AUSTRALIAN TECHNICAL ANALYSTS ASSOCIATION

A VIEW TO THE FUTURE

NEWSLETTER No 1 Vol 2
27 th AUGUST 1990

SO YOU WANT TO BECOME A SUCCESSFUL TRADER IN THESE VOLATILE MARKETS!!

A speculator looking for large, potential moves in a market before they have become obvious to all and sundry, should embrace various elements of Technical Analysis that "flash" bells at major junctures in a market.. It is from these large, and usually quick, moves in any market that significant profits may be generated. Is this not exactly the aim of a speculator? To obtain a better than bank interest rate return on one's risk capital.

One also has to have the temperament to act in a manner inconsistent with the majority - of traders, analysts, brokers, fund managers and the populous at large. This aspect, by itself, represents a major challenge for most market participants. In fact, it may be the main stumbling block to a large number of people.

By thoroughly researching and understanding the shortcomings of the various tools (indicators) and analytical approaches (Elliott Wave, Gann, Astronomy, Fibonacci) used by traders and analysts around the world, one can then begin the quest to put together their own trading "system". Several aspects of a trading system that are often overlooked include the placement of Stop-loss levels, exit scenarios, pyramid points and money management routines. Without these vital ingredients, one is only part of the way to creating their own business plan!

Once this has been achieved, the software and data are available to "test" how their particular set of rules, or system, would have performed in the past. This still does not assess how the individual would have fared following the signals. Other software can then be used by the dedicated future trader to simulate a "real" trading environment. With this approach, one can examine how well one can adhere to their particular trading system without the benefit of hindsight.

ALL THIS - WITHOUT RISKING A CENT IN ACTUALLY TRADING THE MARKET!

Unfortunately, to the best of my knowledge, software has not been developed to address the aspect of discipline. This is a vital ingredient for anyone who is looking to become successful in any field of endeavour. At this stage, the human element in one's trading can not be entirely eliminated. However, with the advent of "expert systems" and "artificial intelligence" software, that day is drawing inexorably closer.

As you can see, the challenge is there for the taking. However, it is a matter of record that the majority of market participants do not manage to reach their goal. By recognizing this inescapable fact, one can then look to learn from the common mistakes made by this group of traders and hopefully avoid making the same ones in their own trading.

IT IS SOMETIMES EASIER SAID THAN DONE - GOOD HUNTING!

IVAN KRASTINS

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LOOKING FOR THE POTENTIALLY EXPLOSIVE MOVE.

OR

TECHNICAL REASONS FOR BEING LONG OIL BEFORE THE INVASION OF KUWAIT

MONTHLY VIEW:

As at the end of June, 1990, the Crude Oil market has been steadily trending down from its early 1990 high. *The important thing to note at this stage is that this high was actually* **HIGHER** *than the* previous rally high made in mid 1987.

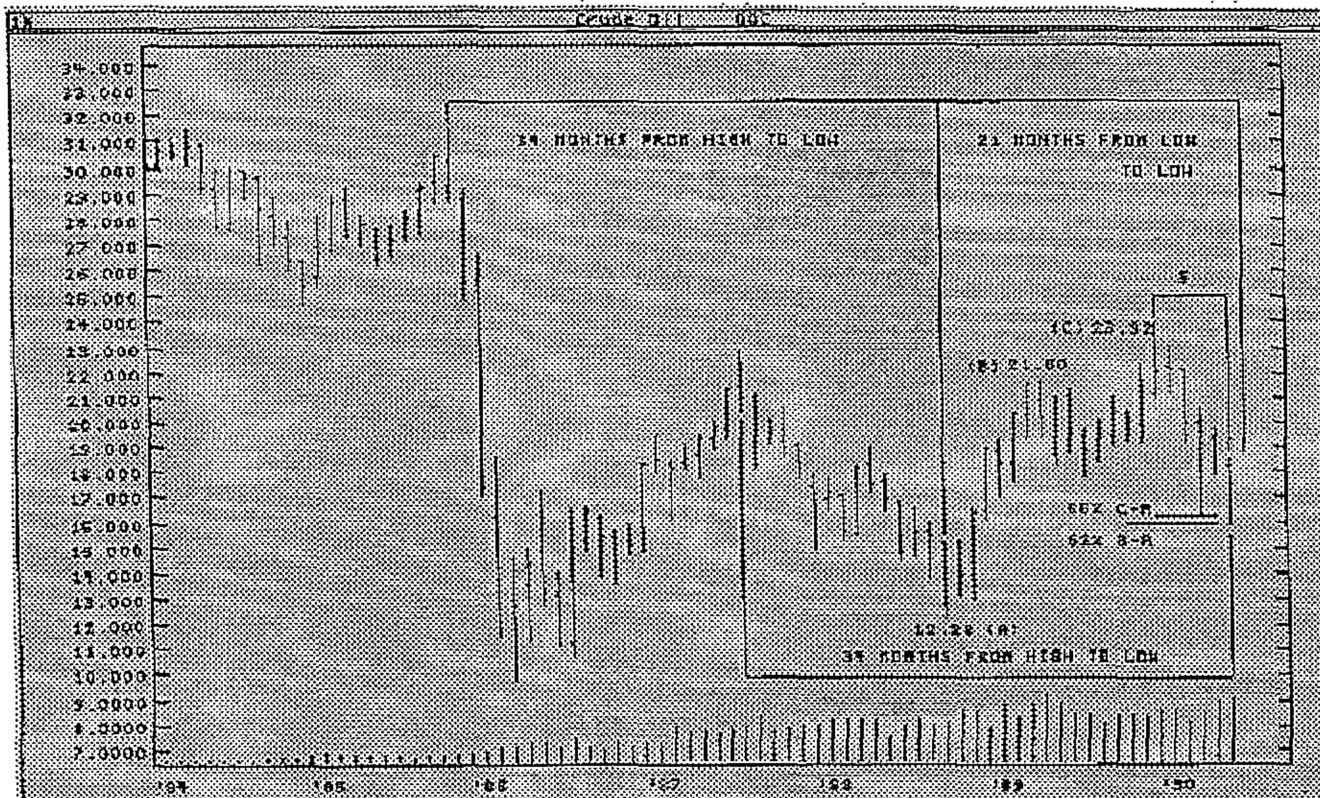
From the monthly chart below, you can see the web of Fibonacci time zone relationships that exist at the current juncture:

5 months from the recent high
34 months from the mid 1987 high

The month of July, next month, offers several more Fibonacci time zone relationships:

55 months from the high in late 1985
21 months from the low in late 1988

The confluence of these important Fibonacci time zones (taken from the previous highs and lows) for this period of June and July, 1990 are "flashing" bells!



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On the previous chart, focus on the price levels marked (A) - 12.28, (B) - 21.60 and (C) - 23.92.

If one treats the move from (A) to (B) as the main thrust up (Elliott Wave impulse move), a move of 9.32 points, then the main Fibonacci retracement of 62% comes in at 15.84.

This is **just** 0.06 points below this month's low of 15.90.

If one views the entire move up (A) to (C), then the market has gone through the 62% retracement level at 16.72.

However, another retracement level used by W.D. Gann (and to some extent by Elliott Wave practitioners) to assess where a market may react is 66.6%. This comes in at 16.16.

This other level is merely 0.26 points above this month's low.

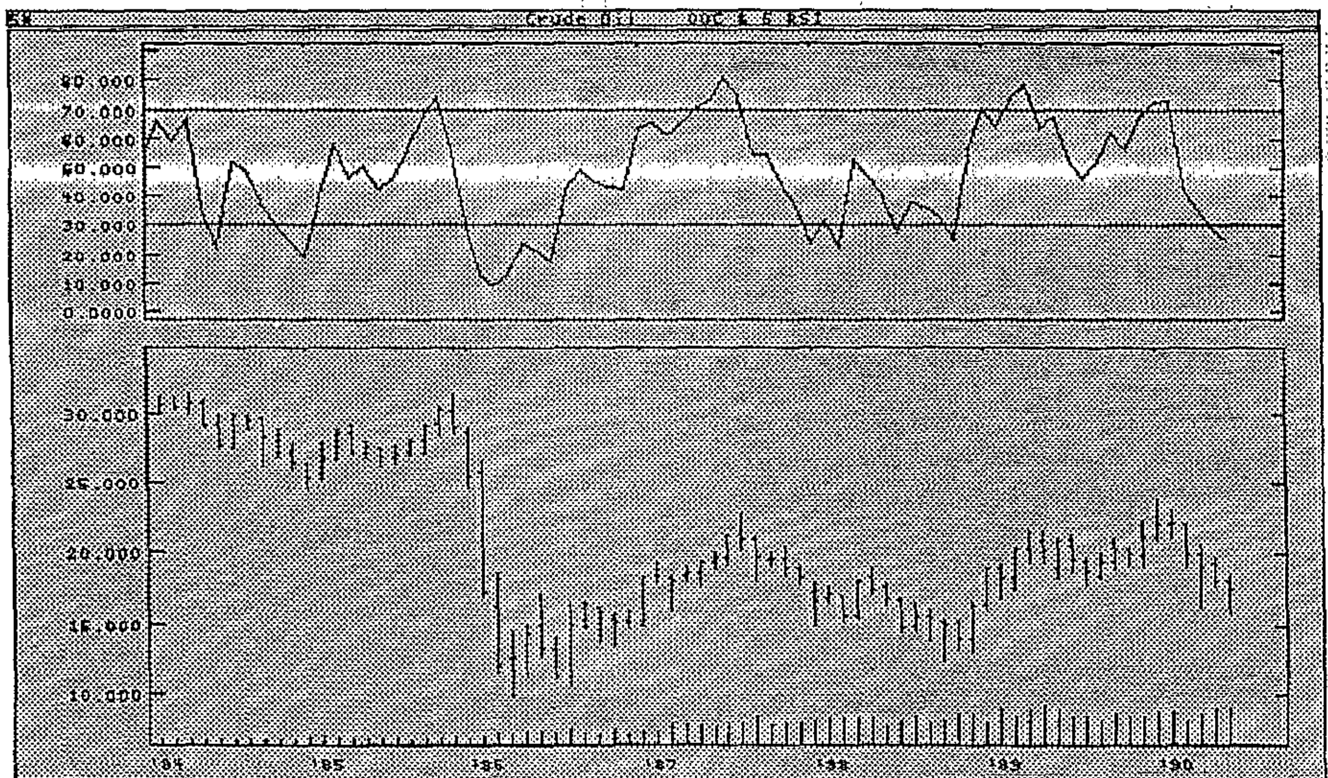
The important message here is that **the market has had trouble breaking decisively through these levels.**

INDICATORS:

Let us now take a quick glance at the Relative Strength Index (RSI). This indicator can be used to measure how "overbought" or "oversold" a market really is.

At the current time, the RSI is below 30. This confirms that the Crude Oil market, on a monthly basis, has the room (technically) to rally.

Market collapses do not begin when the market is already oversold.



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WEEKLY PICTURE:

No less an interesting picture is being presented by an inspection of a weekly chart of the prices.

In terms of Fibonacci time zones this week is:

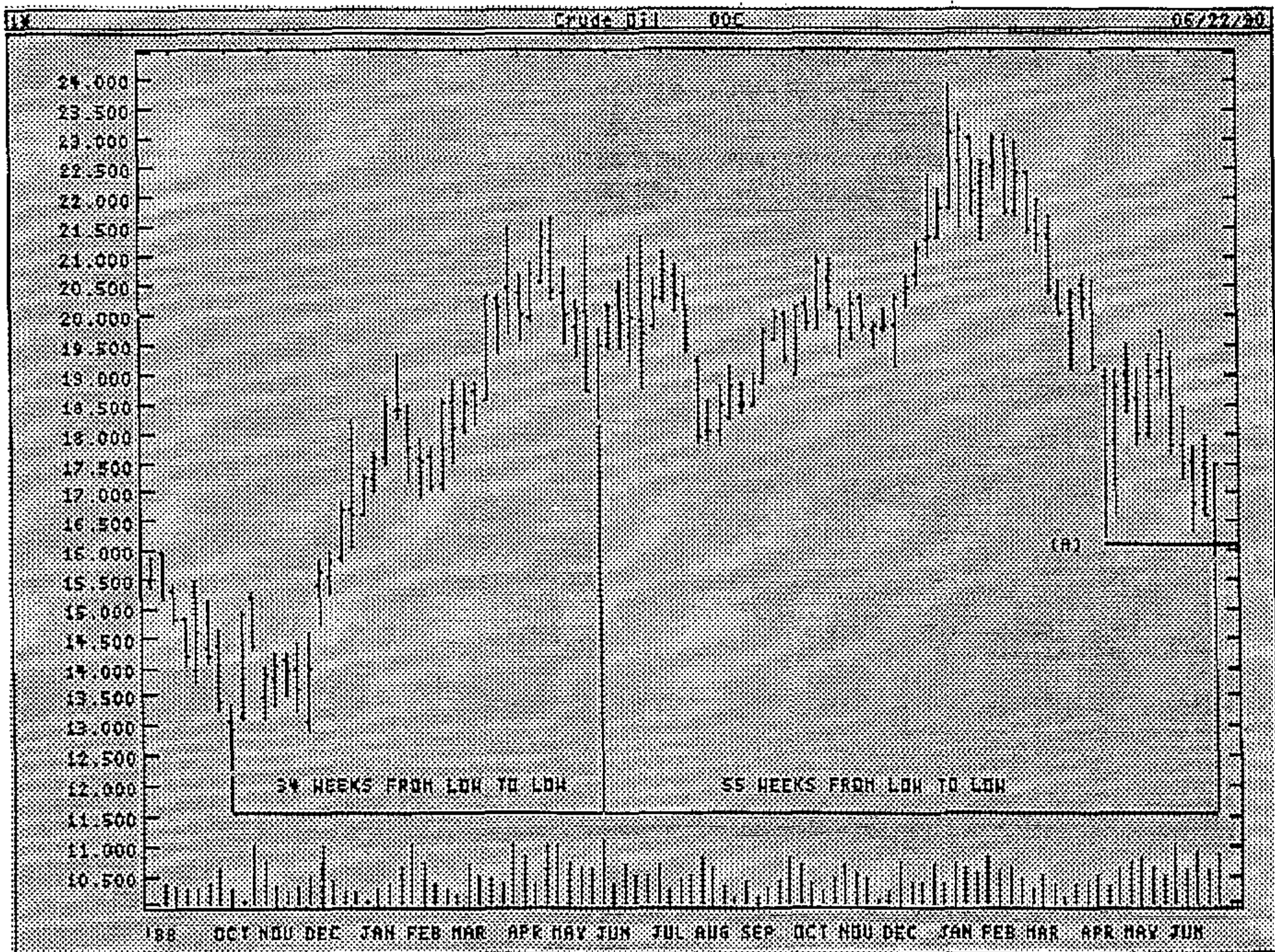
> **55** weeks from the low made in June 1989
> **89** weeks from the low that was made in October 1988

The prices this week entered the critical area noted in the monthly assessment (between 16.16 and 15.84) and **promptly reversed** to the topside - finishing **at the highs** for the week.

An extremely important piece of information has been presented by the prices penetrating the lows marked (A).

The fact that this did not induce fresh selling (and hence a further collapse in price) indicates that it was probably caused by the, by now, frustrated long position holders finally exiting the market.

They made one of **the most commonly made mistakes - placing a stop-loss just below old lows.** This is exactly the wrong place to have a stop-loss.



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INDICATORS:

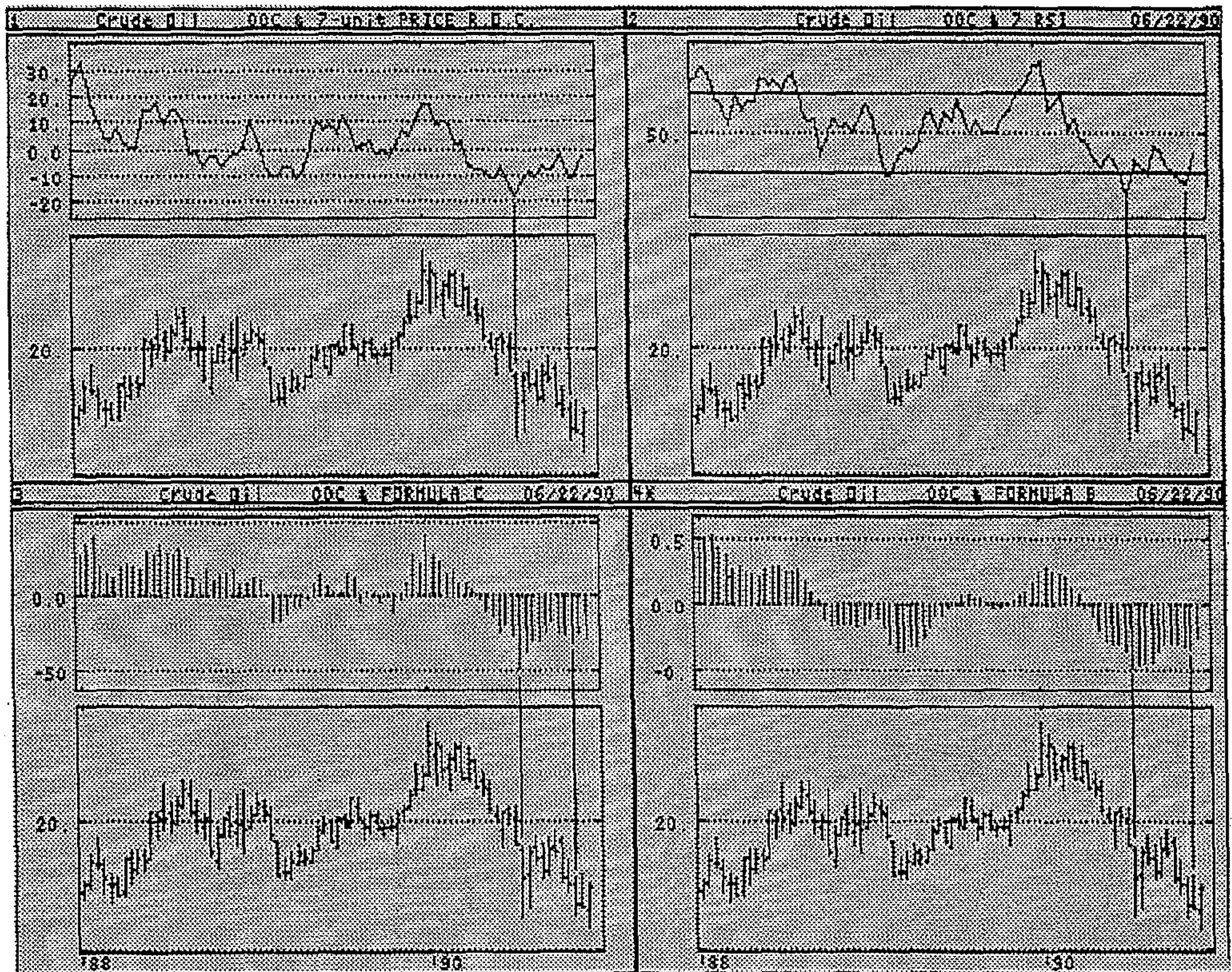
Not only are the "leading" indicators such as ROC (rate of change) oscillators, RSI's and the like in "oversold" zones on a weekly basis, but they are failing to confirm the new lows made by the prices.

A BULLISH DIVERGENCE IS PRESENT ON A WEEKLY BASIS.

Another extremely significant factor is that this bullish divergence is also present in "trend-following" indicators.

This is a more advanced way of treating (the traditionally lagging) indicators like the MACD (moving average convergence/divergence) and the DMI (directional movement index).

An experienced trader will know that it is more than just coincidence when both leading and trend-following indicators give a divergence signal on a weekly basis.



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BOTTOM LINE:

Based on a detailed examination of both the monthly and the weekly position of the Crude Oil market, the **probabilities certainly favour an upward move** in prices.

At this juncture, any estimation of how high the Crude Oil market may go, if at all, would be based on guesswork. The market itself will provide the necessary clues as the move unfolds.

When the mood becomes decidedly one-sided, and the indicators line up on a monthly and weekly basis, the time will come to look at the short side.

This market appraisal will cease to be valid if the prices break **below the lows made this week** (using "spot month" continuous data).

N.B. By using weekly and monthly chart analyses the astute trader, or speculator can isolate the larger, and hence the more potentially profitable, moves in any given market. It also means that they are not looking to "pick" the absolute top or bottom in a market!

Daily data can be analyzed to finesse an entry point, but should be done in the knowledge that, whilst the general approach is the same as with using weekly and monthly charts, a signal generated by the daily chart **must be confirmed by the weekly chart within a week,** or at most two.

Otherwise, one can find oneself involved with merely a correction, rather than a substantial "new" move. This is an especially vital concept for traders of options, rather than physicals or futures.

(Extract from a Special report produced by The Investment Educator.)

AN UPDATE ON THE OIL MARKETS:

The barrage of technical reasons to be long in the Crude Oil market **BEFORE** the "war" broke out certainly did not predict the extent of this current move.

Nor was that the desired aim. The purpose was merely to demonstrate that when Technical Analysis is applied to a market, it assesses the **probabilities of the market having a move in a certain direction.**

It can be stated with complete confidence that the probability of the Crude Oil market rising by another 100%, based on the current picture presented by Technical Analysis, is virtually nonex-

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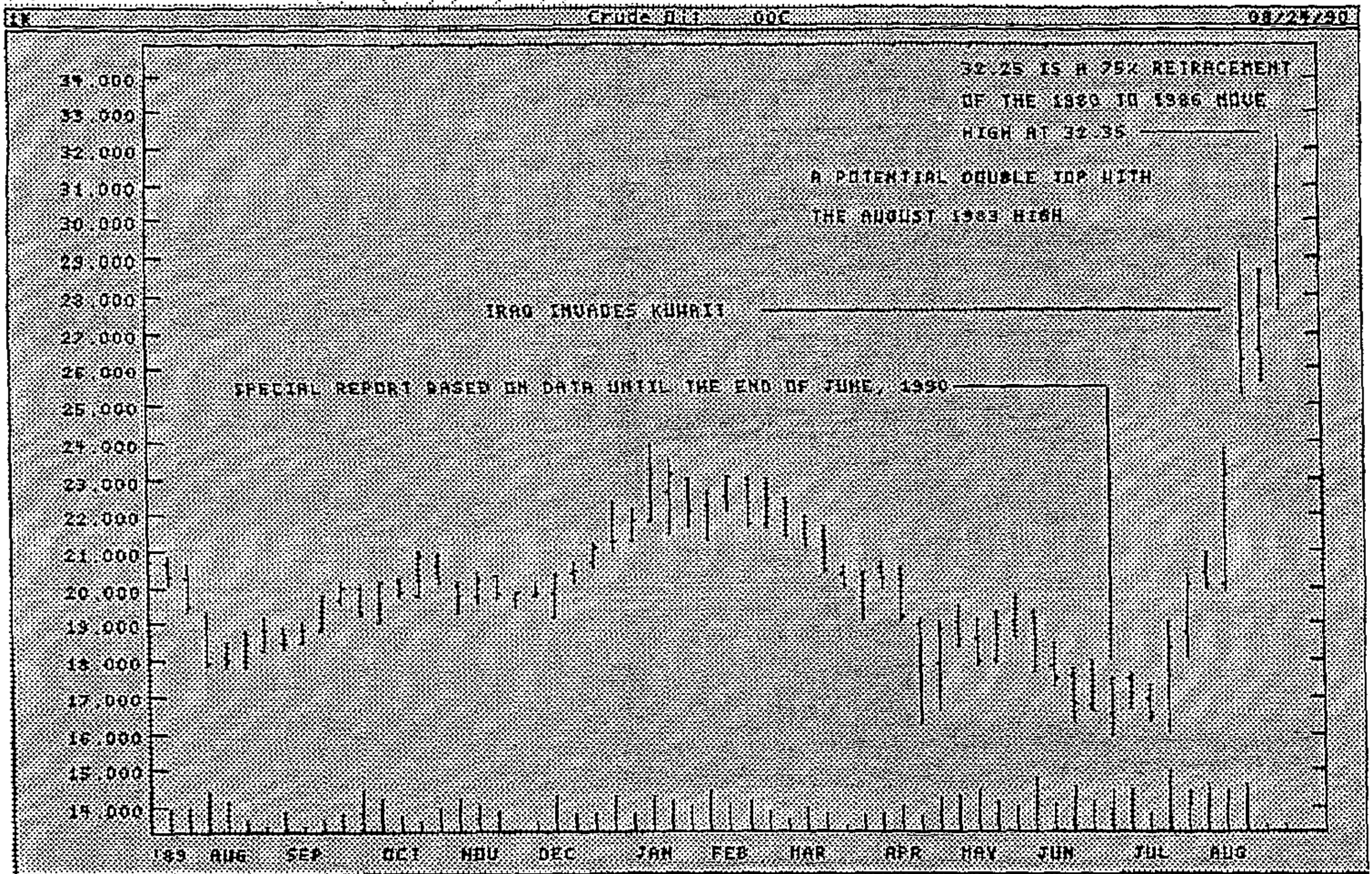
The life of a speculator is considerably easier than for those who use Technical Analysis to forecast. Unless there is an extremely strong case for a view, either way, speculators can sit on the sidelines and wait for the "textbook" opportunity.



It should be noted that the week beginning August 27, 1990 marks **34 weeks** from the January 1990 highs, and the week just ended marks **55 weeks** from the August 1989 lows. This would add weight to the proposition that the upward move in prices could be coming to an end.

The next projected weekly change-in-trend periods occur in the week beginning 17 September (**233 weeks** from the April 1986 low) and the week beginning October 22 (**377 weeks** from the August 1983 high).

November 1990, presents the first monthly change-in-trend, being **55 months** from the April 1986 low. As well as that, the week beginning November 5, 1990 will be **55 weeks** from the October 13, 1989 highs.

The technical picture of the Crude Oil market will help determine whether these projected weekly and monthly change-in-trend periods will be tops or bottoms.

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Viewing the larger picture, it should be noted that a price of 39.75 was reached in March, 1980. The subsequent lows were made at 9.75 in March, 1986. These are the parameters within which the market is currently trading.
The "war inspired" rally has already driven prices through the 62% and 66% retracement levels. Another level that was used by the legendary trader W.D. Gann is 75%. That level is at 32.25. (**Note the high that was made in this last week at 32.35.**)
Replicating the process that was used to determine the probabilities of an upward move in prices at the end of July, one should examine the same indicators that served us so well at the bottom.

WEEKLY INDICATORS:

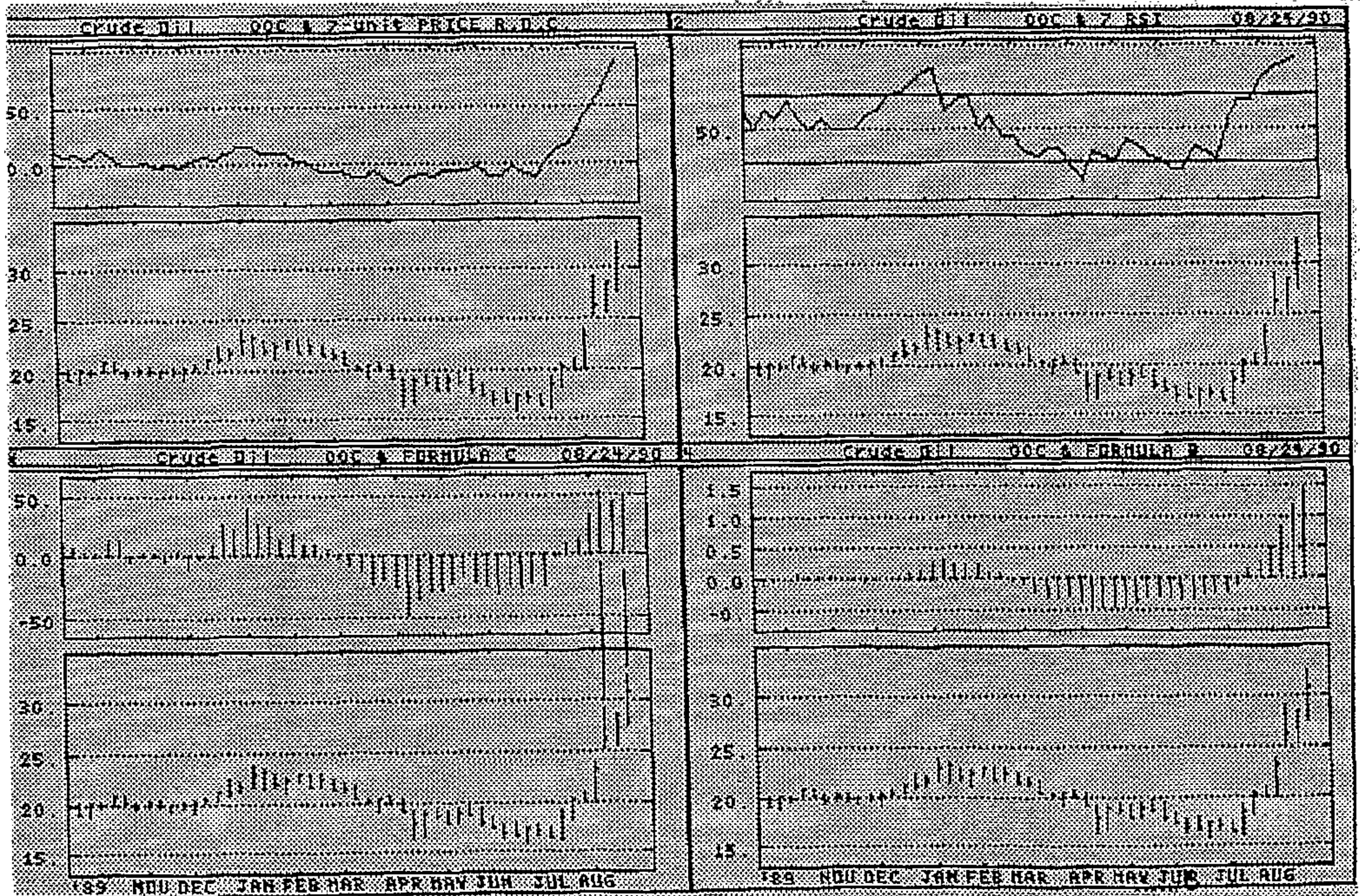
As you may suspect, **all the indicators are in overbought zones**, but all bar one are confirming the new highs. Based on this, the current position warrants stop-losses being raised to "lock-in" profits. **Any short position would be of a high risk nature.**

It should be noted that initial margin requirements in the futures markets by now have also been raised to reflect the increase in volatility in the Crude Oil market. This will have the effect of removing the lesser capitalised traders from the market.

With this in mind, and being cognisant of the fact that most traders are now bullish (and probably long), a light short position could be a real consideration.

Another, market truism to bear in mind is: "... the faster they rise, the harder they fall..." (Anon).

THE CASE FOR A TOP IS NOT AS STRONG AS THE CASE FOR THE LOW IN JUNE.



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The Special Report that you have read, as well as the Update, on the state of the Crude Oil market was greatly helped by a very unique publication now available directly in Australia.

I am referring to a two volume set of reference books called by an extremely low-key name: "The 1990 $upertrader's Almanac" written by Frank A. Taucher and published by Market Movements, Inc. U.S.A.

The Australian distributor is QBL Software Services (26 Joubert St., Hunters Hill, N.S.W. 2110 Ph. 816 1529). They also are the local agents for Technical Tools data and the highly regarded analytical software package A.M.A. - Relevance III.

I had the privilege of being exposed to this excellent publication when I was living and working in Chicago back in 1986. It is, without fear of contradiction, the most complete reference manual on the markets in the U.S.A. that I have seen anywhere in the world.

There are in excess of 700 pages filled with such vital information as projected weekly and monthly change-in-trend periods, W.D. Gann's anniversary dates of the different American futures markets to cycle and seasonal factors, astro turning points, as well as a wealth of trading tips and ideas, deposit requirements, the correct application of orders and much, more.

For anyone who is serious about trading the American markets, this annual publication deserves an inspection.

IVAN KRASTINS
THE INVESTMENT EDUCATOR

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The following articles have been kindly submitted by some of our current members

I must admit I was a little dismayed when Charles Alexiou gave me a call the other day and asked me to contribute to the newsletter. I didn't know where to start or what to say. I stumbled into Technical Analysis when our Chief Dealer decided that we should be watching the charts. Since I had no input into the morning meeting at that time I was it. Because of this I haven't any theoretical background but mainly on the job experience that I have gained since then.

Being on a corporate Foreign Exchange desk my technical analyst hat would only involve around 20% of my day. So as a result I like to keep things relatively simple and time efficient. Although we have both Teletrac and Reutergraphics in our dealing room, I find keeping manual charts more beneficial because it makes me look at all trendlines closely and allows me to mark in Fibonnaci targets, major reversal days etc. I keep charts on a daily H-L-C basis on GBP/USD, USD/DEM, USD/JPY, and AUD/USD as well as a weekly H-L-C AUD/USD chart. Elliott Wave theory is not one of my strong points, so on the charts I have mainly concentrated on looking for reversal or continuation patterns.

On these charts I tend to favour monitoring 3 main models. My favourite is the 14 event momentum model which is very useful for picking up reversals in trends or at least the likelyhood of a trendline holding. Second to that is a 21 event RSI. The main reason behind the 21 events is that on average there are 21 working days in each month, and thus a monthly factor is included in a daily chart. Whilst it is good to watch for overbought or oversold conditions, I have found watching for divergences in the RSI to be more worthwhile. A divergence combined, with a supporting momentum, has proved to be very accurate in forecasting reversals. Finally, a 8 X 13 oscillator is viewed as well to act as confirmation to both momentum and RSI.

These models have been used in conjunction with others at different times, however I have always returned to using the above mentioned strategy to obtain the best results.

Overall I consider myself to still be a novice when it comes to Technical Analysis, with most of my exposure being on the charting side of things. Through the Association I hope to develop my theory and also look at the statistical side of Technical Analysis, and look forward to meeting you all at future functions.

Mr. Mark Frost
ANZ (FX)

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THE STOPLOSS

Technicians as Market Analysts are called upon in their profession to make definitive assessments as to the direction of price. In this traders would not argue. Traders would, as would Technicians, be less eager to admit that these assessments are by nature reasoned outcomes of a quantification of subjective/objective probabilities. But nevertheless the outputs of Technicians boil down to the immediate trading alternatives of to buy, sell or do nothing.

I would argue though that the Technician has a role to play in the next, more bottom line sensitive, aspect of trading - that of money management.

Given that the initial trading decision to buy or sell is taken under conditions of risk probabilities, the profits or losses (hopefully profits) that accrue over time therefore will also be subject to risk. Here money management will impinge directly on the profitability or otherwise of a trade.

Assuming the trader has defined risk/reward tolerances (not always the case), money management tools become essential where the trader basically seeks to maximise profitable (upside) risk to a given "tolerable" level of loss (downside) risk.

Q: How is this loss risk limited?

A: The Stoploss.

As a management tool it is the linchpin of reward and risk. It should be looked upon as a loss limiter.

The stoploss has qualified support generally among traders, but is often the butt of discontent (I would argue misdirected, revealing more a bitterness towards market risk than the failure of the stoploss).

The stoploss also defines a pre-determined point at which an individual trader acknowledges the initial decision to trade was wrong or has resulted in a capital risk beyond his/her (or managements!) tolerances.

Experienced traders will recognise immediately that the dichotomy of trading and capital management decisions are interlinked, but differ in important respects.

For once a trade is opened, based on the Technical (i.e. risk) conditions of the market, the traders must immediately, in explicit or implicit fashion, lock a stoploss to the relevant trade. The first aspect of the trade exposes capital (hopefully) to upside risk.

On the other hand the stoploss limits the downside risk to capital. To ignore stoploss procedures is to acknowledge not so much a trading slackness but an irresponsibility to the capital under management and exposed.

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To illustrate the correct method, take for example an $A/USD trader:

Observe a spot market at .8000 USD with an advised Technical risk profile of 20/80 (downside to upside) risk at spot. The technician also advises that major support exists at .7960. Below which the risk profile changes to 80/20 downside to upside risk.

The trader then agrees to go long $A at spot with a stoploss at .7959 (ignoring spread considerations).

In long hand we have described a trader who on a technical basis is risking 41 points to take a perceived upside risk of 80%. The capital management decision (of 41 points maximum loss) and the trading decision to buy is taken simultaneously. The trade is self-contained - only the profit potential is left to the traders discretion.

All this is very familiar to us all but hardly touched upon in technical articles of our trade. I believe that, while not disparaging the very real contribution that technical analysis contributes to the methodologies of trading, I make the plea that traders and technicians work closer together to maximise upside potential with a minimum of loss using stoplosses.

The stoploss level then, subject to the capital risk tolerances of traders, reflects the balance point between risk and reward. Traders should then acknowledge to themselves that in trading one should not so much seek where they would be right in trades but where they would be wrong.

But of course, this has the stoploss in a passive role of closing trades - of "stop outs". Technical traders will recognise that the use of stoplosses to protect capital from downside risk can be used in reverse. Of "stop in's", where beyond a certain point the risk profile of price squews to an extent that a trader opens a position and exposes capital to an perceived tolerable upside risk.

Having said this of "stop in's" they are of consequence trading decisions, not capital protection decisions - which brings us to the end of this brief note.

In summary the role of the stoploss is crucial to the capital protection/exposure management of a trading position and should be pivotal in a trading strategy that seeks to balance reward within a tolerable level of risk.

Mr. Peter Pontikis
Corporate Technical Advisor
Westpac

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WHAT A CHORE!

The Year is 1983

At this point in time in Australia, Technical Analysis was just beginning to develop it's own place in the investment world. Many investors and traders were unaware and many more were narrow minded in their approach to Technical Analysis. However there was a movement towards utilising this form of analysis as an additional tool, but getting Treasury managers, overseers of dealing operations and other decision makers in the investment world to commit funds was another story. Technical Analysis was not a mature form of analysis in Australia in the early eighties. Sure there were the odd ones here and there who knew the benefits, and my boss at the time, was one of them. However we both suffered the frustration of being half way there and providing only half the Analysis.

Day after day, my penchant for charting would propel me into two hours of updating every morning, another hour and half after work. My life as a committed chartist working for a Melbourne stockbroker was long and arduous. Overnight markets need updating in the morning, our markets need updating after work, still trying to trade futures during the day off either a Point and Figure chart or a five minute line chart.

The interest is beginning to gain momentum, to be able to show a client a chart, to analyze it, or to have them all ready for the morning strategy meetings.

Then from the far side of the dealing room, through the vast array of screens and piles of paper on the dealing desks, the Options trader catches my eye. Oh no, he is walking towards me and I'm only half the way through my morning updates. What could he want? Surely he doesn't want charts on his Options.

The next morning I must add Options against physicals to my list of updates - only 26 of them!

The satisfaction of being able to analyze up to date charts and provide your dealing room with quality, up to date analysis is a driving force and the reward for the hours of updating every day. Then a few minutes later towards the end of the day, when gold has rallied five dollars, the U.S. Dollar has weakened off, our currency has strengthened, pushing the resource stocks down - the charts are out of date!

It's at time like these everyone wants to know which resistance levels have been broken by the A$, all of a sudden the interest is back in the gold stocks. Oh no, I haven't updated them for a week because Gold hasn't been doing anything. As I madly update, opportunities are slipping by, by the minute. I need help!

Admittedly, updating time is time out of my day. I can not speak to clients and dealers, provide strategies, or Support and Resistance levels for the dealers to watch, but then if the boss wants the charts done they will be done. He sees the value in it but can't justify an assistant to help with the updating - the big time devourer!

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WHAT A CHORE! ..2

The requirement and need for broking offices, banks and institutions to have effective coverage of all markets; commodities, currencies, fixed interest, stocks, etc, was becoming a vital part of their operations.

After much investigation, looking for a less pressured job, speaking to other chartists, and becoming somewhat disillusioned with my future as a budding chartist I came across two guys who had an investment management group. To my surprise, and a pleasant surprise it was, Technical Analysis laid a large foundation for their investment strategies. My curiosity was aroused and the questions flowed.

I soon discovered that there was a solution to the boss's problem of having all the charts updated and analyzed, and also my problem of time. Before I approached the boss with my revelation I decided to do some more investigating so I had all my facts right and I could present a case that was irrefutable. I managed to swing a trip to Sydney, I visited the companies that could possible help me with my solution, I collected and collated all the available information I could lay my hands on.

I agreed to meet the boss after work and laid the seeds of interest implying that I had something to tell him that would be to his advantage.

The meeting was a very short one. "I can solve our problem for a quarter of the cost of what we were working on before". Of course any bosses light up when reduced costs are mentioned and you immediately have their undivided attention. I placed the relevant information on his desk and explained to him that by purchasing a computer, a good software package and access to a database I could improve my efficiency and productivity 100%. It was that easy. Upon explanation of my research into the subject I had sold him. If he could have written me a cheque then he would have.

A couple of weeks later I had an IBM computer, the Computrac software package and access to a database to provide me with my data. Four hours updating time turned into five minutes in the morning and five at night. I could now walk into a morning meeting with all the overnight charts updated. I didn't just do 26 options charts any more, I did them all. I had Support and Resistance levels immediately, and the analysis, via the computer, was much more extensive, accurate, and dependable.The effect on my boss was such that he though he had employed another person - at quarter of the cost!

This was the development at that stage in the early eighties.

The year is 1990.

The progression has been so rapid that the data is transferred these days in a split second. A currency movement on the other side of the world is not only flashed up on my quote screen but it is also in my computer and ready to be analysed a couple of seconds later. Be it a currency, commodity, or debt instrument, it doesn't matter, it is all in my computer ready for any such occasion - as any Technical analyst should be.

Such is the competitiveness in today's financial markets that to be out of step with this technology is to give your opposition a competitive advantage. The receptiveness of this form of Analysis is accepted as the norm in alot of dealing rooms and by alot of individual traders these days, however much of the work still has to be done educating people as to the benefits of the computerised Technical Analyst.

By the way my updating time is now nill!

Mr. Richard Lee
TELERATE

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I am currently in the process of compiling a "road-test" on a fairly new (at least directly in Australia) analytical software package called: Relevance III, authored by R. Maynard Holt. This should be ready for the next issue of the ATAA newsletter.

It would be great to hear from any current users of this package. This will enable some of our members to share their thoughts and experiences with others in the group.

Please, don't be shy!! Call me on (02) 922 4991 or fax me direct on (02) 925 0090.

I would like to personally thank Mr. Mark Frost of the ANZ Bank (FX) Mr. Richard Lee (TELERATE) and Mr. Peter Pontikis of Westpac (Corporate Technical Advisor) for their contributions to this ATAA newsletter. A great effort!

Where are the other members? You don't need to be a experienced analyst or trader - you may be just looking at using Technical Analysis.

You may be hunting down a particular book, software package, data or a course. This is your organisation - make the most of it!!

IVAN KRASTINS
EDITOR

STEVEN MUTCH
PRODUCTION TECH

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