September 2012, Issue #4

The Traders Edge Insider

TradersEdge NETWORK

Print This Issue

Greetings from the Pirate!



I hope this month's edition of the Traders Edge Insider newsletter finds each of you safe and refreshed as you return from your Labor Day festivities and the summer season winds down.

This time of year is always exciting in the markets and there's certainly lots going on now, given the political conventions and upcoming election, as well as the continuing saga over in Europe and the questions surrounding the Chinese economy…and more importantly our own!

While the markets have been somewhat lackluster and volatility has been MIA for some time now, it's safe to say things are likely to start heating up and opportunities will surely abound. I look forward to working with each of you to take advantage of those opportunities.

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

Karson Keith's Options Insight



TEI readers know from my previous writings that I do not have an optimistic outlook on Facebook's near-term future...

Read more » page 2

Monster's Perspective



The time of year is probably even more important than news events as summer vacations have slowed trading activity to a crawl...

Read more » page 3

Traders Talk



In this month's Traders Talk, we're chatting with Jeff Augen, well-known author of a number of highly-regarded books...

Read more » pages 4-7

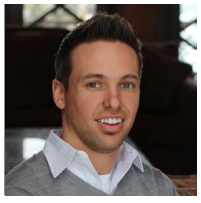
Musings from the Editor



Recently, while driving my two mick sons (Aedan and Colin) to soccer practice, I shared the ol' axiom bout working smart and not hard...

Read more » pages 8-11

Coaches Corner



Welcome to the Coaches Corner! I'm Mike Curtis and today I'd like to discuss a common myth among aspiring traders...

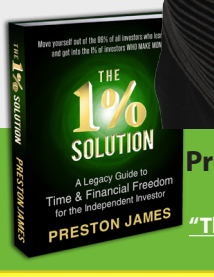
Read more » pages 12-13

Ask The Crew



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

Read more » page 14



Preston James
-Author,
"The 1% Solution"

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Our Accolades Are Written In The Stars!
"Best for Options Traders" Three Years Running



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Trade With The Best!

Upcoming Events & Special Announcements

Be sure to join us in the upcoming October edition of Traders Edge Insider when we talk with Norman Hallett, the founder and CEO of the widely-acclaimed training service The Disciplined Trader. Highly regarded as a coach and trading mentor with nearly 3 decades of experience trading the markets, Norman will share his thoughts and insights on the importance of mastering trade psychology and how doing so is critical to trading success…a notion much subscribed to here at TEI.

continued pg. 11

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Karson Keith's Options Insight: Facebook's Failure Continued...

By Karson Keith



TEI readers know from my previous writings that I do not have an optimistic outlook on Facebook's near-term future. When I first wrote about my gloomy outlook FB was bouncing around the mid 20's and shortly thereafter the low 20'—now the stock is at 18.

Obviously it has not been pretty for Facebook since the IPO. Given the magnitude of the decline, it's difficult at this point to know how much lower it will go, if at all. It's not unusual to see stocks that have experienced sharp, sustained selloffs suddenly decelerate in their decline and then settle in and remain entrenched at a certain level. While they won't decline further from that level, they struggle to climb as well.

This may be the case for Facebook now. As such, my outlook on FB shares remains bearish, but less so than it was. Accordingly, I'm now looking at slightly less bearish positions.

One scenario I'm considering now is a simple credit spread to capitalize on FB either remaining entrenched here or moving lower. I'd sell a call and buy another call further out of the money to cover the position.

A more complex position would be a forward ratio. I'd buy one call near the money and sell two calls further out of the money. The far strike can be adjusted down as time decay eats away at the position. You want to stay as delta neutral as possible.

For now, I will continue to keep tabs on FB for signs of continued decline.

If you have access to the Swing the Ax service, the Phase Indicators will help you better time when the downtrend is coming to an end.

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.

Print

Money Chasing You - Trading Success Stories

"I enjoyed our phone conversation about option Trading. I made another $1185.00 this week. Over the last three weeks I've made $4100.00 plus on two trades the first week and only one trade per week the last two. Needless to say I am extremely satisfied with Preston's Weekly Options. I am 68 and this is the most carefree, easiest, quickest, laziest, surest profits I've ever made in trading futures or options. Weekly Options Windfall has truly changed my life forever! Tell Preston he's my Super Hero!!"

A.G., Ohio

continued p. 13

Monster's Perspective: Does Capital Expenditure at AAPL Signal MONSTER Holiday Season?

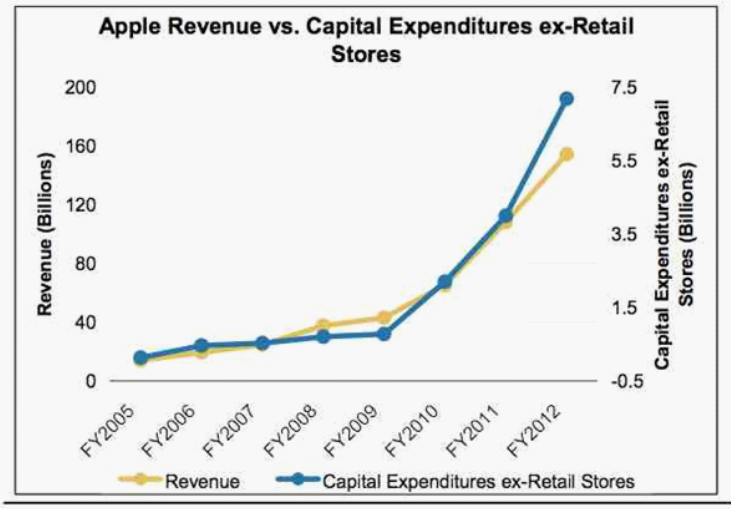
By Jon "DRJ" Najarian



The time of year is probably even more important than news events as summer vacations have slowed trading activity to a crawl. Equities have melted higher during July and August and are now drifting near multiyear highs. On the bearish side, investors see debt problems in Europe and lackluster growth globally. But it's been hard to sell stocks as the economy skirts recession and corporate finances continue to improve.

What better time to talk about AAPL and the Christmas Holiday season?

During the July earnings call CEO Tim Cook and CFO Peter Oppenheimer said that Apple's 4Q 2012 earnings guidance would be down due to a "product transition." Now to me that sounds like code for "we're building inventory for a new product." The two Apple execs repeatedly referred to "confidence in the new product pipeline," also code for a new product coming from the company. Traditionally, increases in capital expenditures at AAPL have a direct correlation to revenue at Apple, thus the spike in spending suggests the company may be set to deliver another record quarter this holiday season.



Source: Company Data, Morgan Stanley Research

Morgan Stanley's Katy Huberty did the following calculation for us: "Apple's revenue and capex ex-retail stores have been 97 percent correlated over the past seven years and the acceleration in capex growth signals a similar acceleration in revenue growth, in our view."

AllThingsD's John Paczkowski also sees Apple's prepayments for inventory components ramping up in a big way. Paczkowski pointed out that AAPL's prepayment for inventory components in the June quarter rose US$1.15 billion over the previous quarter. If you'll pardon the pun that's a MONSTER buildup!

Morgan Stanley's Huberty is forecasting Apple's revenue to reach $56.4 billion in this year's holiday quarter. Based on historical trends, Apple needs to allocate only $1.8 billion of its implied $3 billion of capital expenses in the current quarter to reach that revenue estimate. Investments outside of new product production, such as Apple's ongoing data center expansions, are not likely to represent a majority of the company's capital expenditures, Huberty said. Therefore she believes the $3 billion in expenses planned by Apple in the current quarter suggests a likely upside to her forecast of $56.4 billion in revenue for the holiday 2012 quarter.

Apple's best-ever quarter came in the holiday shopping season of 2011, when the company earned $46.33 billion in quarterly revenue and $13.06 billion in net profit. With the presumed launch of the new iPhone this fall, along with other potential products, Apple is poised to easily exceed its previous record.

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.

Print

Traders Talk:
TEI's Louis Horkan Interviews Jeff Augen



In this month's Traders Talk, we're chatting with Jeff Augen, well-known author of a number of highly-regarded books on option trading and the markets. Jeff has actively traded and analyzed the markets since the late 80s. That work, combined with his background in molecular biology, computer algorithms and dealing with venture capitalist and private equity investors, led to the development of his proprietary Augen Phase Indicators and the creation of the Swing the Ax program in partnership with Preston and Karson. In this first of a two-part interview, Jeff shares some about his background, critical changes he's witnessed in the market, the Phase Indicator and his unique insight.

TEI: Much of the work you do now is centered on the program trading and algorithms utilized by institutional trading groups and investors. What in your background led you to this area of expertise and influenced your work today?

JA: I started as a research scientist at IBM. I went to graduate school in molecular biology. I wrote computer programs and algorithms used for automated pattern search and recognition of protein structures. That work is the basis of this work now. The whole approach of pattern discovery and automated pattern search is underneath all of this work.

TEI: How did you end up working with venture capital groups, given you were a molecular biologist?

JA: I was at IBM in the Life Sciences Computing Group, which was a good fit for me given my molecular biology background. One of the most important goals of the group was to invest in venture capital funds. We had $400 million to invest in venture capital funds. The idea was to identify small emerging companies with exotic new technologies that we could use as headlights into new and future technologies. We weren't trying to make money from the venture investments, although the portfolio did make money. In 2001 and 2002, we were investing in companies that had very advanced biomedical and computing technologies. The idea was to focus on the computer side of the businesses—especially the algorithms and programs.

TEI: What was the biggest lesson to come out of that experience?

JA: I spent a lot of time with venture capitalist evaluating investments. What I came to realize is that people in general make reckless investments. Venture capitalists and private equity investors pore through every fine detail of a company and they only invest after getting to know everything about them. Yet if you asked an individual investor who purchased 1,000 shares of AAPL just a handful of simple question about the company, they couldn't answer you. Karson and I are always critical of long-term stock investing because we don't really know anything about these companies. I tend to know more than others, given my background, but I don't feel that I know enough to have any business investing in them. That perspective came to me by working with the venture capitalists and it forever changed my perspective on investing.

TEI: How would you characterize your early approach to trading?

JA: I was an option trader dating back to the late 1980s. I wrote a number of books on option trading, so my focus all along was options. As the markets became more efficient and more difficult to invest in, I started to focus on finding subtle distortions in the market and trading those distortions and trading the statistics and trying to make money in a way that didn't have a bias… I'm not long, I'm not short, and I'm not picking the direction or picking a stock.

TEI: You mention changing your approach to trading options as the markets became more efficient. Please explain what you mean?

JA: There are two types of option traders. First is the type who trade the mathematical and statistical

parameters around options—the pricing models and distortions—pure option traders. Then there are those that use options to trade stocks. They structure option positions because you can hedge with them, cap potential losses or gains, magnify the gains, trade more or less bullish, etc. Basically there's a litany of opportunities for option traders to trade stocks they have an opinion on. I used to be that kind of investor. I would have an opinion that a stock would go up, but instead of buying the stock, I would structure an option trade as a more sophisticated way to bet on stocks.

After spending a lot of time in the private equity world and with venture capitalists and looking at how they did their due diligence, I came to realize that I was really just getting lucky investing during the boom time when the market, especially the NASDAQ, was rising sharply. I was taking advantage of a boom period in the market. Granted I was making more sophisticated trades than most investors, but I was doing it during a boom time when the direction was pretty predictable.

Then after the NASDAQ crash, I realized that you could make much more money being short in a crashing market—markets crash down and not up. Sophisticated investors can make much more in a crash than in a rally. The second thing I realized was that picking the direction of anything was really very foolish. At that point I focused my full attention on trading the underlying mathematics of option pricing. So I switched from being an options trader using options to trade stocks as a proxy for stock investments to an options trader who trades the underlying mathematical properties of the options. That was a big turning point for me…probably about 12 years ago.

TEI: Why have programmed trading and high frequency trading proliferated in recent years?

JA: I say this all the time—the market has changed quite a bit in the past six months, but if you go back a year or more the change is really dramatic. High-performance super computers have taken over the market. The reason this has occurred is that the cost of super-computing has plummeted. Even going back two to three years, if you wanted to build a very high performance super computing infrastructure you really needed to spend hundreds of millions of dollars. Now for $10,000 you can have a desk-side super computer that has the power of a super computer from a couple years ago. This has created a proliferation of extremely high performance machines connected to the stock exchanges.

TEI: How does this impact the individual trader?

JA: The fact is that at any given time at least 80 percent of the action you see is not individual traders buying and selling, but computers doing the trading. Because of this, all the work that people have done on trading and analysis and charting over the last 50 years is all completely out of date. What you see now that appears to be long-term trends is really nothing more than the accumulated results of all these algorithmic trades going on all the time. Opportunities that might exist are now very quickly and efficiently extinguished, so it's very tough to trade such opportunities versus in the past. The notion that you can make an investment and hold it because of some insight you might have is now completely wrong because the markets change from hour to hour in today's environment. People don't want to believe that, but it's the reality of the situation now.

TEI: So you've created a proprietary indicator to track and take advantage of the algorithmic trading programs that are controlling the markets, correct?

JA: Yes, the main indicator that we use in the Swing the Ax service is called the Phase Indicator. To understand how it works, you have to first understand what constitutes a trend in the markets. Say you have an underlying set of circumstances or confluences of events that cause a computer algorithm somewhere to start to buy something, such as the S&P 500. That buying in itself triggers moves in the market that other algorithms start to sense. There are always groups of algorithms seeking opportunities to go long and others to go short. Because of this, you get the beginning of a rally, but there are moments of drawdowns because there are opportunities to short the rally, causing dips. So different programs are coming in at different times executing longs and shorts. Over time that creates

various phases in the rally. You may see a sustained strong rally followed by a minor correction. Then another rally, but not as strong, with fewer programs going long and more taking profits and some looking to go short. Then another phase begins that is not as strong or fast and corrections are larger. You get different phases in the overall rally. That continues till eventually you reach a point where the programs looking for long positions start to time out and stop and close trades. Finally the buying and selling pressure start to equalize and the rally ends or reverses and does what it will, but the real activity underlying the rally is finished.

TEI: In simple terms, what does the Phase Indicator do?

JA: What the Phase Indicator does is to deconstruct the market into those individual phases and studies them to determine which ones are more powerful. If you have a steep but short rally versus a less steep but longer rally, there's no simple way to compare the two, but the phase indicator does have an underlying mathematical capability of doing so. It can sense accurately when the rally is beginning to end. Same is true if the market is falling. The indicators are following the behavior of trading programs. They take rallies that are triggered by groups of trading programs behaving in different ways and they deconstruct them into different individual phases. Each phase is marked at the end with a subtle reversal. Some reversals matter and some don't and picking the right phases is not that simple. The indicator does it. It appears on our screen as a peak followed by a smaller peak and yet another. We can actually draw a trend line through those peaks, signaling the end of the rally. We call it right almost every single time.

To give you an idea of the strength of our indicators, we have an automated trading program (very crude at this point) that works off the indicators. We're actually going to replace it in the near future. It runs full time on the site trading AAPL. That program is making an unprecedented return and we joke about the fact that while it makes good entries, it makes terrible exits and is always giving up big pieces of profits. Regardless, despite the fact it's a crude automated system, it makes more money than the best investors at the best funds in the world.

TEI: Do you use any other indicators within the Swing the Ax service?

JA: We've actually applied the indicator across all the individual stocks in the S&P 100 simultaneously. We've taken that output and summed it and tracked it. We are now using that as our composite leading indicator, which is an enhancement to the Swing the Ax program. To give you an idea as to the indicator's capability, an early version of that indicator went completely off scale a couple hours before the flash crash of a year ago.

TEI: As far as Swing the Ax, please explain how a subscriber is able to use the service?

JA: Subscribers have been logging in to view the indicators streamed over our site, but now the indicators will be available for people to access directly on their own machines and choose anything that they would like to trade. Each month when people renew their subscription they will get a new package of updated indictors. They will always have the latest version this way. The Swing the Ax site will be a backup for subscribers. The users will be able to trade anything they want, be it Gold, oil, futures, currencies or anything else.

TEI: What's your comment to those that might be skeptical?

JA: We do something that nobody else does that I'm aware of—anywhere. We go live every Thursday morning in a webinar in front of hundreds of people. We put up the indicators and we trade real-time with real money, no matter the conditions. And we make money. We tell you to buy the ES now and we let you know that we'll tell you when to sell it. Then five minutes later we tell you we're approaching the top and the trend is over and time to exit. We get a flood of emails from subscribers each week telling us how

successful they've been using the indicators—literally thousands of dollars weekly. Frankly, you won't find others willing to do that, but we do so every Thursday.

TEI: What about people using traditional indicators to try to look for institutional footprints?

JA: I have a negative view of using more traditional indicators in today's market. They are all based into so many programs on millions of screens around the world now. Trade Station has something like 140 indictors or more on it. So anything that you see in any combination of those indicators will be extinguished in an instant. So they really have very limited value. That wasn't true before everyone had a computer, but now so many millions of people have access to indicators. The proliferation of indicators being used and the explosion in program trading have negated much of the utility provided by traditional indicators.

TEI: Best advice for traders, both new and experienced?

JA: To begin with, I would tell people that anything that is long-term is dangerous. Aside from that, the biggest mistake people make is to follow the investment advice that they get on financial news networks. Never take investment advice from anchors. It's a waste of time to do anything that they say. The things they highlight are already ancient history and the market has already reacted. Another mistake is paying attention to the big names and what they are doing. Like Warren Buffet is buying this railroad. People have to realize they are not Warren Buffet. When he buys he's not buying 100 or 1,000 shares, he's buying the whole company. His risk tolerance is much different than you have and he trades in a much different manner than you do. Trading on the advice of someone with 100,000 or 1 million times more money than you do doesn't make any sense. So, don't take investment advice from billionaires. It's a different game and you'll lose. Another is the concept of having a portfolio and being in the portfolio all the time. Diversifying is a mistake for most. That simply means spreading your money into a lot of different places with the hope you don't lose too much money in any one place. It's much better to become an expert at a single financial instrument or on one particular thing. Trade a very limited set of financial instruments and become an expert at that, be it option trades, stocks, etc. We trade a limited number of very specific things we focus our attention on and we become experts on them.

Jeff Augen, currently a private investor and writer, has spent over a decade building a unique intellectual property portfolio of databases, algorithms, and associated software for technical analysis of derivatives prices. This work forms the basis of a subscription service that he recently launched with Trader's Edge Network. It has also been the subject of six books from Pearson Education/Wharton School of Finance (Financial Times Press): The Volatility Edge in Options Trading, The Option Trader's Workbook; Trading Options at Expiration, Day Trading Options, Trading Realities, and Microsoft Excel for Stock and Option Traders.

Augen has a 25 year history in information technology. As founding executive of IBM's Life Sciences Computing business, he defined a growth strategy that resulted in $1.2 billion of new revenue while managing a $400 million portfolio of venture capital investments. From 2002 to 2005, Augen was President and CEO of TurboWorx Inc., a technical computing software company launched at Yale University.

During the past several years he has been an invited guest speaker at more than 50 industry events, an author of more than 150 articles, book chapters, and editorials, a member of 3 editorial boards, a weekly columnist for Stocks, Futures, and Options magazine, and the author of a graduate-level textbook, Bioinformatics in the Post-Genomic Era (Addison-Wesley 2005).

Augen has undergraduate and graduate degrees in biochemistry from Rice University and the University of Texas.

For More Information about Jeff Augen and Swing The Ax, please visit:
www.SwingTheAx.com

Print

Musings from the Editor: Work Smart…

By Louis Horkan



Recently, while driving my two mick sons (Aedan and Colin) to soccer practice, I shared the ol' axiom bout working smart and not hard. Well, being 10 and 9, they have transitioned from blindly accepting to carefully scrutinizing the bits of wisdom adults (which they refer to as "dolts," aptly so…) like to shower upon them… myself included.

So, they called me on the fact I had told them just five minutes prior that hard work was critical and to go out during practice and work their butts off or I'd personally chase em down in front of everyone. Ouch….hoisted by my own petard, it would seem.

Ego bruised from the comeuppance and keenly aware that the denuding of my invincibility was now firmly underway, I proceeded to explain that while working smart often involves hard work, hard work is not always performed in smart fashion.

Sorta suspect they didn't quite grasp the subtlety involved. Same holds true for us dolts… Seems lots of traders seem bent on going it the hard way. They fall into the trap of believing that possessing superior intelligence, logging long hours and willfully undergoing stomach-churning rollercoaster rides on a daily basis will inevitably lead to nirvana as a trader. Were that only true a whole mess of peeps that have come and gone would have stuck and been successful. Just ain't so…

Now don't misunderstand me…I'm not advocating the flipside—the stupid and lazy approach. Plenty of peeps out there constantly searching for black boxes, gurus and short cuts, but it's counterproductive to spend time dwelling on the "fools and their money " approach.

No, working smart in trading is found in the middle ground—where your efforts are streamlined and craftily simplistic. You've a good plan in place and your time, like that of any good management team, is spent executing to plan.

So, how do you go about working smart in trading? Well, that's a bit subjective and you'll get lots of answers from peeps who've been around, but there are some key areas you should definitely ponder upon, be you a newb or someone who's been giving it a go for a while.

Lose the Preconceptions

Pretty normal to come into the biz with certain perceptions bout what trading is and entails. Most do, myself included years back. They can range from a belief that you need to know the markets inside-and-out to the vision of the successful trader as a gunslinger. Lose em. You'll never know the markets completely…nor do you need to. And the perception of the slick Wall Street trader with six guns blazing, nerves of steel and an emotionless approach to the markets…strutting round kickin booty and taking names—is bunk.

There are myriad others and you know best the ones you harbor…lose em. Trading is not what we read about in many books, nor is it what we see portrayed in movies. Done right, it's boring and methodical…much like shop-keeping. It's a business that revolves around a solid plan…and success is predicated on the ability to execute to that plan time and again for as long as you remain in the biz…period.

Leggo that Ego

A lot of peeps come into trading with inflated egos… NOOOOOoooooooo…….

Well, yes, it's true. K, nothing wrong with a little ego, but you have to check it at the door when trading. That feeling of superiority will kill ya. If you haven't figured it out yet, you're not gonna outwit the market, no matter how many marbles you got rolling round in your noggin. I don't care if you're Stephen Hawking, you're not gonna come to decisions faster than the computers that control the markets nowadays…period.

Here's the deal—if you plan to invest then use those extra marbles and get to know everything you can

about a company (good luck!), but as a trader it's not your job. Whatever you do, tis best to recognize what you're up against—trade desks, hedge funds and research teams with super computers and deep pockets that are constantly culling information in fractions of milliseconds—seeking to arbitrage what they know ahead of others. So to take the approach of becoming the expert just plays into their hands. You will keep feeding their bank and not your own if your plan is predicated on being the smartest man on the block.

Moreover, though it seems counter-intuitive, being too smart about a particular stock or market or the macro picture can be a hidden detriment. Back in the late 90s I had a friend who knew the banks—especially BofA. He did well for a long period…so much so that he got into the position of managing a good-sized sum of money in a hedge fund for other traders and friends/families… Eventually though, he fell hard and lost almost everything. All the while he was going down the tubes he bitched that the market and traders simply did not understand the real story or the locked up value of BofA. Believe me, it was painful to watch it all play out over time…and a big lesson to me and others.

Do yourself a favor and accept that trading for the individual is about getting in the way of moving money—pure and simple. Not guessing or beating the big players to the mark…nor always understanding why this or that is happening.

Now I'm not saying smart is bad…but too smart can be a real problem! Just sayin…

Specialize

Lots of peeps believe you gotta be prepared to trade many different types of markets/instruments/securities from one day to the next, due to the ever-changing nature of the market. Today it's crude futures because of the inventory numbers due out, yesterday it was options on several Semi stocks and a couple networking companies, and tomorrow is looking like currencies given the scheduled… yadayadayada…….

Wow, that just sounds…busy…and nuts. A jack of all trades simply loses money in many different markets.

Just like you can't know everything, you can't trade everything. And why would you want the brain damage? Fact is part of designing a good business plan is determining what makes sense for you in terms of the instruments you trade, as well as the focus of those instruments. If you're gonna do stocks or options, learn a handful and follow em each day—get to know their patterns and nuances. Or go with ETFs or futures on the big indices and commodities (don't start with crude, trust me on that one…), currencies via Forex, etc.

One huge mistake many traders fall into after they've gotten their feet wet is to feel they need to spread their wings and use some of the knowledge they've accumulated…test different waters, as it were. To do so they start to incorporate screening programs using the "wide-cast net" approach. They screen for all kinds of stuff daily and nightly, and then trade different strategies/markets/instruments based on whatever comes back via their screens. I've seen many peeps screen for up to 30 to 40 different setups and scenarios daily—I've seen few do so successfully. Frankly, it's way too much work and senseless to boot for most.

Keep it simple. Create a plan…then trade what fits your plan exclusively. Trading smart is not about staying busy or keeping your money at work; it's mostly about trading when you should be and doing so in areas where you've created an advantage for yourself through familiarity... period.

Lean and Hungry

When it comes to funding your deck, capitalize your account with enough to allow for what your plan calls for; but don't overdo it. You gotta learn to trade lean until you get good and comfortable and have proven your system to the point where you completely trust it. Then ramp it up and trade large…

Not something most books will tell ya, but putting a bunch of money in an account can actually create some nasty little habits and issues for you. You end up feeling you have to put the money to work, whether you can effectively do so or not. Till you really get it down and have logged some serious trade hours, trying to manage multiple trades/positions is tough. When the markets get

up and move, sh_t happens quickly and it's easy to watch two or three positions and forget about the other five trades you got on…or worse, freeze as the pucker factor takes hold and miserably stand by as your positions all jump on the Silver Bullet train to Hades.

Another major issue is that too much cushion gives you a false sense of security. While some scoff at this, I've seen it at play. A large deck makes peeps feel somewhat bullet proof. It opens them up to carelessly accepting loses and slippage. "Ah, that was a stupid trade...oh, I thought I cud catch the…big deal, I'll get it back on the next...dang, another fat finger trade…shoot, I shudda used a stop—I swear I will next time… ." I could provide myriad examples, but you surely get the picture—if you offer up free dollars to the market, it will oblige you and liberate them from your account in short order.

My suggestion is that if you have $50k to fund an account with, do so for $5k. Whatever amount you're working with (down to $5k…in which case you have to be extremely disciplined), break it up in similar fashion. Better to learn the lesson of trading lean and sweating it out…even blowing up the account. And then doing it again, again and again. You'll learn more from blowing up four $5k accounts then you will ever learn from drawing down $20k against a $50k deck. The bloke who loses four times is four times the wiser, while the guy who's lost $20k from the $50k deck is just starting to experience the pucker factor…and sure to lose more!

Trading lean focuses your trading by forcing you to be efficient and discerning in your actions. You think about every trade…and think twice again before ever pulling the trigger. You don't accidently get caught up in stupid trades. Same holds true for not using your stops or blithely accepting slippage. You either make good decisions and execute good trades more often than not, or you're done.

Really quite simple—if a good trade doesn't work, then you move forward and no harm. Good plans are predicated on this very premise. If you make lots of stupid trades, even if some work (which they will statistically), then you are headed for the door whether you know it or not.

Just like the shop-keeper, you don't want to be overly cheap, but you do have to be smart and somewhat frugal, with a sharp eye always focused on containing costs, executing to plan and maximizing margin in a balanced fashion.

Step Away

The markets are big and complicated animals, no doubt. So it's not surprising that peeps can get completely absorbed when it comes to trading. You can learn for a lifetime and still have much to learn thereafter.

Spending hours on end each day and night in front of charts, back-testing, forecasting and creating plans… only to later find yourself readjusting plans because of the unexpected…not fun. Now I'm not saying there aren't long hours and lots of learning and many charts to map… Certainly not saying jump in without knowledge.

But there is the practical aspect. You're not gonna learn it all in a day (or ever), nor will you become successful or rich in a day. But you can lose it all in a day…or burn out in a day—seen it happen; almost had it happen to me one day, as some of you might recall me mentioning a few months prior.

The reality is that you have to learn when to trade and when to step away. Fact is that most of the day, with relatively few exceptions, you shouldn't be in the market. Aside from Forex peeps, for the most part you should plan to be active mornings and afternoons leading into the close. Most other times the market is ripe for manipulation and nothing more than noise; so if you're sitting there staring at a screen, you will inevitably succumb and make stupid trades, bar none.

Just like you shouldn't have the tube on while trading, get out from in front of your computer when you shouldn't be trading…period

To balance effectiveness against burn out, set a reasonable amount of time daily to do your trading-

related work—no more than a couple hours. Use this time to do your research, study charts, review the macroeconomic picture, review news accordingly, apprize yourself of important issues or upcoming events (earnings, specific conference, etc.), attend to your P&L, etc.

And leave it at that!!!

If you don't, you will find yourself sucked in… I'm reformed, so I say this from experience. Trust me, there's no for reward or special recognition for spending countless waking hours and sleepless nights tethered to the market. Moreover, you lose something that you're supposedly working to gain—happiness and quality of life.

Bottom line, you have to approach trading like the marathon runner versus the sprinter…pace yourself. The goal is to work the least amount of time and undergo the least amount of frustration while paying the bills, obtaining goals you've set and experiencing quality of life…period!

While lots of this seems boring and common sense in nature, the fact is that the vast majority of people who attempt to trade blow out…and the vast majority of those peeps crash due to not exercising common sense and working smart versus just working hard.

Do yourself a favor…Work Smart!

Louis Horkan
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.

Print

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

In the November edition of TEI we once again feature well-known option trader and author Jeff Augen in an exclusive Traders Talk interview. We're gonna follow up with Jeff on some of his views on the global economic situation and the prospects for the markets short and longer term. He'll share his thoughts on how the world of trading is changing and how individual traders must learn to adapt or perish. Jeff will also share some more about his proprietary Augen Indicators and the Swing the Ax program.

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…



Coaches Corner: Dispelling the Myth

By Mike Curtis



Welcome to the Coaches Corner! I'm Mike Curtis and today I'd like to discuss a common myth among aspiring traders—the belief that the market is out to "GET THEM!"

Who among us hasn't felt that early on in our career? Eventually we come to realize the market doesn't know who we are…or for that matter care about taking our money. But starting out, there's no doubt it can feel like we're sporting a big bull's eye each time we enter a trade, as it seems every trade entered goes in the opposite direction hoped for.

Times like that it's hard not to get frustrated and feel as if you've developed some sort of eternal bad luck. I've actually had more than one coaching client tell me, "Oh, you want the stock to go up… well, I'll short it in my account and there's no doubt the stock will move higher!"

Having worked with many new traders who've experienced the "market is out to get em" anxiety, I've identified what I think are the two key causes underlying these feelings of insecurity:

1) Lack of a comprehensive trading plan that incorporates proven high-probability strategies that have been properly tested and vetted.

2) Hesitation due to unchecked emotions and/or fear.

Let's start by looking at this first problem. Executing high probability strategies can ensure that you don't **NEED** the market to move in a certain direction to succeed. No one can predict exactly where the market is going and when it'll do so—so avoiding trades that require a specific directional movement to be profitable will improve your results.

Learning strategies that have a higher probability of success can help you **BEAT** the market. Sometimes "bad luck" is merely the result of trying to apply a trading strategy that is inappropriate and unlikely to succeed. Remember, there are thousands of strategies out there and you need only find one or more best suited to your situation that's capable of shifting probabilities in your favor.

What's more, bad luck doesn't really exist in the market. With every trade there is someone making money and another losing money…or at least one party is foregoing opportunity. Fact is you just need to align yourself with the side that is making money. If you're trading strategies with proven success that are capable of providing even the slightest probability in your favor, you can beat the bad-luck myth. The key is adopting a system that enables you to identify market direction and provides a heads up as to when the market cycle will probably change—allowing you to trade ***with*** the market instead of ***chasing*** it.

When it comes to hesitation resulting from fear and emotions, the underlying cause is generally the same—the lack of a solid trading plan.

Traders that shoot from the hip often lack a good strategy and rarely get totally comfortable when it comes to taking on risk and pulling the trigger. When they do finally get comfortable enough to execute a trade they're generally late to the party and the real money has already been made.

Having a set plan of action in place eliminates the negative effects that fear and emotion have on the success of your trading efforts. The combination of a good plan, sufficient trading education and practical experience trading live markets will provide you with the comfort level necessary to trade with confidence in any market condition. Trading confidence is important because it enables you to apply your strategy **CORRECTLY** and to react accordingly when things change.

The axiom "Plan your trade and trade your plan" should be a guiding principle for any trader. Making decisions in the heat of the moment will almost always result in faulty judgments and bad outcomes.

Overall, you should always remain apprized of what the broad markets are doing and be aware of the current market cycle. Tools help us identify where the 'big money' is flowing. Beyond that, a good plan of action should strike a balance between position sizing, risk management and operating intellectually (rather than emotionally), allowing for tactics that are proactive rather than reactive.

Bottom line, if you're afraid of "bad luck" or feel the markets are "out to get you," step back and analyze your approach. You'll find that a good plan and disciplined approach go a long way toward eliminating bad trading habits, keeping emotions in check and alleviating fear.

Mike Curtis has been an active trader in the derivatives markets for 8 years. He has mastered the world of equity and index options along with spread trades, futures and foreign currency. He loves teaching and has personally coached over 500 individual 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. He is a husband and father of 4 young children and currently lives in Salt Lake City, Utah.

You can contact Mike at 801-717-3993 to learn more about the Traders Edge Coaching Program.

Print

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

"After subscribing to the Weekly Options Windfall website I decided to subscribe to the W.O.W. monthly advisor. Once again a good call by me.

I would recommend this highly for anyone with some extra income to invest who is not sure on how or where to invest their money.

The advice is spot on and you will make money with Preston. And he is big enough to admit when he is Wrong! (Nobody is right all the time!)

After this I got his 1% Solution Book and that opened my eyes to a lot of great information about investing in the market. Well worth the small investment for that book....especially the discussion on earnings announcements and his great advice on Investor's Business Daily, which is killer! This is great stuff!"

B.F., New Jersey

"The W.O.W. strategies have taken the stress out of trading for me. I'm finding that I make better decisions when I'm calm and really understand the trades I'm making. It's fun and interesting to be in the markets again. Now I don't spend hours and hours trying to figure out what stock I should trade. You guys have given me specific things to look for when I do research. It either fits, or it doesn't. The 'Money Press' trades are the "workhorse" trades but I'm beginning to try splits and the 'Sunrise-Demise' trades, too. The "pinning" strategy on Friday afternoons has proven to be especially successful for me.

If you are familiar with The Dog Whisperer, Cesar Milan, he always makes a big deal about getting his students, both human and canine, into a calm, submissive state of mind. Preston's strategies, along with Mike's coaching, have helped me to accomplish a calm, rational state of mind, wherein I can be successful."

S.R., North Carolina

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



Q. I am new to options trading; can you recommend a good broker?

A. TradeMonster is excellent for option trading and the type of spread trades that we focus on. OptionsXpress is also very good. I would take a look at these two services first.

Q. The Couch Slouch is an awesome strategy. What are some guidelines for choosing the strike prices for the Put spread?

A. There aren't really any defined guidelines for choosing the strike prices. We typically want to go as far out of the money as we can while still bringing in a reasonable credit.

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. Very new to Options and their language: short leg, long leg, short put and protective Put. Which ones mean buy short leg or long leg? Short put or protective put?

A. **Short leg** is to sell the equity in question to gain a premium at strike price. It is called a short because a trader is in essence selling something he does not own.

Long leg is a trader actually buying the equity.

Short put in the context of the above would mean to sell a put. **Long put** would mean to buy the put.

The protective put is to buy put options (going long) as insurance against a drop in the price of shares of the equities purchased. "Equities" is a term used to indicate "Put" and "Call" trades.

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

Print

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

SEND EMAIL