

Greetings from the Pirate!

Hi everybody, I hope this edition of Traders Edge Insider finds each of you safe and ready to take advantage of some of the opportunities that are sure to abound as we head into the 4th quarter.

While many tend to fear October, given that some of the nastiest market breakdowns occurred during the month, the fact is September actually holds the dubious distinction for being the worst-performing month in the market—actually sporting negative returns historically.

Now we definitely want to be on guard for any sort of October surprise. That's especially true given the economic and political backdrop both here and abroad. That said, the major indices have surprised many and stand now poised to challenge and even overtake all-time highs.

Considering the events dating back more than a decade, it makes sense this could prove to be a pivotal—maybe even critical—period for the markets... Or not... Time will tell, but we do appear at some sort of crossroads.

Whatever occurs, we are going to trade what the market presents us with, just as we always do. For now, I encourage you to read and reflect on this month's edition of TEI—you'll find it's packed with plenty of good info that will benefit and enlighten as together we move forward into what is sure to be an interesting period in the markets!

— Preston James



Preston James
—Author,
"The 1% Solution"

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Upcoming Events & Special Announcements

The Indicators are Here, The Indicators are Here...

Good news for our [Swing the Axe](#) trade community. Karson and Jeff are pleased to announce that the Augen indicators are now available for download! That's right, now you can download our proprietary indicators to your own system, empowering you with the ability to use the indicators real-time at any time. You can customize your screen setting, look back in time and take advantage of the many other cool features. What's more, you can use them for any stock, currency or ETF over

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Karson Keith's Options Insight

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Coaches Corner

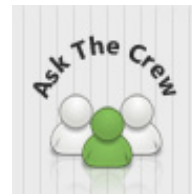
Hi, I'm Jon Wirrick joining you once again in the Coaches Corner. Those of you who have had me as a coach know I'm a big fan of the "keep it simple" ...



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Ask The Crew

Crew members tackle questions submitted by readers each month...



[Read more » page 15](#)

Norman has created a series of FREE "Mastery Minutes," one minute-motivators for traders, to help you avoid big trading losses and increase profits. Download them here: [FREE "Mastery Minutes"](#)

Karson Keith's Options Insight: Buying the Election. QE3 Flop?

By Karson Keith



It is no secret that during an election year the market usually finishes higher. This year we have a president that is more determined than ever to "buy" the election.

But despite all of the attempts to prop the market up we find ourselves only mildly higher for the year. The most recent "stimulus", QE3, is short-lived so far. The market made one minor move on the announcement day and since then has been back to normal.

There are several reasons why this stimulus has been ineffective, but the primary reason I believe it will continue to make little or no difference in the markets is TRUST. The previous stimulus plans simply didn't work as expected and they were much more direct than QE3. So why should anyone expect QE3 to work when the previous attempts failed?

The world is in turmoil so it is very difficult to identify the exact reasons underlying why the market does what it does sometimes, but it is clear that QE3 has not had the desired effect thus far.

It bears stating that only a few election years have finished lower on the year, the most recent being

2008. That said, I don't believe you can blindly place trades based on historical election year patterns, given that we are in a completely different world with dynamics that did not exist previously.

On a side note, it is looking more and more like AAPL has seen its peak.

Karson Keith

Karson Keith's interest in trading started at a very young age. By age 13, he began trading and managing his father's money. Today, his passion for trading has attracted a following of like-minded income traders seeking his help in taking their trading to the next level.

Karson specializes in cutting-edge options strategies, volatile markets and small trading accounts. He not only has single-handedly grown several small accounts into large portfolio margin accounts within just a few months, but he has also helped countless people achieve the same results.



Money Chasing You - Trading Success Stories

"I really appreciate the past two Tuesday Swing The Axe webinars. They have (been) full of extra information and have helped me make more winning trades and fewer losing trades. This past Thursday all my trades were winners.

The Straddles/Strangles and Short Butterflies have also opened up a new, surer way to trade. The extra information on Leading Indicators was almost a "crystal ball" to look into the future.

I feel that all this terrific information, with the ability to replay the webinars, trains the group to become "snipers." We can find the exact target. See it clearly in the cross hairs, then execute! We get in at or near the correct time, then exit at the correct exit. If our entry is not at the exact top or bottom, we still have up to five minutes in many cases to compensate our entry or exit. We can "snipe" the market using our Indicators and make money so much more accurately.

Thank you both for all your work and the understandable way you present the Indicators to us."

W.R., SC

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Monster's Perspective: September was a great month for Time Warner

By Jon "DRJ" Najarian



Chris McKhann and David Russell of optionMONSTER have been tracking the big media company Time Warner throughout the month of September and we thought the Traders Edge Network readers might be interested in their research.

On September 10th David's headline read "Confidence Shown in Time Warner" over this TWX chart:

remain above \$41, they'll keep the \$0.31 credit and options will expire worthless.

Selling puts is a common strategy when investors like a stock but don't want to expend capital getting long right away. It lets them program an entry at a lower price if a pullback occurs, while also letting them make some money if it never touches to their desired level.



He wrote "One investor is selling puts in Time Warner as the media stock returns to levels last seen when the tech bubble was deflating".

optionMONSTER's tracking programs detected unusual volume in the October 41 puts, with 10,250 contracts trading against open interest of 1,724 contracts. They all changed hands for the \$0.31 bid price, indicating that they were sold.

The investor is on the hook to buy shares in the media company for \$41 if they close below that level on expiration. But including the premium already received, their entry price would be \$40.69. Should the stock

On September 9th, TWX was down 0.3 percent to \$43.51 in morning trading, but is up 23 percent in the last three months. Earlier in the session it touched \$43.84, its highest level since mid-2001. Today's put- sale activity pushed total option volume in Time Warner to more than triple the daily average.

On September 27th Chris led into his story, "Limited Downside Seen in Time Warner" by pointing out that "Time Warner is just off four-year highs reached last week, and one trader is targeting a floor beneath the stock."

A trader sold 5,950 December 38 puts for the bid price of \$0.27, according to optionMONSTER's system. Open interest was 1,637 contracts at the start of the session, so we think that this is a new position.

This put selling could be viewed as another bet that TWX will remain above \$38 through the December expiration, a level that has seen support going back to July. This trader is also showing a willingness to buy shares on a pullback below that level.

TWX is up 1.9 percent this morning at \$45.49. The media giant closed Friday at \$45.90, its highest level since September 2008. Shares were below \$29 a year ago and broke through resistance at \$39 at the start of August.

Remember that short puts can be an excellent way to acquire stock or generate income in your account. Many retail traders use this conservative strategy to generate income in their accounts.

Jon "DRJ" Najarian

Jon 'DRJ' Najarian is co-founder of optionMONSTER® and co-lead analyst for the InsideOptions™ trade idea alert systems. He spent the first 29 years of his trading career trading in and around the pits of the Chicago exchanges. Jon is a frequent contributor to CNBC, the Wall Street Journal, and other prominent financial media organizations. Mr. Najarian also co-developed the patented trading algorithm the Heat Seeker®, used to detect unusual trading activity.



Upcoming Events & Special Announcements, *cont'd...*

any timeframe and in any size. You've asked and now we're happy to deliver—directly to your home system. Check the [Swing the Axe](#) site for further details. Please keep in mind these indicators only work on the Trade Station platform.

Traders Edge Network Blog

Be sure to check out the Traders Edge Network blog each Thursday afternoon, as TEI Editor Louis Horkan offers a bit of tongue-n-cheek commentary on what's occurring, as well as insight on things you need to be aware of and suggestions on how best to succeed in these markets. Trust us, this isn't the same ol' staid, button-down rehashed news or analysis you're accustomed to running across most places! Join us each week on the Traders Edge website (www.tradersedgenetwork.com) and be sure to leave a comment telling us what you think...

Money Chasing You - Trading Success Stories, *cont'd...*

"I have become fascinated by the Augen Indicators. I experimented with it in the early morning hours (3.00 AM). The performance is really astonishing.

Thanks for your delivered supreme services. From (what) I have seen thus far (the indicator really captured the volatile moves of yesterday excellently) I will become a long term subscriber of the Phase Indicator."

R.S., NE

"Sincerest thanks to Jeff and Karson for the amazing webinars! I have been trading my own portfolio for about ten years now and heard many good things about Mr. Augen. There was so much great information that I learned from the webinar that I am in the process of getting all of Jeff's books as we speak.

I am very excited about implementing what I have learned so far and look forward to continuing up the learning curve with the great information that can be found in the materials."

E.W., IL

Traders Talk:

TEI's Louis Horkan Interviews Norman Hallett



In this month's Traders Talk, we're chatting with Norman Hallett, CEO of Subconscious Training Corporation, the producer of The Disciplined Trader Program. Norman is a highly-regarded professional trader with more than three decades of successful trading experience. He's devoted more than a decade to educating traders on how to become successful, with emphasis in the areas of trade psychology and the creation and utilization of solid trade programs. Norman shares his unique insight garnered from years of assisting thousands of traders worldwide in their quest for a discernible path to success in trading.

TEI: How'd you get your started in the business?

NH: I started in 1979 with a very small options firm that was selling privately held options out of the Mocatta Metals Corporation. This was before exchange-traded options came out during the 80's. That gave me an understanding of commodities and their potential.

The first individuals I worked with back then were either buying or selling options and we were working with the premium. We bought call options in gold and silver. In January of 1980 the gold price reached \$850 and silver shot up to \$50 with the Hunt Brothers. All those people that I had sold \$10,000 options to that had invested \$10,000 to \$20,000 suddenly had hundreds of thousands of dollars in capital in a matter of four to five weeks. I didn't realize at the time that was a historic move that wouldn't be seen for another decade or so. The potential of the market was indelibly etched in my mind.

Later I moved to Paine Webber, where I was hired to help increase their futures business... I eventually departed and became a commodity trading adviser and ran several million in my own program...I've spent the last decade primarily in the educational part.

TEI: What was the early lesson to come out of that time and experience?

NH: In the beginning you tend to want to add filters to your trading plan in order to define your trades...

take fewer trades, but better trades. What you wind up finding along the way is that too many filters causes a certain paralysis and a frustration which can lead you to taking trades that aren't really qualified trade. I found that long-term successful trading is a matter of knowing yourself and then balancing what you know about yourself with what's available in the market. I've learned that simple is good and complicated is bad...simplicity in trading is the key to successful-trading long term.

TEI: What made you realize the importance of focusing on the mental and emotional aspect?

NH: Well, I had been working with my own mental game for a couple of decades. I didn't realize that what I was doing was really taking some of the things that my wife, one of the premiere hypnotist in the southeast United States, was doing with her clients... helping people with their lives. I came to understand that what you believe and hold predominant in your mind is where you're going to head. If you don't see a bright and successful future for yourself as a trader and keep that thought predominate in your mind, you won't head in that direction. If you're being controlled by fear of performance and constantly reminiscing on what went wrong with trading versus what's gone right, your projection to the future will be clouded. The clearer you are on having a positive outcome in your trading, the more you do the things that will create that positive outcome.

TEI: You started to concentrate on the education part along the way. What was the genesis for doing so?

NH: A decade ago I decided to concentrate on the mental and emotional aspects of trading. This is what most traders ignore. No trader wants to say, "I'm the problem." The answer to poor results in trading is always "I need a better system or a better way to analyze the market." But those solutions never turn to you. That's where I come in. During that time my wife actually came home one day and said she had worked with a stock broker that day that was having

trouble with his trading. Suddenly it hit me right smack in the middle of the head...I'm living with the solution. Been married for 32 years and I realized my wife could really help me to translate what she does to help a lot of traders... It was the realization then that we we're really living this and seeing it work for me that led to us taking that and making it available to everybody. At least that part of the training—the mental and emotional control. So in our program, we have a large section on really training your mind on the subconscious level.

TEI: Can you share some on mastering trade psychology and how you address it in your program?

NH: At that time I thought to myself there are not a whole lot of people in the area of trading psychology. Yes, there are authors...Mark Douglas, Van Tharp, Jake Bernstein who wrote "The Investor's Quotient" and others. They all talk about the poor thoughts that come up and how you have to control them through having a solid trading plan. Although that's true, that's not the fast track for individuals in the mental control area. The fast track is to actually train your mind on a subconscious level so that you're decision making, which is your conscious mind, is not dominated by negative thoughts about your trading or about you. Your subconscious mind holds your beliefs about what's true for you. Your conscious mind makes decisions based on what those truths are. So, if you're making poor decisions in your trading, it's likely because you're holding a subconscious dominant pattern that's not beneficial to your trading. For instance, as a trader you may think that trading is gambling. As a child you might have heard your parents talking about how trading is gambling. And then all of a sudden you wonder why you can't pull the trigger on a trade. It's not something that's obvious, but if you look into it you can see that the problem is a subconscious pattern that's not serving you as a trader. The great part is that you don't really need to go to a psychiatrist or psychologist to delve into what the problem is...All you really need to do is create another subconscious set of neural nets that carry the right message:

*I have a valuable trading plan.
I pull the trigger every time my trading plan gives me the signal.
I believe in my trading plan.
I'm a wise and disciplined trader.
I do the things that a wise and disciplined trader does.*

Those kinds of beliefs, if established in your subconscious mind, will have you making the right decisions. Your conscious mind will make decisions now based on these new dominant behaviors. And the way to get them to be dominant neural pathways is to just really relax and do a little self hypnosis—it's very easy.

TEI: What do you consider the biggest impediments to successful trading?

NH: Based on the feedback we get in our training, a big one is focus. To remain focused and to eliminate distraction. Whether it's CNBC, somebody walking into the room, self-created distractions where you step away from the screen, etc. Without focus you're going to make mistakes. You tend to forgive yourself, but if you look back you'll find they were all preventable. You need to follow and remain with that trade in a very focused manner. You must consider your trading a business and maintain disciplined focus.

Another area of great importance is patience—you need to be patient in your trading...wait for the setups to complete themselves. I find that a lot of traders jump the gun. Their trading plan says they make their move after the formation on the 10-minute bar is complete. But at the nine-minute point the market is moving up and they jump in to grab those points, since obviously the trade is going in the right direction. But of course, the market often corrects and the sought-after formation never actually completes, leaving them stuck in a bad trade. Patience is a key virtue in trading. Patience to let the trade go if it's not going to happen...to not take the trade. So you must be patient and wait for the A-plus trades—the high-probability trades. You need to identify those high-probability

trades for yourself and then spend your time being patient for those to happen.

The third is keeping a positive expectancy. In other words, expecting success and envisioning yourself as a successful and valuable trader. Create some positive energy in the very beginning of your trading day, whether it's doing some affirmations or some subconscious training. We actually offer Mastery Minute one-minute motivators for traders that can be downloaded to the iPhone. They provide a one-minute pop of enthusiasm and positive energy right in the beginning of the day. Those are the three areas I would concentrate on as a trader who is struggling and looking for real and consistent change. Not another system or another Holy Grail.

TEI: What are the biggest mistakes you see traders consistently making and what should they focus on?

NH: I find that traders give up too easily. Also, it's about maintaining a total program. It's one thing to maintain a positive vision of the future as a successful trader, but it's not going to have legs or be believable to you unless you've done the homework. You've got to have a solid trading plan and I find that too many traders don't. Having a solid trading plan that you can believe in is something of extreme importance. Without such a plan you're really not going to get any place.

Along with the positive expectancy you need to concentrate on keeping things simple rather than complicated. And you have to spend your time focusing on your A-plus trades. You need to go back to your past trades and look for the setups and the exit strategies that resulted in your best success as a trader. Then have the patience to only trade those particular A-plus strategies. This is important because you've already proven to yourself that you'll win more if you stick to those strategies. If you stick to making the A-plus trades you're making fewer trades, saving transactional costs and headaches, and you're taking the more high-probability trades based on your own success and history. That's the kind of structure that you need to create in order to ensure that when you're envisioning your positive expectancy, it has roots that

you can actually believe in. Then it's a matter of training your mind to follow it...to execute the trade and then execute the exit strategy.

TEI: Your experience is that traders generally haven't focused enough on trade psychology?

NH: I'm always asked the question of how many traders actually win and how many lose. When I'm in front of an audience I'll always ask that question. I'll get people yelling 99 percent, 90 percent, 80 percent... And they're about right—studies have been done and the actual number is about 90 percent. Why is it that the vast majority is losing? I think there is a correlation between the vast majority paying little or no attention to trading psychology. Everybody needs to understand trading psychology, but nobody really wants to. Nobody wants to admit that they are the problem. So I wind up seeing people all the time that have already blown out two or three accounts. They realize that they've got to do something different or get out of trading. I'm always thrilled when somebody just starting to trade comes to me—I really feel that they've done it right. But it's a rarity... The fact is you don't have to experience the pain in order to get to the profit.

TEI: What's your advice for the person that's been at it a while, but continues to struggle to turn the corner and achieve profitability?

NH: At some point the frustrated trader has to draw a line in the sand and say this is either going to work for me or it's not going to work for me. They should focus on their experience. They have to find a way to stay positive—to develop a positive frame of mind so that they're not doubtful moving forward with their trading plan. They need a trading plan that recognizes the need for daily affirmation right in the beginning...something to pump them up...not falsely, but something that gives them real confidence on a daily basis... Over the course of time a good trading plan will result in a positive outcome. You must have a responsible trading plan that's been back-tested, has great money-management elements, good risk rewards and so on. You also need to simplify and have the patience to wait for the A-plus trades. If you trade less, but more

effectively, I think you're going to find that all of your past experiences will feed very well into knowing what a good trading plan is for you... We didn't talk much about this, but it's important to look into who you are and the kind of personality that you are. You need to have a trading plan that fits who you are. Focus on those pillars in your structure and you're going to be more successful.

One other key element not focused on enough is having clarity of your exit strategy. This is really where you should be spending the majority of your time. Not on your entrance, but your exit strategy. That's where I come in mostly. The majority of traders will spend most of their time and focus on entering correctly and then looking for a place to pull profits or exit and take a loss. You've got to have an exit strategy that is a little more sophisticated than that.

TEI: Let's finish it up with your best parting advice.

NH: We've covered most of the points. I would again emphasize the idea of identifying you're A-plus trades based on your own experiences in trading...not just back testing. Your experiences are a sum total of what happened in the market and your response to what happened. So if you're noticing that something happened in the market and your response to it resulted in a positive trade 70 percent of the time, and the risk reward was very good, then that should become your A-plus trade. Have the patience to stick to those set-ups...you're much better off taking the higher-percentage risk in high-probability trades versus spreading your risk over lower-probability trades. So be patient and concentrate on the high-probability trades.

The other key point is not to be afraid to train your mind. You're in control of your mind. What do you put in your mind by looking at CNBC every day...you're putting in the fears and the emotions of the market, which isn't necessary a good thing. Everything in the market, including the emotions, is in the chart. All the emotions and other things that can affect us are irrelevant, because they're already considered in the last price that was traded in that market. So analyze the chart and trade what you see. Stay in control with the positive expectation of your future, keep a very tight risk-management policy, specifically define your exit

points and you're going to see your fortunes turn from negative to positive—from struggle to success. Keep control of what you can control and ignore the things that you cannot control. It's really as simple as that.

Norman Hallett, CEO, STC

Norman Hallett is the co-founder and CEO of Subconscious Training Corporation (STC), headquartered in Parkland, Florida. STC develops state-of-the-art mental training software for a wide variety of areas, ranging from business to sports to business skills to trading.

The company's core concentration is the training of Traders through its 6-week online "The Disciplined Trader Intensive Program".

After having spent time with Paine Webber as a stock broker, Mr. Hallett has developed numerous successful startup companies, including the CTA investment firm of Hallett Commodities, Inc., and the Introducing Broker operation, NCH Commodities, Inc. Mr. Hallett holds a BA in Mathematics from the University of Cincinnati.

His high-profile style resulted in him being a frequent guest of the Financial News Network and culminated in his popular radio talk show, "Risky Business", which had a strong 5-year run.

His concise ebook, "Mental Fitness for Traders", went viral and has been downloaded by over 100,000 traders worldwide.

The Disciplined Trader Trading And Support Program has tightened up the trading discipline of thousands of traders from 16 different countries.

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Musings from the Editor: Worries Aside...A Hidden Message?

By Louis Horkan



Well, we've come through the tricky month of September and managed to close out the 3rd quarter in fairly decent fashion, all things considered. As things stand now, the broad indices are flagging bull, with both the INDU and the SPX within relatively easy distance of tagging historical highs in very short order.

So, let's take a gander at some of the bigger, more pressing issues to gain some perspective on how they might play out and influence the markets in the home stretch of 2012. (For those of you who might complain that the Mayan Calendar issue was overlooked—save it for the hand...)



With such a backdrop, you'd think the world was at peace and things stood in good order...not so much. Not gonna find many peeps that will argue against the fact that the world is a mess.

Moreover, we would appear to stand poised for resolution on a number of key macroeconomic and geopolitical fronts (fair to say dangerous in some cases) as we head into the 4th quarter...no small matters, to be sure. It's not hyperbole to state that a number of the issues at hand might well shape things positively or negatively for some time to come.

What all this is gonna mean for the markets and us as traders remains to be seen. While I am one who veers toward being informed and influenced almost entirely by price action, failure to attempt to gain some perspective on the big picture is a fool's game.

Home-Front Issues

In the U.S., we are faced with the just initiated QE3, which has been met so far with the enthusiasm of Rocky VI. While the allure of cheap money and a guaranteed window of Fed accommodation is appetizing, the fact is things are heading in the wrong direction on a number of key economic fronts and this is a bit of desperation by a Fed that is growing increasingly concerned we will slip yet again into recession. That doesn't mean that the move can't or won't help, but we do need to see it for what it is and what it implies—the long-awaited light at the end of the tunnel may not be at hand...a depressing prospect, given the expectations built into this year in terms of recovery.

We also have the fiscal cliff just over the horizon and the implications there are huge. Frankly, neither side wants

to deal with the fallout, but the intervening election makes it impossible to do anything for the time being. So it would appear we are again set for a theatrical production of last-minute gamesmanship in Washington. Hopefully this time around the pols will come to agreement before lasting damage is done.

Speaking of the election, we will soon enough be delivered (for now) from the deluge of commercials, daily polling data, non-stop news coverage and the paid hoard of prognosticators employed by both sides to convince us they are the party offering real answers.

For now we can expect the rhetoric to step-up in more shrill fashion leading to November 6th. No doubt we'll be treated to more generous helpings of the ol ditty "this is the most important election of our lifetimes" mantra bandied about by self-interested pols. It may in fact be true this around, given the state of the country and the world, but we've heard it all too many times and there are few left that believe the notion that "who" sits atop the throne in DC will have any real effect on where we go from here.

Looking abroad...

Middle East

The Middle East has always been a powder keg and the West has long maintained a penchant for misreading the tea leaves in that part of the world, as it were. The most pressing concern is the nuclear issue in Iran and the increasing isolation on the part of the Israelis in the region, given the Arab Spring developments and fallout. Don't misunderstand that for taking sides or assigning blame. Simply an observation on the lay of the land as it stands now.

While the players in the region are decidedly at odds, what's equally troubling is the fact that while leaders the world over have long-feared a nuclear-armed Iran and have sworn that such would not come to pass, collectively (ourselves included) they've done little more than dance about and skirt the hard issue.

Well, the time of saber-rattling and gamesmanship may well be morphing into a much more dangerous form. We've convinced ourselves for many years we could

control this issue and it would somehow work itself out. We are only now waking to the fact that we have no real control or sway in the region. We lack the political will to do anything, so the Israelis have now put a true red-line in place. Agree or disagree with their stance or our approach, fact is we've disengaged and punted on the issue—now we are forced to sit back and hope.

Don't know bout you, but I find this to be the scariest situation facing the entire world and there really is no overstating how ugly and disrupting this entire scenario could become.

Beyond the threat of war in that region, we are left with the reality that oil prices stand to sharply climb (barring some sort of positive resolution between the parties) due to disruption concerns and the accompanying fear premium that will drive up the price of crude. Such an increase could easily topple our nascent recovery and drive the economies of Europe deeper still into recession.

Europe

What hasn't been said about Europe? Odds are still very much in favor of a Greek default. And other members of the PIGS remain very much in peril, sans the Irish. The focus is on Spain for now, but the issue has always been the shared currency and lack of a central bank with the power to specifically address the concerns of each individual member of the Union. Oh, and the hard core stance taken by the Germans. Well, not to blame them... they are simply acting in their own best interest, which is a core tenet of economic theory—we all do it.

While the situation remains acute, the fact is the world has become accustomed to the notion of the Euro doing a deep six and the Union itself breaking apart...if it comes to that. While this entire tragic drama has play out painfully slow and has caused tremendous disruption throughout the global markets for several years now, this may turn out to be one instance where the "kicking the can down the road" approach on the part of European politicians may have actually worked to their benefit and ours.

That said, the problems remain myriad...and they can and will bring us down if they unwind further still. But on a comparative basis, the situation is not near what it was this time last year. Bottom line, they are in a recession and

will be for some time to come...and thereafter growth will remain anemic for some time to come. But they aren't going away and however it plays out (with some or none exiting the EU) the European parties will emerge and once again exercise collective muscle on the world stage.

China

The big-red engine has slowed considerably in this past year. They have been the driver for quite some time and have been a counterbalance to the problems in the West during the course of the financial crisis, so this is indeed a problem. Safe to say the fears they might stumble, which in turn would likely torpedo recoveries in economies the world over, have come to pass...more so in Europe than anywhere else.

Exacerbating the issue of slowing growth is the fact we remain largely ignorant when it comes to China and its economy. While we can gauge the health of our economy and that of most other areas of the world, we continue to fly blind when it comes to what is fast emerging as the second most dominant player in the world. Tis fair to say that guessing the "hows" and "whens" regarding growth in an economy of such import is not the prescribed approach when it comes to managing our own economy.

But guessing is in fact what we are doing...and will continue to do until such time as we strengthen bonds and our overall relationship. There's certainly lots of questions to be answered, such as where it is headed, how it will assume it's role as a super power, how it will do when forced to carry the weight of the world (as the U.S. has done for decades), whether they will truly open their borders and markets to the rest of us, yadayadayada...

The one thing we do understand for certain is that the government there is very pragmatic. While they may cheat at trade, prop up numbers/cook the books at the corporate and governmental levels, engage in shenanigans with their currency, etc., we can count on them to throw a whole lot of money and resources at keeping their economy bustling. Translated, while Europe and the U.S. are hamstrung, China is flush and will take all necessary measures to move forward themselves and the rest of us. Sure there will be bumps, but betting against them and their ability to "spend" the rest of us into growth is not a bet I'd take.

Comparatively Viewed

Serious issues all, to be sure. Plenty of reason to believe we are in for some sharp reversal from these near-record levels. Well, there you have it...end of story...

Not to be a nudge, but I wouldn't mind throwing out one or a couple simple questions before setting out to short the market... With the backdrop being what it is, why are we parked where we find ourselves? Is this nothing more than a pratfall setup that stands ready to ensnare the bulls and believers? That might very well be the case.

On the other hand, maybe there's some method and logic to the fact markets here are poised near historical levels. Might it be that the market has discounted all information, as it is supposed to do, and having engaged in an exercise of relative/comparative analysis, decided that the picture is better than would appear?

Running a bit with this mindset, it's worth considering where we've come from and what we've dealt with in the past dozen plus years—pretty amazing stuff. What's most surprising is that we remain far from healed. In fact, we've accomplished little in addressing those issues that got us to this state in the first place.

In that sense, we are very much like Rocky. We've had the hell beaten out of us and acted terribly (sorry to you Stallone fans out there), yet bloodied and bruised we continue to stand. Economies here and abroad continue to function. And it's fair to say we are probably closer to the end of this mess than the beginning at this point.

Perhaps that is the message of this market...

Look, I certainly have no idea where things are gonna go...nobody but the fool will claim such knowledge. I wouldn't be surprised to see the INDU and SPX u-turn today and provide us with yet another October downside surprise. Frankly there's no need to spend much time contemplating that scenario. Suffice it to say that were the markets to tail-turn and head abruptly south, it will be perceived as a very negative signal...one many will view as a "Tell" that we are gonna backslide into recession, further extending this painful period. A downer, to be sure, but not total calamity.

On the other hand, what might an upside break represent? Maybe nothing at all. Or, maybe such a move would signal something well beyond a bullish technical trigger for the broad markets. Would it be foolish or naïve to view it as recognition on the part of the market that the underpinnings of real healing are in place, combined with a view that the horizon holds promise for organic growth within our economy.

of economic disaster. Yet we have come through it all intact...changed, but very much still in the game.

Moreover, when you put things into perspective, we have survived in this past decade just about anything you could possibly envision, short of nuclear war. Ironically, that is more of a real possibility today than at any time since the Cuban Missile Crisis.



Pollyannaish? Perhaps...

Trust me, I'm not going out on a limb to guess "what ifs" or to read tea leaves. But it's worth noting as we enter the new quarter that unexpected catalysts have emerged in the past that turned decidedly bad periods around. The release of the Iranian hostages is a good example. Some would even argue the US Olympic hockey victory around that same time changed our mindset and became a catalyst for renewed hope. The same can be said for the collapse of the Soviet Union, poignantly punctuated by the fall of the Berlin Wall. Historic events all that positively influenced our psyche and our desire to engage in the markets.

Can the emergence from the turmoil of the past dozen or so years be placed in the same category or given the same weight? Dunno... we shall see. But the fact is we have come through the worst economic period since the Depression. We have existed for some time on the brink

Notwithstanding such a chilling prospect, the question at hand is whether there is indeed a message in the market for us to discern?

Time will tell...

~LH
Editor

Louis entered the biz in the late 80s and spent over a decade working as a trader, instilling him with unique insight into trading and the markets. In 1998 he switched gears to become the group editorial director for a large network of award-winning, trading-focused newsletters. In 2002 he became the founding editor-in-chief for two financial trade magazines—each served approx. 40,000 independent financial advisers nationwide. He's appeared on business TV, in the business press and on numerous biz-focused radio programs in the past. He writes market commentary and analysis most days and trades on a daily basis.

Coaches Corner: Six Building Blocks of Trades

By Jon Wirrick



Hi, I'm Jon Wirrick joining you once again in the Coaches Corner. Those of you who have had me as a coach know I'm a big fan of the "keep it simple" philosophy. As such, I thought I'd take a different approach and focus on helping newer traders break down and understand the types of stock trades available in trading.

In my experience, traders often get overwhelmed by so many of the different strategies out there. Strategies with multiple legs in them, often referred to as spread trades, can be particularly difficult for those new to trading. I've found that by stepping back and dissecting the various trade options, traders generally find them easier to understand—and in turn execute.

The reality is that there are three main instruments you can trade in the equities market; a stock, a call option or a put option. That's it! With each of these there are only two things you can do—buy or sell. This means that there are really only six basic types of trades you have to focus on as a newer trader.

- 1) Buy a stock long, which is a bullish debit trade.
- 2) Sell a stock short, which is a bearish credit trade.
- 3) Buy a call, which is a bullish debit trade.
- 4) Sell a call, which is a neutral to bearish credit trade.
- 5) Buy a put, which is a bearish debit trade.
- 6) Sell a put, which is a neutral to bullish credit trade.

All trades are made up of some combination of these elements, which I refer to as the six building-blocks of trades. If you've been feeling confused with some of the different strategies, take the time to learn these six trades inside and out. When you're analyzing a position you just have to break it down.

Buy a Stock Long – You buy a stock with the hope that it will increase in value. You can then sell the stock at a higher price and you make the difference. Example – Buy XYZ stock at \$50. If the stock goes up to \$60 and you sell it, you make \$10 per share.

Sell a Stock Short – Selling a stock short is the exact opposite of buying the stock long—you're anticipating

the stock dropping in price. In a short, you reverse the order of buying and selling, so you sell the stock first. You can then buy the stock to close the trade at a lower price and you make the difference. Example – Sell XYZ stock short at \$60. If the stock drops to \$50 and you buy it back to close the position (referred to as a buy-to-cover order), you make \$10 per share.

Other than short-term day trades, I don't typically sell stocks short. Buying a put or employing a spread strategy involves far less risk and offers the advantage of greater leverage. When selling a stock short your risk is theoretically unlimited because the stock price can rise infinitely and the money you'd have to pay to purchase shares would rise with the price.

The reality is that you can make or lose money whether you buy a stock long or sell a stock short and no stock goes to infinity (except maybe AAPL). You should always define your risk when you enter a position and manage it accordingly. Plan your trade and trade your plan.

Buy a Call – You buy a call in anticipation that the call will increase in value. You can then sell the call back to the market at a higher price. Example – Buy an XYZ Dec \$50 call for \$3. If XYZ goes up in value and your call increases to \$6, you can then sell the call to close the trade and you make \$3 per share, equating to \$300 per contract. Keep in mind that a call option represents the right to buy the stock at a set price. Calls typically increase in value as the stock rises.

Sell a Call – You sell a call in anticipation of the call dropping in price. You can then buy the call to close the trade and you make the difference. Example – Sell an XYZ Dec \$50 call for \$6. If XYZ stock drops in price and the value of the call falls to \$3, you buy the call back for \$3 to close the trade and you make \$3, equating to \$300 per contract.

When selling option premium you can also let the option expire worthless if it is out of the money at the time of expiration. In this case, you achieve max profit, which

was your initial credit—the \$6 per share you sold the contract for. Assuming the call had extrinsic value when you sold it, the call will decrease in value if the stock stays where it is or goes down. Inversely, your risk is unlimited as the call increases in value as the stock rises.

Buy a Put – You buy a put in anticipation of the put increasing in value. You can then sell the put for a higher price and you make the difference. Example – Buy an XYZ Jan \$100 put for \$4. If XYZ stock drops and the value of the put goes up to \$7, you can sell the put to close the trade for \$7 and you make \$3. Puts are the opposite of calls. A call is the right to buy while a put is the right to sell. Puts increase in value as the underlying stock drops in price, so if you thought a stock was going to drop, you could buy a put.

Sell a Put – You sell a put in anticipation of the put decreasing in value. You can later buy the put back at a lower price and you make the difference (or let it expire worthless). Example - Sell an XYZ \$100 put for \$7. If the put decreases in value and you buy it to close for \$4, you make \$3 per share. If the put had intrinsic value associated with it when you sold it, the value would decrease if the stock price stays the same or goes up.

The next trades I want to cover are called spreads. Spreads are really just a means of reducing risk in a trade. There are many types of spreads but the most common are called vertical spreads.

Bull-Call Spread – You buy a call and sell a call at a higher strike price with the same expiration date. Since the call you are buying is more expensive than the call you are selling, this is considered a debit trade. The call that is purchased is the dominant part of the trade.

A bull-call spread provides a means for buying a call while lowering your risk. When you sell the higher strike price call you reduce your debit in the trade. Given that your debit in the trade represents your maximum risk, by reducing your debit you've reduced your risk in the trade.

Bear-Call Spread – You sell a call and buy a call at a higher strike price with the same expiration date. Since the call

you are selling is more expensive than the call you are buying, this is considered a credit trade. The call that is sold is the dominant part of the trade.

A bear-call spread provides a means for selling a call while lowering your risk. When you buy the higher strike price call, you eliminate potential infinite risk and effectively cap the amount of risk you have in the trade.

Bear-Put Spread – You buy a put and sell a put at a lower strike price with the same expiration date. Since the put you are buying is more expensive than the put you are selling, this is considered a debit trade. The purchased put is the dominant part of the trade.

A bear-put spread provides a means for buying a put while lowering your risk. When you sell the lower strike price put you reduce your debit in the trade. Given that your debit in the trade represents your maximum risk, by reducing your debit you've reduced your risk in the trade.

Bull-Put Spread – You sell a put and buy a put at a lower strike price with the same expiration date. Since the put you are selling is more expensive than the put you are buying, this is considered a credit trade. The put that is sold is the dominant part of the trade.

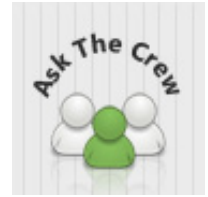
A bull-put spread provides a means for selling a put while reducing your risk. When you buy the lower strike price put, you gain the right to sell the stock at a lower price, thus limiting the amount you can lose in the trade.

There are myriad strategies available to be implemented in trading, but all equity trades boil down to these six basic trades. Remember that you can buy or sell a stock, buy or sell a call, or buy or sell a put...and that's it!

Jon Wirrick

Jon is an active trader and private coach to Traders Edge Network investors needing help learning to apply a consistent trading method. Through his mentoring, he has helped hundreds of people change their financial situation through trading in the financial markets.

Ask the Crew: Crew members tackle questions submitted by readers each month



Q: Just signed up for Weekly Options Windfall. Trying to find the math for selecting the long protective put in the calendar spread. Some positions are a month out, some are at the end of the year, some are a couple of strikes OTM and some are further. There must be some math to it; any insight you can provide would be very helpful?

A: There isn't an exact calculation to how we pick the puts. A very general guideline is we are usually spending about 2 times the weekly premium on the 1 to 2 month-out OTM put. However, Preston has been going a bit further out in time on a few of these and you want to pick protection that isn't too close to the money, yet still provides protection. Usually that is a strike or two out of the money.

Q: Where do you get the intrinsic value and the time value of a stock?

A: Intrinsic value is the amount that a strike price is in the money. If you buy a 250 call and the stock is valued at 255 then the difference between 255 and 250 is 5 dollars of intrinsic value. The option may cost 6.00, in which case the extrinsic value (time value) is the 6.00 minus the 5.00 intrinsic value, which equals 1.00 of time value.

Q: What are the risks involved when you do an iron condor? Also, what do you need to be watching for in order to exit the trade before expiration date so that you don't wind up buying any stock?

A: The risk in an iron condor would be the difference between the strikes minus the premium you received.

So if you took in a \$1 credit for both sides and there was a \$5 spread in your strike prices, you would have a \$4 risk on the trade. To avoid buying any stock or having stock put to you, keep an eye on the time value of your sold options. If the time value is less than 0.10, keep a close watch on your position and consider closing it. I've only been exercised early a couple of times. One time it was on a Thursday after a dividend had been paid out and I woke up being short several hundred shares of stock—the call was exercised. The other time the stock had a dramatic drop and the time value was at 0 and I didn't buy back the option and ended up with stock when the put was exercised.

Q: I am new to Pirate strategies on weeklies. When you get into a credit spread on a Friday and it goes against you is there a stop loss point or do you hold and let the spread be your stop loss?

A: The spread is your stop loss, but if things are just not going our way we will get out long before it gets to that point.

Q: Can you define what "things are just not going our way" is?

A: When we get into a trade we expect the stock to behave a certain way. For example, if we get into a position expecting it to pin to a strike price and it doesn't, then we would just get out. Every trade we get into we should have a solid idea what we are anticipating; if the stock is acting weird then we just bag it.

Our goal is to cover ground that will benefit the entire community...so get busy sending in those questions...



Money Chasing You - Trading Success Stories

Experienced recent trading success or have a lifestyle success story as a result of your trading?

We would love to hear it!

Please email them to: alicin@tradersedgenetwork.com

Comments, Questions, Contact Us

Hey Gang, when we say we value your presence in the Traders Edge Network, we really mean it! It's not really a network, or for that matter much fun, without each of you participating... Please don't hesitate to send us your thoughts, comments, suggestions, criticisms or questions. PJ

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