a narrow range bar, this is a reversal to the upside.
2. Watch for BOTH light volume AND a very narrow range as this is a prelude to an explosion out of the small range bar in one direction or the other.
3. Hawkeye thinks that prices move too fast and have to wait until volume catches up hence congestion after moves until x amount of volume has been filled. then price moves up again.

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ABOUT THE AUTHOR

Nigel Hawkes is the founder of Hawkeye Traders and has been trading since 1986. His only tools are graph paper, pencil and a calculator. Nigel is now president of one of the most powerful volume trading software systems available today - Hawkeye Traders.

Nigel conducted rigorous studies in volume spread analysis and price action, testing his own theories and methods. He then developed his own indicators using the open high / low close, which he found gave an edge over conventional volume spread analysis as it takes no account of the open. This resulted in his trading becoming profitable and consistent. After a long journey with several programmers and thousands of hours, the software was completed and made available worldwide.

THE ULTIMATE BARGAIN HUNTER

By Charles Mizrahi, InsiderWealthAlert.net

In 1934, co-authors Benjamin Graham and David Dodd wrote Security Analysis.

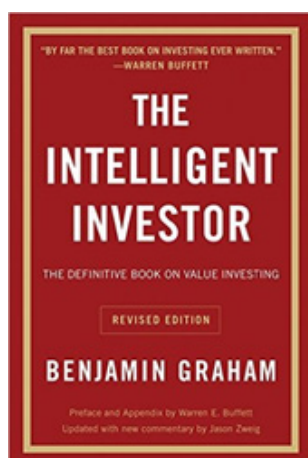


This 700-page book laid out the structure for a logical approach toward investing. It took investing out of the dark ages of astrology, hunches and tips. The authors said that successful investing is based not on chance or guesswork but on analysis of a company's past record. It provided structure and logic and created an intellectual framework for sound investing.

A few years later, in 1949, Graham wrote *The Intelligent Investor*, which, unlike *Security Analysis*, was geared to the layperson. The book found its way into the hands of a teenager in Omaha, Nebraska. Reading the book, he said, changed his life. That teenager was **Warren Buffett**.

Buffett read the first edition of *The Intelligent Investor* early in 1950, when he was 19 years old, and he has said, "I thought it was the best book about investing ever written. I still think it is." In a recent interview when asked how his investing approach has changed since he started investing, Buffett said, "My approach to investing I learned in 1949 or 1950 from a book by Ben Graham, and it's never changed."





Over the past 80 years, Graham’s principles have continued to endure, and they are even sounder and better understood with each passing year. Graham’s approach toward stock investing comprises three principles:

1. View stocks for what they really are – pieces of a business and not wiggles on a chart.
2. View the stock market as your partner, which he called Mr. Market, in which each trading day he offers to buy or sell your shares. Keep in mind that he is there to serve you, not to guide you.
3. Buy only when there is a gap between the price of the stock and the underlying worth of the business – or, as Graham called it, “a margin of safety.”

Graham, also known as the father of security analysis, approached the stock market not as a financial engineer using complex mathematical equations, but as a businessperson.

I have found over the years that if investors get the first principle, that stocks are pieces of a business, the other two principles flow from there. But if they have a hard time seeing stocks in that way, they probably will never get it and will end up buying and selling stocks based on everything but the fundamentals of the business.

PRIVATE INVESTOR

It never ceases to amaze me how successful businesspeople apply one approach to investing in a private business and another when it comes to stocks. Imagine the owner of a private business making decisions based on the following:

- Deciding to open a new division only when the 50-day moving average of his company’s daily sales crosses above the 200-day moving average of its daily bank deposits.

- Upon hearing of the nationalization of a bank in England, he calls a business broker and offers his 100-year-old very profitable family business for sale at 30% below its intrinsic value.
- After a government report is released that shows unemployment rose to 7%, he then calls a competitor and offers to buy that business for 25% above the company's asking price. The reason for his exuberance is that the unemployment number was 0.20% lower than his forecast.
- While charting his company's bank deposits, he notices that the chart pattern is tracing out an "inverse head and shoulders" pattern, and he makes a decision to lay off 20 employees.

If these decisions were actually made by a private businessperson, I question how long the person would stay in business. It would be hard to find a businessperson drawing conclusions on such disconnected data and actually implementing them. Yet most investors would not give it a second thought if I told you I was talking about stocks instead of a private business.

Most people who invest in stocks forget that they are actually pieces of a business. Instead they make decisions on buying and selling pieces of that business (shares) based on emotion and with very little regard for the underlying value of the business. In a nutshell, these types of investors are not in the proper mind frame that Graham laid out in his first principle.

Graham said the key to a sound investment is to "consider yourself as a part owner," which is a very sensible approach for sound investment. Ask yourself: "If there was no market for these shares, would I be willing to have an investment in this company?"

As a value investor, you know that over the short term stock prices fluctuate based on how popular a stock or industry is. Traders buy stocks simply because they are rising and sell them because they are falling. They even have a name for it, momentum traders. These traders don't perform any analysis on the company's financial statement, competitive advantage or stock price in relation to the value of the company.

The stock price fluctuations caused by this type of approach offer the value investor an enormous opportunity. When a stock or industry becomes unloved and unwanted, the stock price drops to levels that have no relationship to the underlying worth of the business.

What seems outright silly when it comes to making decisions in a private business, investors have no problem applying to stocks. Over the long term stock prices move in step with the intrinsic value of the business. It is during times when the stock price soars way above the intrinsic value of the business that we want to be sellers, and buyers when the stock price trades for a fraction of the business's worth. Warren Buffett said it best: "Be fearful when others are greedy and greedy when others are fearful."

Viewing stocks as pieces of businesses instead of as symbols that are traded thousands of times during the day gives a value investor a big advantage. Instead of making investment decisions based on the release of the Federal Reserve Bank of Philadelphia's Fed Index or the U.S. Census Bureau's Construction Spending report, value investors make investment decisions based on the company's financial statement and the difference between price and value.

Now, doesn't that make much more sense?

THE SECRET INGREDIENT

During the late 1970s, Warren Buffett was hardly a household name.

In 1979, the Berkshire Hathaway annual shareholder meeting was held in a fourth-floor lunchroom, the biggest space available at a Berkshire-owned Omaha business, and plenty big enough for the score of people expected.

A hand-lettered sign was taped to the double doors: "Meeting in progress." Alongside the vending machines and a coffeemaker, Warren Buffett called the meeting to order.

As chairman, Buffett went through the perfunctory official business in about five minutes, and then some of the people left. “I’ve got an hour, and if anybody wants to stick around and talk about the investment business, I’m available,” he told those remaining.

Only 20 shareholders showed up in 1979. It took close to 20 years before attendance topped 1,000.

Buffett and Berkshire have come a long way since then. **Attendance at the 2015 shareholder meeting was more than 40,000 and took place at the CenturyLink Center.**



After hearing Buffett speak in 1979 in the lunchroom of National Indemnity, one attendee invested \$12,000, his life savings, in Berkshire. What impressed him most was how Buffett explained things. “He was like a professor. He was able to make it real clear.”

One of Buffett’s great gifts is simplifying complexity. He is able to get to the heart of the matter rather quickly and make it very palpable for the average person to understand.

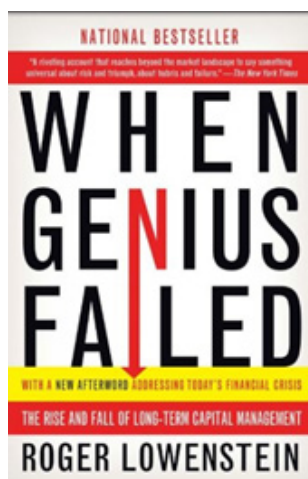
CLASSROOM VISIT

In 1977, Buffett was invited by his friend Professor Jack McDonald to speak to his class at Stanford Graduate School of Business. One of the students, Tim Bliss, jotted down notes on Buffett’s presentation. One of the points Buffett stressed was that there is “no correlation between hard work and intelligence, maybe [even an] inverse relationship.”

To make the point, Bliss even wrote down this equation: 80-hour week + 200 IQ = \$0. To most investors this would seem rather odd, since the popular perception is that hard work and high intelligence are the cornerstones to investing success. And it seemed kind of a crazy notion that working harder and being smarter would lead to poor results.

Throughout my investing career, I've come to the conclusion that Buffett is right.

I've met many successful investors who worked no more than 30 hours a week, and odds are they didn't graduate in the top half of their class.



In fact, Long Term Capital Management had a list of 16 partners that included two future Nobel Prize winners, and PhDs from MIT and Harvard. Yet in September 1998, the firm collapsed. The Federal Reserve Bank of New York organized a bailout of \$3.6 billion by the major creditors to avoid a wider collapse in the financial markets.

Buffett remarked:

“If you take the 16 of them, they have about as high an IQ as any 16 people working together in one business in the country, including Microsoft. An incredible amount of intellect in one room ... [They had] hundreds and hundreds of millions of their own money up [at risk], super-high intellect and [were] working in a field that they knew. Essentially they went broke.” (Source- Buffett Talk to MBA Students at Florida University 1998)

MORE THAN HARD WORK

If hard work and intellect will get you only so far, what makes for a successful investor? Temperament.

Buffett did say that there is a tremendous correlation between approach, temperament and success. Money can be made in the stock market if an investor possesses the following qualities:

1. **Is not tempted to invest every day.** Great investors pick their spots and don't invest every day the stock market is open. The key is to invest only when the odds of success are greatly in your favor.
2. **Has an even temperament.** Don't get overly excited when markets go your way, and don't be depressed when they go against you. Once you do your research and make a purchase based on your analysis, let the facts prove you right—not the daily gyrations of the stock market.
3. **Is disciplined.** Stick to an approach that is based on sound logic and has withstood the test of time. Ben Graham said that every investor “should be able to justify every purchase he makes and each price he pays by impersonal, objective reasoning that satisfies him that he is getting more than his money's worth for his purchase.”

ADVANTAGE: YOU

Most investors think they are at an extreme disadvantage when it comes to investing in stocks.

They would argue that the institutional and hedge fund manager has advantages in terms of resources, access to company insiders, and a whole team of analysts, dedicated to selecting stocks.

While that might appear that way on the surface, the individual investor is able to neutralize those advantages...and even has a leg up on the institutional investor.

Before you dismiss the idea that you have the edge, keep this in mind: Only a small fraction of mutual fund managers outperform the S&P 500 over a five-year period. If the institutions held all the cards, a larger percentage of them would outperform the benchmark on a more consistent basis. In fact, the opposite is true.

The approach we take offers us an edge that most mutual fund managers, hedge funds, and institutional investors do not have: a concentrated portfolio, no restrictions on holdings and the luxury of time.

CONCENTRATED PORTFOLIO

I always question how good a mutual fund manager's 85th best idea is. By law, fund managers must diversify their holdings, very often keeping less than 1 percent in any one stock. Instead of knowing much about a few companies, they try to know a little about many. A widely diversified portfolio (100+ holdings) proves to be a recipe for mediocre performance.

In contrast, our portfolio holds a concentrated portfolio of no more than 30 stocks. By sticking with our best ideas purchased at attractive prices, our portfolio has done very well over the long term. In fact, it has outperformed the S&P 500 by a wide margin.

But do keep in mind that over the short term and during rising markets, we run the risk of looking silly as our holdings are priced based on their popularity with investors and not their intrinsic value. We will accept looking silly over the short term and being right over the long term any day of the week.

NO RESTRICTIONS

Most mutual fund and institutional managers have built-in restrictions as to where they can invest. A mutual fund, for example, has a clearly defined mandate, which is, many times, based on industry (e.g., technology), market cap (e.g., small caps), or region (e.g., global companies).

If there are stocks trading outside these areas for 10 cents on the dollar, the mutual fund manager is prohibited from buying them. In contrast, we are limited only by our ability to find value. If we can't find value, we will wait patiently, and lower our buy trigger to valuations we believe offer us a margin of safety.

LUXURY OF TIME

Institutional investors are usually compensated on an annual basis. They do not have the luxury of buying and holding for the long term, and that is why they focus on a company's quarterly results. To qualify for their bonuses or incentive fees, they need to outperform their benchmarks over short-term time horizons. Their concern is not how the company will perform over the next five to ten years but how much the stock price will move over the next 90 days.

Our advantage is that we view short-term price fluctuations as meaningless and we make decisions based on the outlook of the business. We spend our time researching companies, trying to figure out how they will continue to increase their market dominance over the long term instead of trying to guess what their earnings will be over the next quarter. Our goal is always the same: buy great businesses when they are selling for attractive prices.

Warren Buffett said:

Time is the friend of a wonderful business. It's the enemy of the lousy business. If you're in a lousy business for a long time, you're going to get a lousy result. Even if you buy it cheap. If you're in a wonderful business for a long time, even if you pay a little too much going in, you're going to get a wonderful result. (Source- *ibid*)

To show you just how powerful the investing approach used by both Graham and Buffett can be, I'd like to introduce you to one company founded on these principles. This company looks remarkably similar to what Berkshire Hathaway looked like 40 years ago when they were making huge double-digit returns. The company has grown at a rate of 21.3% per year for the last three decades — and it's poised for more impressive gains in the months ahead.

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www.TradingPub.com/LRHP8



ABOUT THE AUTHOR

In his more than 30 years of recommending stocks, Charles has knocked the cover off the ball, and has compiled an amazing record of success.

He is the editor of *Hidden Values Alert* and the *Inevitable Wealth Portfolio* newsletters. Hidden Values Alert has been named one of Marketwatch.com's 10 Best Advisors from October 2007 to January 2015...a period that included the Financial Crisis of 2008 and the subsequent bull market that began March 2009.

While many gurus boast of astronomical rates of returns over very short time spans, their claims don't stand up to scrutiny. Instead, their "returns," when reviewed by an independent third party, melt away faster than ice cream on a hot summer day.

The returns that Charles has racked up are certified by Hulbert Financial Digest – the fiercely independent rating service that tracks the performance of financial newsletters.

Charles is also the author of the highly acclaimed book, *Getting Started in Value Investing* (Wiley).

TRADING CRUDE OIL AND NATURAL GAS NEWS WITH BINARY OPTIONS

Cam White, TradingPub.com

Trading into news always involves risk, but if you have a good strategy, it can also be very profitable. In this chapter strategies will be discussed for trading weekly inventory reports for Crude Oil and Natural Gas.

CRUDE OIL

Every Wednesday, Crude Oil inventory reports are released at 10:30 am EDT by the Energy Information Administration (EIA). The report measures the change in barrels of crude oil held by US companies. It's not uncommon for the actual inventory reports to greatly miss the forecast projections from the analysts. When that happens, there can be wild swings in the price of crude oil.

With binary options, you are making a decision about the likely direction of the market relative to a strike price within a defined time period. If the price of the asset you are trading agrees with your opinion at expiry, the trade settles for \$100 per contract. If it doesn't, the payout is \$0. You can always exit a position early if you want to take a partial profit, or to minimize losses if the trade is moving against you.

One strategy for trading crude oil inventory news is to place an OTM binary option trade on either side of the underlying indicative price before the release of the news. Here's an example of how this strategy was used on Wednesday, July 29, 2015:



Before the 10:30 am crude oil inventory reports were released, the market was traveling sideways, straddling the 47.62 strike price. The following strategy was used:

- The 9:00-11:00am time frame for Crude Oil was selected for this trade
- At 10:16am, two OTM trades were placed on either side of the underlying price of the market:
 - BUY Crude Oil at >48.42. Maximum risk \$19.50, maximum Reward \$80.50
 - SELL Crude Oil at >46.82 Maximum risk, \$20.75. Maximum reward \$79.25

For this trade to be successful, one trade needs to expire in the money, and the other trade takes a loss. The maximum risk on the losing trade is subtracted from the reward earned on the successful trade.

The worst case scenario in this strategy is if the market doesn't react to the news, and continues to trade sideways. In that event, you may wish to exit both trades to minimize losses, if possible.

At 10:30am the Crude Oil Inventory Report was released, badly missing estimates by over 4 million barrels. In an instant, the market shot straight up, making the BUY order good.

It continued to climb all the way to the 11:00 am expiration. The SELL order expired for a full loss. The net profit from this trade was \$59.75 (exchange fees not included).

NATURAL GAS

Every Thursday at 10:30 am EDT, The Energy Information Administration (EIA) releases the Natural Gas Storage Report, which measures the change in the number of cubic feet of natural gas held in underground storage during the past week. If the actual report misses estimates significantly, it can instantly result in large upward or downward moves in the price of Natural Gas Futures contracts.

The question then becomes “Which way will the market move on the news?” Will it spike up, dive down or trade sideways? You could decide to sit on the sidelines and wait for the market to digest the news when it is released. You could decide to place a trade in advance of the news. You could also choose not to trade Natural Gas on a news day.

Let’s assume you believe that the Natural Gas Storage Report will miss estimates, resulting in a possibly significant price move on the news. Since there is no way to know what the news will be, you could decide to hedge your trade in advance of the news with two out-of-the money (OTM) trades. When you place an OTM trade, you risk less money for a greater reward, since you are at a disadvantage relative to the current price of the market. Let’s take a look at an OTM trade on the Natural Gas Storage report released on Thursday, August 13 2015.

The Natural Gas market traveled sideways at around 2.91 going into the 10:30 am news release. At 10:21am, just prior to the release of the news, two OTM trades were placed on either side of the market, with an 11:00 am EDT expiry:

Trade Details (Executed at 10:21am EDT):

Contract: Natural Gas (Sep) >2.950 (11AM)
 Expiration: Thu Aug 13 11:00:00 EDT 2015
 Direction: BUY
 Quantity: 1 Contract Price: \$20.25
 Max. Risk: \$20.25 Max. Reward: \$79.75

Trade Details (Executed at 10:21am EDT):

Contract: Natural Gas (Sep) >2.870 (11AM)
 Expiration: Thu Aug 13 11:00:00 EDT 2015
 Direction: SELL
 Quantity: 1 Contract Price: \$84.00
 Max. Risk: \$16.00 Max. Reward: \$84.00

If the market moves significantly in one direction, one contract becomes more valuable, while the opposing contract becomes less valuable. If one contract expires in-the-money for a full profit, the other will expire out-of-the money for a loss. One trade acts as a hedge against the other trade. The worst case scenario is that the market doesn't react to the news and trades sideways. In that event, the maximum loss you can incur in this example is \$36.25 (exchange fees not included).

Here's how this OTM strategy played out.



When the 10:30am Natural Gas Storage Report was released, it missed estimates significantly. Within five minutes, the market dove all of the way through the SELL strike price at >2.870 to around 2.850. Two opportunities now presented themselves:

1. Exit the trade early and take profit, or

2. Let the trade continue for the remaining half hour and see if it expires at or below 2.870 for a full profit, bearing in mind that if the market expires above 2.870, the payout is \$0.

The trade expired at 2.8456, allowing the SELL contract at >2.870 to expire in-the-money for a maximum reward of \$86 per contract. The BUY contract settled out-of-the money for a payout of \$0, resulting in a loss of the \$20.25 risked on that trade. This resulted in a \$65.75 profit (exchange fees not included).

There are many strategies for trading the news, but an OTM binary options strategy gives you the opportunity to profit from large moves in the market without exposing yourself to excessive risk.

SPECIAL OFFER

Open a Free Nadex Demo Account here - www.TradingPub.com/demo

It will be funded with \$25,000 in play money. Test these strategies and see how they work out for you.



ABOUT THE AUTHOR

Cam White is a Partner Relationship Manager with the TradingPub. When he joined the Pub in June 2014, his first assignment was to become familiar with Nadex. He downloaded the demo software and dove into the Nadex platform. A self-professed “crash test dummy”, Cam tests directional and non-directional strategies with Nadex Binary Options and Nadex spreads and publishes results.

Cam also publishes The Probability Report, which can be found at this site - www.TheProbabilityReport.blogspot.com . It is a monthly newsletter featuring Nadex webinars, and contributes articles on Nadex to financial media outlets.